END-TO-END LIFECYCLE MANAGEMENT

Think holistically, enable digitally, manage with clarity
Introduction

Many of today’s supplier and third party interactions are purely tactical and leave little space for true insights through integration. Truly effective end-to-end lifecycle management leads to a holistic value-based relationship between suppliers and buyers where one does not gain advantage at the expense of the other.

To create this type of partnership, operation models enabled through technology that support third-party centricity stances need to be adopted, while fostering innovation and mitigating risk.
Organisations need to be asking themselves:

Are your suppliers in tune with your business objectives? And are you getting what you negotiated and paid for?

Have all the risks been mitigated and how do you stay on top of them?

How are you balancing managing existing providers and fostering new entrants to develop and grow sustainable outcomes for both parties?

Answering these critical questions requires analytics and data which offer a means for measuring performance, identifying opportunities, mitigating risks and helping move the organisation from being reactive to one that is proactively engaged with both the business and its suppliers and third parties.

Within this article, we will cover off three critical dimensions of Contract management, Supplier Risk (Includes third parties) and Relationship management. All three are key in obtaining a holistic view across your extended value chain.
Remediating or replacing supplier arrangements due to non-delivery of the targeted outcomes is a key consideration for many organisations. Often a large amount of work has been put into upfront pre-signature activity such as contract formation where obligations and their associated performance indicators and service credits are determined. Then when reviewing post-signature activity there are many occasions where much of the intended value of the contract had been lost through value leakage or forgotten through inadequate obligation management.

Those in contract or supplier management roles frequently feel they are shackled to low value and manual activity due to lack of automation in the processes they are managing. There is a need for automation across the key pillars – performance management, contract management, financial management and risk management.

There are a number of strategies that can be put in place to deliver more sustainable supplier relationships and value.
Often the success of a client/supplier relationship can be traced back to the foundations they are built upon. In the context of contract management this is the work that’s done in the pre-signature period.

The most successful partnerships have three distinctive elements.

**Balanced Contracts** – standard contracts that balance risk across each of the parties and are focussed on the project outcomes.

**Relationship Focussed** – an engagement and service delivery model based on trust and empowers the supplier as opposed to a high governance transactional model.

**Sustainable Negotiation Outcomes** – setting the negotiation team up to negotiate for value, with a focus on delivering a sustainable model for both parties.

Many contracts fail to deliver true potential value as much of supplier management time is devoted to low value data management and reporting. Valuable time can be freed up by automating data management, reporting compliance and basic risk management activity. There are many software platforms across the contract lifecycle management (CLM) landscape that have high levels of embedded automation.
Value leakage in contractual agreements is a recurring problem with contract management. The loss of value can be attributed to:

- over-payment
- un-checked consumption
- unclaimed credits and discounts
- scope creep
- loss of focus on improvement and innovation
- unclear accountabilities
- no holistic view of supplier performance
- transactional relationships.

Leakage can be fixed through a combination of process, governance and technology with the benefits proving to be well worth the investment of time and effort in proper controls throughout the process.

There can be an overabundance of KPIs created within a contract that are in complete misalignment to the targeted outcomes an organisation might be seeking. The key to a successful supplier partnership is to manage outcomes which are aligned to the strategic direction and service philosophy of the organisation. The most efficient and accurate reporting is that which has the least amount of human intervention. Reporting should be automated within a contract performance management system.

Risk is present in all business decisions that are made but embedding risk within the day-to-day operations of contract management will ensure the potential impacts can be better accounted for.

Risk controls should be built in through holistic risk management categories that cover all areas of supplier risk including ownership, geography and capacity, to name a few. Risk currency will ensure that risk visibility is kept current through ongoing assessment while a clear ownership of risk related activities should be established, and finally leverage automation for risk related activities.

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Third party/supplier risk management

Balancing out the value equation

Organisations are increasingly reliant on third-party suppliers to deliver business-critical products and services to customers. Some organisations are finding that failures by third parties can significantly impact their ability to operate effectively and tarnish their societal trust and reputation. Both of which have significant downstream operational delivery, quality and cost implications and potentially upstream growth impacts.

While value and risk have been openly discussed as part of the procurement agenda, the global pandemic highlighted that more needs to be done given our connected global supply chains. Organisations are beginning to address the concerns around these issues, but it’s evident they need a clear strategy for the selection, approval and management of third-party suppliers. As there are a myriad of stakeholders involved, from the business as well as the procurement and risk functions, developing and implementing this strategy continues to be challenging.

Supplier risk became a key emerging focus for organisations through the pandemic, although it is only one element of end-to-end supplier lifecycle management, the other two being contract management and supplier relationship management – without all three lenses, you or your organisation does not have a holistic view across your entire supply base be they material, moderate or those found in the tail. The aggregation of your entire supplier eco-system creates the goods or services you provide to your customer.

Through extensive work with organisations across the world KPMG has identified a number of key challenges that exist across third party and supplier risk management. These range from supplier concentration through to ongoing management and governance.

• **Supplier Concentration Risk:** Across all sectors there has been an increase in supplier concentration which raises dependency and competition concerns. The move towards digital transformation and cloud implementation has accelerated this risk and will continue to do so.

• **Third Party Governance:** Increased regulatory focus, and the financial and reputational impacts of getting it wrong, has required organisations to have better third-party risk management processes in place, given documentation and accountabilities invariably continue to be insufficient and unclear.

• **Supplier Risk Assessments:** Often these assessments are performed in siloes and on a reactionary basis, with limited depth and a lack of subject matter expert input. This often results in the insights from the risk assessments not being rigorous enough to be used to inform sourcing strategies and future decision making.

• **Third Party Supplier Management:** Generally there is a lack in capacity and capability to be an effective process with limited engagement with subject matter experts to support effective supplier oversight.
COVID-19 Impacts: The pandemic has amplified the impacts of third party and supply chain disruption and challenged organisation’s ability to plan and execute key third-party risk management components. Some specific examples from a COVID-19 perspective include:

- business continuity and resiliency risk;
- IT and Cyber Risk;
- key person risk;
- inadequate service provider monitoring; and
- fourth party risks.

Consider this further by examining each critical element that creates overall supplier risk. There are several categories which are often not addressed from an accountability perspective. Some reside within the procurement function, while others sit within risk management teams, the wider business or at times aren’t addressed at all.

This graph often raises questions around how these elements work together. Too often risk assessments are not conducted until after post-contract award, making it challenging to get a supplier to agree. Equally, when risk assessments are conducted post award it could become apparent that a newly appointed vendor is unsuitable and has several red flags that could impact operations, reputation or a trust agenda – assuming the question has been asked. Risk assessments need to be integrated earlier in the category planning and sourcing process, coupled with continuous monitoring (more on this below), to enhance effectiveness.

However, just performing a risk assessment is not enough, organisations need to enable continuous monitoring to ensure that a supplier is complying with their stated obligations to mitigate identified risks in an agreed upon, adequate way. It’s imperative to ensure that the assessment and resulting outcomes are effective – risk and its management needs a considered approach.
KPMG’s 2020 Third-Party Risk Management1 survey spoke to 1100 global executives to understand their challenges. The outcome was distilled into five key themes.

Third Party Risk Management (TPRM) is a strategic priority. More than three out of four respondents to our survey (77 per cent) say TPRM is a strategic priority for their business. Additionally, six out of 10 respondents say their organisation’s most severe reputational risks come from third parties’ failure to deliver. These responses highlight how dependent most businesses are on third parties to deliver critical products and services to their clients and customers. At the same time, growing regulatory pressure – particularly in relation to privacy breaches and the loss of customer data, or to operational resilience – is putting third-party relationships under additional scrutiny.

Six out of 10 (59 per cent) respondents stated that their organisations had recently been subject to sanctions and regulatory findings in relation to TPRM.

Organisation are inconsistent in their approach. Businesses work with a wide variety of third parties worldwide, and each third party manages a subset of risks on the business’ behalf. For good reason, businesses need to understand each third party’s ability to manage risks in line with expectations before deciding whether to engage that third party. Worryingly our research suggests that many organisations are not prepared for the complexity that comes with assessing multiple risks in a cohesive manner across business lines and regions. Holistic risk identification and assessment upfront in the onboarding process, as well as during the lifecycle of the contract, is crucial for organisations to have line of sight into the risk profile of their entire third-party portfolio. Three-quarters (74 per cent) of respondents admit that their organisations urgently need to make TPRM more consistent across the entire enterprise.

A risk-based approach is the number one ‘get right’ for TPRM programs. Managing third-party risk in today’s business environment is far from straightforward, and the scope of the program, along with the amount of coordination involved, can feel overwhelming. A situation not helped by limitations in resources and budget. Half of the businesses that responded do not have the required capabilities in-house to manage all of their third-party risks. We believe organisations can achieve both efficiency and effectiveness by taking a risk-based approach to assessing and monitoring third-party products and services that present the highest risk to the organisation.

Data and technology are improving TPRM teams’ performance. Across industries and regions, respondents indicated that the sheer volume of third-party assessment activities has increased in recent years. In the beginning TPRM programs simply increased headcount to complete a greater number of risk assessments. Today, organisations have the potential to innovate their approach in three areas:

- greater automation of the TPRM process internal workflow;
- leveraging shared utility providers for due diligence questionnaires and responses; and
- moving away from point-in-time risk assessments to continuous controls monitoring.

Globally, only around a quarter of businesses are using technologies to improve either workflow automation or monitoring of third parties. Technology is, however, the most favoured investment (61 per cent) that respondents make when additional funding is made available to them.

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1 Third Party Risk Management outlook 2020

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It’s time to sustainably scale the program. Organisations are integrating, streamlining and maturing their TPRM/Supply Risk programs to better understand the risk of goods and service disruptions resulting from third-party non-performance. Further, organisations are expanding risk identification, assessment and management to material and lower level suppliers. Many organisations have room for improvement across their entire operating model, inclusive of service delivery model, process, people, governance, data and technology. With that in mind, our analysis has helped us refine the steps that organisations should take to upgrade their TPRM programs. Many organisations are approaching the journey towards best-in-class differently, however given the sensitivities most are focusing on starting the journey slowly before speeding up. This is a challenge that won’t resolve itself, organisations need to start somewhere in managing the risk.

Our local and global research confirms that organisations are considering TPRM, including supplier management, to be a strategic priority. We see businesses being led by procurement, and risk functions taking a proactive approach to TPRM/supplier risk, exploring how to refine and expand existing processes, and streamlining through technology enablement and innovation as part of their end-to-end supplier lifecycle programs.

As organisations adjust to global events and economic uncertainty, historical third-party assessment information and control environment analysis needs to be updated to account for new risks and challenges. As a matter of urgency, organisations should improve business resilience across critical customer/client services by accurately understanding the role third parties play in delivering these services and adjusting policies, controls and mitigation plans accordingly.
Supplier relationship management – the business-critical dimension

Prior to COVID-19, much attention was placed on developing win-win relationships with strategic suppliers that focus on value of spend and business critically. Now organisations have to devote more management attention to critical suppliers in the growth stage.

Many organisations are experiencing disruptions in the reliable supply of key products and services due to the impacts of COVID-19 and must act to also strengthen relationships with a new cohort of suppliers to protect business continuity. This group of critical suppliers is also likely to contain a number of strategic partners of the future assuming that spend grows sufficiently for them to move to maturity. We have seen a number of organisations struggle to lock in such supply when current spend levels with these critical suppliers may only be moderate, significantly constraining the market power and attractiveness of the buyer. There are ways however that technology and other approaches can help organisations influence the sentiment of these suppliers and raise their standing as a buyer of choice.

Most mature procurement teams segment their organisation’s supply base, often based on spend value and business criticality of the products and services being procured. Underpinning this analysis is the need to adequately consider supply risk. We have identified 10 domains for third party risk that should form part of this calculation as shown below:

Third party risk domains:
In many cases, where a comprehensive supply risk assessment is in place, this will not have been updated to reflect the new reality of a pandemic affected world. COVID-19 has not only amplified the impacts of third party and supply chain disruptions but also challenged the ability of global organisations to plan and execute key third-party risk management components such as onsite assessments. Some domains facing a heightened supply risk level from a COVID-19 perspective include:

- business continuity and resiliency risk;
- IT and Cyber Risk;
- key person risk;
- inadequate service provider monitoring; and
- fourth party risks.
Organisations must overlay the changed supply risk considerations across the supplier segmentation matrix and consider which business critical suppliers are under threat, from which risks and what is proactively being done to address this situation?

Where the supply of critical products or services is at risk, buyers must work closely with suppliers to secure prioritised deliveries or establish alternative sources of supply. The inherent challenge here is that alternative suppliers may either not exist or be unsuitable or that the balance of power lies away from the buyers when spend levels are low. Specific relationship strategies and actions aimed at improving supplier sentiment should be enacted. Organisations should consider:

1. **Standardise requirements**: Align with the suppliers preferred specifications to reduce inconvenience and cost of the buyer’s business.

2. **Maximising possible spend**: Aggregate requirements and channel additional spend to critical suppliers to enhance the size of the buyer’s account to increase attractiveness. This is particularly important for suppliers identified as potentially being future strategic partners where spend is forecast to grow materially.

3. **Commit to forward demand**: Invest in quantifying the forward demand profile for the supplier’s product/service and share this information to give more certainty. As a step beyond this, consider pre-purchasing, or paying a deposit for forward deliveries.

4. **Map and eliminate relationship pain points**: Reduce the friction of doing business – consider trying to streamline supply processes, avoid repeated requests for similar information, pay on time, invest in technology such as supplier self-service portals and electronic invoicing capabilities.

5. **Consider direct control of freight and logistics**: Enter into direct arrangements particularly where products are being transported by air and the buyer is far away from the critical supplier or the supplier is not shipping products to other organisations near to the buyer. This helps to provide some surety in a restricted freight environment that the products can be delivered.

6. **Broaden the agenda**: Show active research and interest into the suppliers’ business to identify further collaboration activities, potentially unconnected to the specific supply agreements.
7. **Aid with marketing:** Offer to feature in marketing materials produced by the supplier through offering your logo, or a positive testimonial.

8. **Conduct regular engagement:** Invest in the relationship through a regular cycle of direct engagement at the management level. This may involve a commitment to conduct joint future planning, supply resilience and performance meetings every six to nine months.

9. **Build personal connections:** The likely lack of face-to-face contact for the past 12 months or more means that greater focus should be applied to engage suppliers through Teams/Zoom meetings to facilitate personal connections.

To stand most chance of success, these specific actions to boost the attractiveness of the buyer to business-critical suppliers should be laid on top of the six bedrock foundations of good supplier relationship management:

1. **Executive sponsorship:** Senior leadership in the buying organisation actively supports supplier relationship management and appreciates the value and security of supply benefits this process can deliver.

2. **Proactive strategy:** A thoughtful, proactive and resourced supplier relationship management strategy is in place to ensure that the solutioning and approach are aligned to organisational needs.

3. **Organisational structure:** A well-defined and resourced organisational structure that describes roles, responsibilities and interactions explicitly among the sourcing, Supplier Relationship Management and business partners, with minimal overlap.

4. **Structured framework:** A suite of procedures, guidelines, tools and templates are available to help structure engagement with strategic and critical suppliers. This framework is aimed at increasing levels of mutual collaboration, performance and benefits realisation for buyers and target suppliers.

5. **Technology enablement and data visibility:** Deployment and full use of contemporary contract management and supplier management technology solutions to smooth the interactions between buyer and suppliers, manage mutual obligations, provide accurate and visible data on the business being transacted and report on performance outcomes.

6. **Culture of trust:** A culture of trust is key to unlock the potential of internal resources and external suppliers alike. Organisations with leading supplier relationship management programs effectively extend a culture of trust from their internal organisation to their supply base to the point where it’s difficult to differentiate between organisational and supplier resources. All are working in a unified manner for one common goal.
The changed operating environment given the global pandemic has highlighted the interconnect ecosystem in which we operate and demands new supplier relationship strategies, particularly for perhaps previously overlooked lower spend, but business critical suppliers and third parties that have not been treated as strategic in the past. Failure to do so increases the risks of lack of supply and the consequential interruption to business continuity and your organisations trust agenda. We recommend some specific mechanisms by which this situation may be avoided to compliment more traditional approaches to supplier relationship management. These activities must be implemented in a genuine and consistent manner to maximise the value from these critical relationships in a way that builds trust.

The first step is to re-assess your end to end value chain, across suppliers and third parties to determine the risk, this will determine relationship strategies needed to ensure continued supply from critical suppliers.

In closing, end-2-end lifecycle management is now more than ever a critical business activity, it is the holistic view across your extended value chain incorporating Contract Management, Supplier Risk (or third party) Management and Relationship Management. All three work together throughout the lifecycle connected through an integrated operating model, underpinned and enabled through robust data and systems with the purpose of adding value, mitigating risk and protecting your organisations trust agenda.

To find out more about Agile Procurement Management using leading practice with KPMG Powered Procurement head to the links below.

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Third Party Risk Management Outlook 2020
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