

Procurement & Supply Chain
Prof. Corrado Cerruti

Chapter 4

Buying business services

Learning objectives

- The increasing importance of the buying of services.
- The differences between buying services and buying goods.
- Different views on buying services and the implications for the purchasing process.
- The importance of **stakeholder management** for buying services.
- Specific areas of attention in **specifying services**, and selecting and contracting service providers.
- The importance of **professional contract management**.

Professional purchasing

- Outsourcing and offshoring means service companies have become aware of the necessity to put professional purchasing and contract management in place.
- Purchasing excellence explains how to professionalise purchasing, making use of two types of processes;
 - strategic management processes
 - Enabling processes.

Increasing importance of services

- The purchasing to sales ratio for industrial companies may range between 60 and 80%.
- For service companies the purchasing to sales ratio usually amounts to 10–50%.
 - For service providers the largest part of their total cost is related to personnel.
- Professional services-buying is rising on the corporate agenda.

Differences between goods and services

- We define services as ‘the management of a series of more or less tangible activities, which take place in the interaction between customer and supplier employees, that either or not in combination of physical goods or solutions are offered as an integrated solution to customer problems’.
- Since services involve people and every person is unique, service exchanges cannot be standardized. Services relate to the exchange of knowledge, expertise and capacity that are embedded in human beings. Therefore, the actual exchange will be different depending on the individuals a buyer deals with. This explains why it is so difficult to produce and buy services at a consistent quality (Ellram et al., 2004).

TABLE 4.1 Differences between goods and services

<i>Pure services offering</i>	<i>Pure product offering</i>
100% Services	100% Product
Intangible	Tangible
Production, distribution and consumption are simultaneous processes	Production and distribution are separated from consumption
More difficult to demonstrate (not available)	Can be demonstrated before moment of purchase
Cannot be transported	Can be transported
Is an activity or a process	Is a physical entity
Is produced in interaction between buyer and seller	Is produced in a specialized remote facility
Customers participate in production process	Customers in general do not participate in the production process
Cannot be stored	Can be stored
Property cannot be physically transferred	Property is physically passed on to new owner

Classifying Services as portfolio

- Portfolio consisting of four quadrants (i.e. leverage products, strategic products, routine products and bottleneck products).
- Can be based upon two criteria: financial impact and supply risk.
- Serves to develop four differentiated supplier strategies.

Pre-contractual stage

- Specifying: defining the scope of work for service providers.
- Selecting service providers.
- Contracting for services.

Specifying

FIGURE 4.1 Methods for specifying business services

Input specification →	Throughput specification →	Output specification →	Outcome specification
Focus on resources and capabilities of the supplier	Focus on supplier processes needed to produce the service	Focus on the functionality or the performance of the service	Focus on the economic value for the customer to be generated by the service

Source: Adapted from Wynstra and Axelsson (2002), p. 144

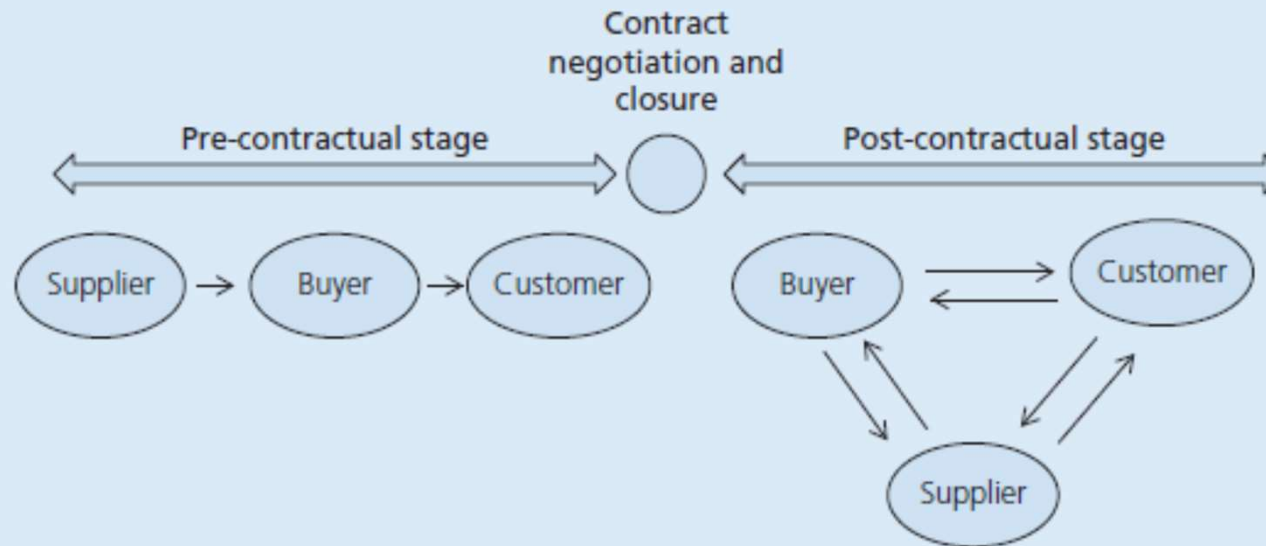
Figure 4.3 Some suggestions for contracting services

- Specify the performance to be delivered by the supplier instead of the activities to be conducted.
- Describe when and where the service needs to be provided.
- Describe who would benefit from the service and in what way.
- Check reputation, expertise and qualifications of the supplier.
- Request the CVs of key personnel and make sure that personnel are available during the period in which service needs to be delivered.
- Analyze how the service process will be organized and check the quality system and training policy of the service provider, discuss potential threats and weaknesses, and, most important, the risks.
- Invite potential service providers to present a business case which is based on the scope of work.
- Check the cultural fit between your company and the company of the service provider.
- Aim for a performance-based contract, an SLA that includes critical performance indicators as well as a detailed work plan and time schedule.
- Agree on financial, personnel, technical and information resources to be made available by the buying organization.
- Prepare for detailed inspection and quality procedures.
- Discuss and agree on procedures for dispute resolution.
- Agree on performance-based payment schedules.
- Agree on an effective communication structure and make working arrangements.

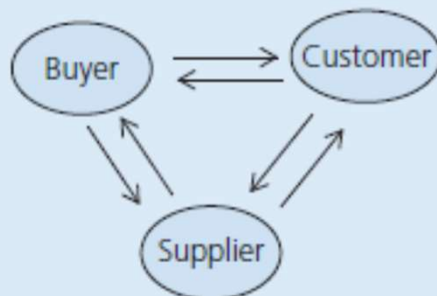
Post contractual stage

- Contract manager is responsible for selecting the right contract, contract negotiation and contract compliance by buyer and seller.
 - the buying organisation and the service provider should actively collaborate to establish a successful service delivery.
 - an effective link between the tactical purchasing process and the operational stages of the project and contract execution means that operational staff members should be consulted at an early stage about how activities actually take place.

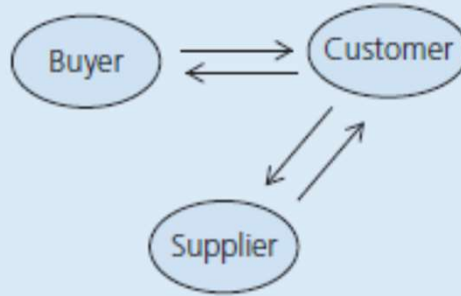
Figure 4.4 Triad configurations in services delivery



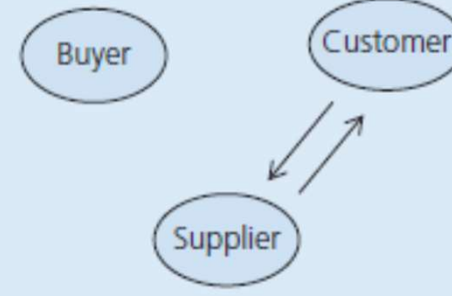
A. Fully connected triad



B. Partially connected triad



C. Disconnected triad*



* Supplier serves as a bridge

Involvement of purchasing in contracting for services

- Traditionally, buyers were involved in low importance services e.g. travel, print or courier.
- Increasingly buyers are involved in high importance like marketing and ICT.
- These types of services may not be contracted for by the purchasing department, but by the respective functional departments using their own contacts.
- When tight interpersonal relationships between internal customer and supplier exist, it will be difficult for any buyer to interfere.

Summary

- Traditionally, services buying was limited to contracting for facility services.
- Buying services requires specific expertise and close collaboration with internal experts in the company especially if an internal customer has strong personal relationships with the service provider.
- Challenges include:
 - deciding on the specification of services.
 - objective selection criteria.
- Service-level agreements stimulates internal customers to express the key performance indicators.