

Supplier Diversity Meets Supply Management

SPEND MATTERS ANALYST TEAM

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Part 1: The Basics of a Program

This research brief is meant to serve as a general primer for procurement professionals needing to bring supplier diversity into their daily activities across the supply management function. We also hope it will prove useful for newly appointed supplier diversity managers and for senior procurement managers and corporate directors wanting to understand how supplier diversity fits in with their business, day to day and strategically. Our intention is to help you make the business case not just for greater investment in diversity programs but for the right programs to begin with.

The Diversity Stakeholders

Now that you have some grounding in the bigger supplier diversity picture, let's look at the regular chores of the diversity team (often an individual or two at the most) and everyone else in procurement who should influence diversity spending strategy, management and reporting. From an internal point of view, you are (or will be) faced with a plethora of expectations from corporate stakeholders. To name a few:

- Your public sector-focused sales team wants to understand how you have helped small and diverse businesses (SMWBE) in its territory.
- Your Fortune 500 clients expect regular detailed reports that describe how their business with you has resulted in expanded opportunities and results for small and diverse businesses.
- Your marketing team wants to know all the above so it can craft statements and targeted campaigns that enhance your brand image.

The first step with any diversity program should begin with understanding your spend and your current vendors. To accomplish this, you absolutely need to invest some time and resources in spend reporting

Yet you'll rarely get much of a budget from the C-level to accomplish the above. Moreover, you will also be faced with SMWBE vendors expecting contracts and numerous local, state and national organizations (public and private) wanting to know how your organization is performing and handling supplier diversity. If that's not enough, you'll be expected to give presentations on "your" progress to just about all of these groups, as well.

Getting Your House in Order

The first step with any diversity program should begin with understanding your spend and your current vendors. To accomplish this, you absolutely need to invest some time and resources in spend reporting. This is also known as spend analysis, although supplier diversity requirements may introduce certain nuances beyond standard spend visibility requirements (e.g., multitier reporting).

Start with spend classification and cleaning ERP data, which requires working closely with accounts payable and quite often IT, as well. Your friends in these areas will provide you with a detailed list of the past 12 to 18 months of spending data (we suggest going back at least 18 months if it is the first time you do this) across all of your vendors.

Then, give this file to a solution provider (e.g., [supplier.io](#)), which will match this record against its own databases. Don't even think about doing this yourself; it's not worth the effort. This third-party firm will flag known SMWBE firms with the appropriate tags and even help you determine which entries are duplicates, where there are parent-child linkages, match against IRS for tax ID accuracy and compare against other databases (e.g., OFAC) to discover other potential issues with your vendors.

Their final report should ideally be used to clean up your ERP and vendor management solutions and will serve as the basis for the many reports you will need to create for your constituents, both internal and external. This activity should be paid for out of general IT budget since it is an effort that supports master data management (MDM) and data quality for all areas of the company. Save your precious (and too small) diversity budget for other programs.

Finding SMWBEs

In many cases, diverse vendors will come knocking on your door. But are they the right suppliers you should be working with? No doubt, there are also existing supplier or business networks that you should consider. Depending on your procurement partners, platforms and technology solutions you should speak with firms like supplier.io, Aravo, SAP Ariba, Hubwoo, IBX, ConnXus, Coupa, D&B, Fedbid, MFG.com, Jaggaer and others about their supplier diversity-focused business network content. Many of these providers are improving the degree of supplier enrichment data they offer in their solutions, platforms and networks on a consistent basis. This includes diversity data. If their capabilities are limited today, check back in a quarter or two.

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Capacity Constraints and Planning

As soon as you start to find the right set of SMWBEs that have the products, quality, and price point that you need, the real challenges of effectively managing diversity programs will set in. Because many diverse suppliers are relatively small, by nature, you may run into delivery and capacity constraint challenges.

This is the No. 1 obstacle facing supplier diversity teams and diverse firms when they have gained some traction (meaning that the SMWBE has the right products and services at the right price points, but your organization, the Fortune 500 or 1000 client, by definition, will have such a ravenous appetite that the SMWBE is an automatic chokepoint in any larger rollout).

This is a topic we will further address in Part 2 of this analysis, but one trick is to employ a targeted rollout. Home Depot, for example, uses a store-based approval approach where promising SMWBEs can be “confined” to working only with a few stores, prove themselves, and scale up in a more controlled fashion. If this works for your organization, it can be a worthwhile activity, but you need a larger system in place to be able to move the proverbial business dial through multiple micro-rollouts throughout the company.

Part 2: Partnering with Diverse Suppliers

Continuing on, let's jump to **supply chain finance**, which is tied to the previous point we explored in Part 1 of our analysis: capacity constraints and planning. The current banking environment continues to strongly favor larger businesses with solid balance sheets over smaller, entrepreneurial ventures. Even getting a line of credit as a smaller business can prove challenging. Given this, it is no surprise that SMWBEs will not have access to capital at nearly the same attractive rates as the average Fortune 500 firm.

Therefore, the first step in engaging with diversity suppliers once they're in your vendor master should be to not squeeze your SMWBE with net 90 terms. To the contrary. With worthy SMWBEs (as well as with non-SMWBE smaller to midsize suppliers) you should consider extending more attractive credit terms.

For outcomes, whether you get preferred delivery, higher quality, better post-sales support, more favorable warranties or better pricing based on prompt payments as a result of getting diverse suppliers paid faster than the norm, it is important to consider the need to engage the broader finance organization (e.g., AP) and even other functions to implement a program successfully. And try to broaden your vision and go outside the standard procurement playbook in the process.

The below example is from a Michael Porter study:

"Nespresso, one of Nestlé's fastest-growing divisions, has expanded the market for premium coffee. Obtaining a reliable supply of specialized coffees is extremely challenging, however. Most coffees are grown by small farmers in impoverished rural areas of Africa and Latin America, who are trapped in a cycle of low productivity, poor quality and environmental degradation that limits production volume. To address these issues, Nestlé redesigned procurement. It worked intensively with its growers, providing advice on farming practices, guaranteeing bank loans and helping secure inputs such as plant stock, pesticides and fertilizers. Nestlé established local facilities to measure the quality of the coffee at the point of purchase, which allowed it to pay a premium for

better beans directly to the growers and thus improve their incentives. Greater yield per hectare and higher production quality increased growers' incomes, and the environmental impact of farms shrank. Meanwhile, Nestlé's reliable supply of good coffee grew significantly. Shared value was created."

Note how Nestlé used its more favorable access to capital to effectively finance the transition, and deployed coffee "black belts" to create change, and used its name, expertise, and leverage to drive contract terms and processes at the tier 2 level.

Multitier Bid Opportunities

As the Nestlé example shows, by reaching deeper into your supply base, you can uncover a lot of value. This might not traditionally be considered supplier diversity, but it should be. You don't need to go overseas to find these opportunities. It is an exceedingly interesting area right here in the U.S., where spend categories and opportunities at the Fortune 500 tier 1 supplier level can be significant in terms of both absolute dollars and volume levels. Moreover, many tier 1 supplier requirements come with such strict terms and conditions (e.g., insurance, bonding, liability) that smaller firms simply can't step into the ring.

In a nutshell, the open registration process offers a web-based path to provide initial registration data, to "raise your hand as a supplier" and start to engage with the customer without first being invited to do so.

This is where an understanding of the second and even third tier can come to the rescue. By matching up multiple smaller firms and having them support a larger firm higher up in supply chain, the same SMWME goal can be met

as if the SMWBEs were doing business with you directly. This is an underdeveloped area at the moment, with a few solution providers currently working on ways to make the engagement and management of this process easier outside of basic reporting. We expect providers to introduce enhanced capabilities here for supplier procurement and supplier diversity professionals in 2013 and beyond.

At Odds With Supplier Rationalization Goals?

One of the most challenging questions around supplier diversity is how best to balance supplier inclusion with supplier reduction initiatives. This is a bit of a false dichotomy, with technologies such as procure-to-pay, e-sourcing, vendor lifecycle management, business networks, big data analytics and heuristics all working to expand the pool of data points while lowering the expense of managing the content.

Better systems manage the gathering of data points dynamically, providing a more targeted path for suppliers as they identify their category areas of expertise and capabilities without drowning them in irrelevant questions.

Yesterday's challenges of keeping the ERP system's AP master as lean as possible was mainly a factor tied to the ERP system's shortcomings in relying on much vendor-related data being "maintained" in parallel "systems" such as file cabinets, Excel files, Access databases and so forth. Thankfully, the newer systems capture these extended data points, eliminating the need for labor intensive parallel

management systems — automating the gathering of on-boarding documents, compliance check-off lists, background checks, financial risk assessments and the like.

This doesn't mean that the ERP systems should be polluted with all this data, just that with an effective MDM approach you can have both clean ERP data and a rich pool of vetted, nearly on-boarded suppliers available to general procurement. Moreover, if you really want to be in synch with supplier rationalization programs as part of diversity initiatives, reference the multitier strategy above. You can always require your tier1 suppliers (with your guidance) to recruit and manage lower tier diverse suppliers on your behalf.

Open Registration

This is a critical component tied to the earlier "more suppliers" step. It stands in contrast to the prevalent closed registrations offered by typical ERP and vendor management installations. In a nutshell, the open registration process offers a web-based path to provide initial registration data, to "raise your hand as a supplier" and start to engage with the customer without first being invited to do so.

The open solution then guides suppliers through a path of extended data gathering fields and a bit of back-and-forth with corporate procurement if and when a fit is identified. It is essentially an iterative RFI experience that allows for as much data gathering up front as possible, saving time and work for all parties involved. Better systems manage the gathering of data points dynamically, providing a more targeted path for suppliers as they identify their category areas of expertise and capabilities without drowning them in irrelevant questions.

Part 3: Integrating with The Business

Perhaps the most important element that supplier diversity professionals should incorporate into their program management efforts is how to constantly incorporate general procurement efforts within their own. Working *with* general procurement should be the top priority for diversity teams. All too often, the trap for supplier diversity professionals is to lead a silo-based activity with few touch-points with general procurement.

Yet the more supplier diversity efforts tie into mainstream procurement programs and initiatives, the more effective a diversity program will be. Consider the concept of “open registrations” that we explored in Part 2 of this analysis. With open registration processes, it’s tempting to roll out a solution focused exclusively on diverse vendors. But this often results in a registration black hole where diverse vendor registrations go to die.

Working with general procurement should be the top priority for diversity teams.

A broadly adopted registration solution where all internal users rely on the same data is far more likely to generate visibility, bid inclusion and general traction beyond just the diversity function. Similarly, the diversity professional needs to be active in the general sourcing and procurement tools to understand company strategy, spend trends, category challenges and upcoming initiatives.

Sell Side Relevance

Even more than multitier sourcing, sell side relevance is an area of enormous importance to supplier diversity. By demonstrating how SMWBE initiatives make a difference on the sell side, the function will take on a completely different profile. Becoming a source of revenue — or at least being able to show linkages to the top line — will enable supplier diversity to become more than just a cost center.

Staying close to the money is important not just to understand what is being bought but also to demonstrate how high profile SMWBE successes can lead to sales wins. The successes can be individual firms or aggregated spend numbers tied to regions, clients or industry verticals. In order to find, locate and use the right pins in the supplier data haystack, however, supplier diversity leaders must work closely with sales. These efforts should include attending sales meetings, understanding the market strategy and finding areas where it’s possible to make a difference and strengthen proposals and presentations.

This will also help you orient your supplier diversity program (and time) toward revenue generating opportunities rather than more rearview mirror compliance activities that will only continue to pain supplier diversity (and much or all of procurement) as a cost center. Obviously you still have to show a clear spend history, community impact, multitier spend cloud and trends, but these activities can (and should be) automated, not to mention as easy as pulling the right report.

Mandates vs. Incentives

It’s tempting to mandate that a certain portion of spend has to go to a certain subset or flavor of supplier, but this is counterproductive, since it rigidly forces decisions that can lead to peculiar subcontracting practices of dubious or even unethical qualities that perpetuate the affirmative action image and even opens you up to lawsuits around reverse discrimination. The latter is not just a possible outcome; it is quite likely. Many lawsuits have gone against firms with poorly discussed supplier diversity rules and practices. Incentives are far better.

Sharing supplier diversity “carrots” rather than swinging “sticks” can start with creating SMWBE visibility and awareness in the general procurement team, as well as among existing tier 1 (direct) suppliers and then working toward including the SMWBEs in opportunities where they

have a reasonable chance of performing well. Using this approach, the ultimate outcome will be more sustainable, and you will not create animosity or other problems.

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Best efforts goals represent a good model to pursue. For example, contractual terms are included in your agreements with your direct suppliers to the effect that they will provide you with a report around not only the SMWBE impact arising from the contract in question but also to document how they went about determining the subcontractors they used, including SMWBEs. A bit of daylight and process thinking can address much inertia.

Budget Challenges

“Supplier diversity teams never get any funding” is an all-too-constant refrain. Yet this is a legacy challenge, resulting mainly from the cost center orientation to diversity, in which budgets get consumed by basic activities such as getting clean procurement data, and the technology needed to get to square one. This challenge will never change as long as the cost center mindset is in place. Supplier diversity and procurement leaders must focus on following the earlier advice we referenced around shifting to a sales strategy focus and supporting efforts where you move closer to the money and work with sales and operations to enable their goals. This is easier said than done but is a critical path to move forward.

Part 4: The Details Matter

As we conclude our initial series on creating a roadmap for success with supplier diversity initiatives (see Part 1, Part 2 and Part 3), we come to a handful of final, in many cases tactical, recommendations that can make or break program success. These are the “school of hard knocks” lessons focused on supplier diversity data management that we encourage our readers to take to heart, learning from the mistakes of others (including us) as we’ve helped to rollout and manage these programs over the years for dozens of organizations.

First on our list is reiterating the importance of how and why **details matter**. The proverbial guy with horns and pitchfork lurks everywhere details live, and data cleansing and classification is no exception. Unfortunately, cleansing and classification efforts are actually more complicated than they seem. The corporate data point of reference is usually the AP vendor master, and the reports you (the SD professional) are expected to come up with on a regular basis are typically rear-view mirror activities that are concerned only with how much your company paid to SMWBE firms in the previous quarter, year or by contract (especially if you have federal contracts). To make this insight forward-looking and actionable is another matter entirely, but it first requires taming the spending devil.

Next we come to **goal alignment**. Here, we view the root cause complication from diversity efforts: it comes from the fact that AP data is being managed by people and systems that are geared primarily toward managing financial relationship information and on-boarding compliance (e.g., code of conduct compliance, credit risk, insurance levels and similar requirements). For this reason, it’s likely that diversity-focused on-boarding and vendor management questions such as which particular category the diverse vendor in question should be sorted under and whether or not the vendor in question is currently certified are likely to take a third-row seat in standard supplier management initiatives. For this reason, it’s best to invest the time to work with AP as much as possible up-front with a broader charter that encourages their best efforts.

Category overload is something diversity professionals are accustomed to. There are quite a few diversity categories, including woman, minority, veteran, service-disabled veteran, American Indian, LGBT, HUBZone and SBA 8(a). Another dimension is the certifying agency. For example, certified SMWBEs can get their credentials from one of the big brands such as the [National Minority Supplier Development Council](#) (NMSDC) and the [Women’s Business Enterprise National Council](#) (WBENC) or from one of a long list of city, state and federal organizations that certify SMWBEs — several hundreds of them, actually.

Even local utilities have SMWBE certification programs. Then there is self-certification, something that many vendors (and buyers) do in supplier lifecycle management tools and elsewhere in their interactions with buying organizations. Solid ground is not so firm when it comes to audits from non-validated information sources.

To make matters worse, when it comes to **confusion and definitions**, the companies (i.e., your customers) requesting supplier diversity spend information reports have somewhat inconsistent ideas around which vendor category “counts” and which type of certifying organization is recognized. Other questions can arise, as well. For example, how long to grandfather in suppliers who were once verified as diverse, but have now fallen into an unknown status? It’s a mess, really. Create standardized definitions up-front and save the hassle. (This requires close cooperation with your sales team.) Your sell-side can be a powerful ally, so learn to develop this relationship.

And with apologies to Steely Dan, we also need to acknowledge that **old-school is no longer cool**. Further complicating the issue of definitions, certification and category overload, the two main certifying organizations (NMSDC and WBENC) make matters even harder for the Fortune 500 and the technology firms that support them by firewalling their certification records.

You can access them — for example, if you are an NMSDC corporate member on the national level in good standing (i.e., you pay from \$20,000–\$40,000 per year for national membership), you do get a login to its relatively crude website permitting manual individual record searches. Paying a few thousand for local NMSDC council membership gets you no such access. Unfortunately, these organizations refuse to share their databases with any data cleansing organization or provide APIs to populate ERP, P2P and other corporate systems with accurate information. It is worth noting that supplier.io has had the right to use this data to augment its clients' data cleanses, but no reselling or sharing beyond that.

As part of the need for recognizing the need for better data, you should seek out third-party friends (e.g., supplier.io).

Most peculiarly, NMSDC quickly pulls recently expired supplier records from its database so clean audits are actually impossible to conduct. Ironically, this is a counterproductive attitude that significantly reduces the value of taking the time and money to get an NMSDC or WBENC certification. The two organizations do a great job in other areas, but not supporting large-scale automated data cleanse and classification efforts is a decade behind the times; nobody has the time to validate records manually. As a reference, a typical Fortune 500 firm has 50,000–100,000 active vendor records. This needs automation to work.

We also need to acknowledge the prevalence of **bad data**. No matter whom you speak to in the industry, there is *no* provider out there who can give you a perfect assessment. Some are better than others, yes, but they *all* have flaws, and some are quite substantial. Some providers have (at least in the past) tried to get around the NMSDC and WBENC walls through various forms of subterfuge involving data aggregation across multiple parties, among other things — benign activities that only served the goal of better supplier diversity data. This is a challenge to everybody.

As part of the need for recognizing the need for better data, you should seek out **third-party friends** (e.g., supplier.io). Two critical takeaways from this analysis should be that you will never get to perfection, and that you need a partner to work with for supplier diversity data cleansing and management. This is an activity that you go through only infrequently, while the solution provider partner does it on an ongoing basis. This should be a partner you can refer to for clarification and follow-up in case of an audit or other challenge.

The Final Word

So, what's the answer when it comes to supplier diversity and data management? It all depends. You need to understand your sell side, what reports your clients expect, which their recognized criteria are and the needs of your own industry vertical. The combination of these factors will then guide you to establishing which criteria you need to stay on top of — and which partners to work with. No doubt, many judgment calls to be made along the way, and this is still an area where experience can trump technology.