

# Controlling Tail Spend

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The New Front in  
Optimising Procurement



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## INTRODUCTION

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The term 'strategic sourcing' has become something of a mantra in purchasing and supply chain management, but behind the rhetoric lies a simple principle that the procurement function should support organisational competitiveness. In practice this can include anything from realising savings through aggregating demand to tapping into the expertise of suppliers when developing new products and service offerings. While emphasis on the core purchasing categories that have the potential to make a strategic impact is to be expected, care should be taken not to neglect the spot buys, one-off purchases and maverick spending that are to be found in nearly every organisation. Individually these sundry purchases may seem inconsequential from a financial perspective. Yet, if firms took the time to analyse their total off-contract spend they may quickly come to form a different impression. Off-contract spend, or tail spend as it is known throughout industry, accounts for approximately 20% of total procurement expenditure in the average firm. Reliable estimates suggest that anywhere up to 20% of tail spend is waste.<sup>1</sup> To put this in monetary terms, a firm with a total procurement budget of €10 million is possibly losing in the region of €400,000 through inefficient tail spend purchasing. No wonder tail spend is becoming the new front in

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<sup>1</sup> Accenture (2013) Stop Chasing the Tail.  
Available at: [http://www.accenture.com/SiteCollectionDocuments/microsites/supply-watch/13-0205U\\_StopChasingTail\\_PoV\\_LoRes.pdf](http://www.accenture.com/SiteCollectionDocuments/microsites/supply-watch/13-0205U_StopChasingTail_PoV_LoRes.pdf)

reducing costs and streamlining the procurement function.

## **WHAT IS TAIL SPEND?**

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Tail spend comes in many forms. It includes low price, low volume items that fall outside the main spend categories, purchases made directly from high street retailers, unauthorised expenditure, and high-end technical items made by non-purchasing officers. In some cases there is a reasonable explanation for tail spend items, such as immediate need for a particular component or the fact that a product is not available from any current supplier. In other cases tail spend is of a more maverick kind and involve employees purchasing items which have not been sanctioned by the purchasing department or other senior management. Either way poorly controlled tail spend results in higher procurement costs for the firm and undermines accountability and corporate governance. In most cases tail spend is carried out by employees outside the procurement function who have neither the time, the expertise nor the incentive to research the marketplace and secure the best deal – a surgeon buying straight from a medical device company without consulting their purchasing department, for example. Left unchecked, random purchasing can erode the competitiveness of any firm's cost base.

## **COSTS ASSOCIATED WITH TAIL SPEND**

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There are various costs, financial and non-financial, associated with poor management of tail spend. Most obviously, the ad hoc nature of tail spend invariably means that organisations end up paying a higher price for goods and services than should be the case. The price charged for one-off purchases will likely be higher than a price agreed under a managed contract. For example, the cost of one-off stationery purchases versus the cost of buying from a managed contract or from a framework agreement. A high volume of individual purchases also means that opportunities to aggregate spend and exploit economies of scale are also lost. To put the problem of unmanaged tail spend in perspective, research has shown that the bottom performing quartile of firms in terms of maverick spending spent \$10,000 more per full-time procurement employee than the top performing quartile. Hence, unregulated expenditure leads to higher variable costs and a corresponding diminution in competitiveness.<sup>2</sup>

It is not only in higher item price that tail spend can have a negative impact. More individual purchases from a large number of suppliers creates more paperwork and invoice handling. This has a direct labour cost in terms of additional administrative hours spent processing purchases. It also has an opportunity cost, as the time spent dealing

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<sup>2</sup> APQC is the international resource for benchmarks and best practices.

with invoices and associated tasks could be more productively used in other areas of procurement, such as supplier engagement and researching trends in the marketplace. A lack of controls over tail spend can also undermine corporate governance and financial probity, and transparency suffers if there is little or no record over what the organisation is spending its procurement budget on.

## **CHALLENGES IN ADDRESSING TAIL SPEND**

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If poorly managed tail spend affects competitiveness, why are organisations slow to act on it? There are several points worth considering here. Firstly, the relatively low amounts associated with one-off buys and spot purchases are unlikely of themselves to generate impetus for reform. It is only when tail spend is viewed in the aggregate that stakeholders are likely to sit up and take notice. Secondly, by its very nature tail spend falls under the radar of financial planning and inventory management systems. In the absence of reliable data it becomes difficult to quantify unmanaged spend or the potential savings from moving all purchasing requirements onto managed contracts. Thirdly, the absence of robust control systems mean that some firms, in spite of having clear guidelines of how purchasing is to be carried out, are not able to monitor the implementation of such guidelines. With no monitoring and policing, unregulated spend can go unchecked. Fourthly, in large organisations

there may be a lack of co-ordination between the central purchasing unit and the various departments and functions. Without such co-ordination there is always a chance that some employees will adopt a laissez-faire attitude over what they buy and from whom. Fifthly, the age-old problem of resistance to change may act to disrupt any attempt to overhaul procurement procedures. So even if firms are broadly aware of a less than satisfactory tail spend system, there are several related factors that can make changing the status quo difficult.

## MANAGING TAIL SPEND

Difficult though it may be, organisations simply cannot ignore the competitive imperative to better manage their tail spend. While this process will vary across organisations and sectors, there are steps that should be common to all (Fig. 1).<sup>3</sup> Fig. 1 Managing Tail Spend



<sup>3</sup> InforSys BPO (2013) Available at: <http://www.infosysbpo.com/offerings/functions/sourcing-procurement-outsourcing/white-papers/documents/long-short-managing-tail-spend.pdf>

To begin with firms need to conduct a comprehensive spend analysis and retrieve all available data on what products and services are being bought. This requires bringing all parties and departments with some involvement in purchasing together to collate records and statements covering all purchasing activity. The second step is to analyse the retrieved data, define what constitutes tail spend, separate it out from managed category spend, and estimate its value in terms of total procurement expenditure. Having isolated tail spend, the third step is to classify it into spot buying, fragmented spend, one-off purchases, and maverick spending as each of these will pose different challenges are will require different solutions. The fourth step involves moving from classification of tail spend to identifying ways in which it can be managed more effectively. Questions such as, 'can we incorporate fragmented spend into existing managed contracts?', and 'what action can be taken to eliminate maverick spending?' are relevant here. Completion of the fourth step leads to devising specific tactics for better managing tail spend. It also requires the organisation to quantify potential savings from implementing their new purchasing strategy and developing metrics against which the new arrangements can be assessed. The sixth and final step is to create awareness throughout the organisation of the new procurement arrangements, justify the case for change, and support staff in changing their behaviour. Importantly, managing tail spend is not a once-off event. To be successful organisations must look to measure performance against pre-defined metrics such as direct cost savings, compliance levels, and transaction costs on an on-going basis. The key to effective management of tail spend is learning from experience and building on gains already made.



## **BENEFITS OF CONTROLLING TAIL SPEND**

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An overhaul of tail spend can yield tangible and intangible benefits for all firms, even those with relatively small procurement budgets. Cash savings are realisable if more expenditure is brought under managed contracts or is based on competitive bidding from interested suppliers. Greater awareness of what is being bought and by who also allows the purchasing manager or purchasing unit to identify where savings can be made. Having a data trail, particularly an electronic data trail, improves transparency and auditability. Thus, the incentive in managing tail spend is not only a financial one but a governance one. Making the procurement function leaner contributes to a leaner organisation overall and cuts down on administrative hours. The internal functioning of the firm is strengthened to the extent that procurement is lean, automated and integrated with other activities. A more efficient procurement system even stands to generate goodwill and attractive payment conditions for the organisation on account of more satisfied and engaged suppliers.

## **TAIL SPEND & E-PROCUREMENT**

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Fortunately for the average firm, getting to grips with tail spend has become much easier with the advent of e-procurement. e-Procurement

enables firms to take control of all purchasing, whether strategic or ancillary, by using a common web-based platform through which to interact with the supply marketplace. By using hosted e-procurement platforms the level of compliance with company procedures increases, the time spent processing invoices decreases, and openness and transparency are greatly enhanced. While no one would suggest that e-procurement software services are a silver bullet for supply chain management, they are a proven way to reduce tail spend costs. Nearly all aspects of business management have improved from the application of web based technologies. The procurement of goods and services is no exception, and organisations should be more proactive in availing of its functionality for the management of tail spend.

## CONCLUSION

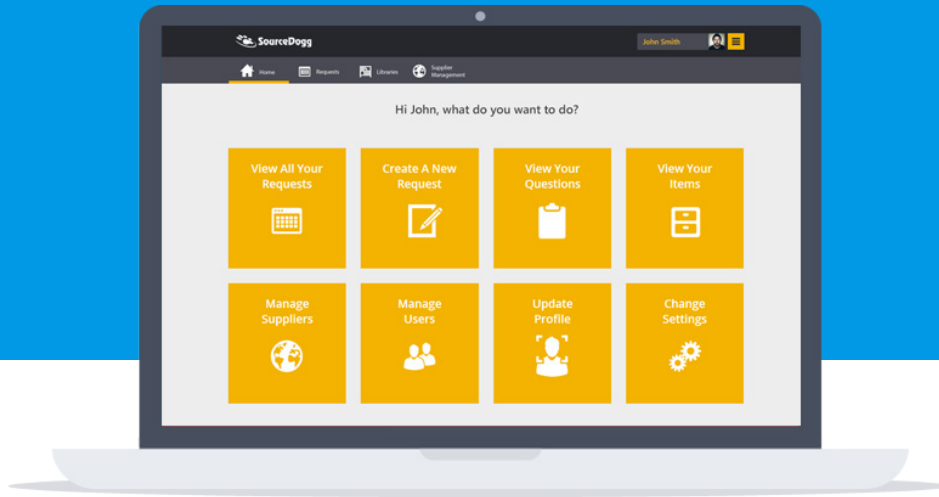
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There is no shortage of incentives and financial pressures for firms to take a second look at their tail spend. Initially it might appear that potential gains from changing the status quo are too small to justify action. However, closer inspection should reveal that paying attention to the more prosaic, day-to-day purchases makes sense financially and improves organisational effectiveness and probity. As the saying goes, “look after the pennies and the pounds will take care of themselves.”

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