Procurement Risk Management

Like life itself, procurement is an inherently risky endeavour. Suppliers can fall short of the mark in quality, quantity, or timeliness. Rogue spending and fraud can erode your profits without being detected until it’s too late. Internal processes may not be optimised, resulting in costly errors and exceptions. And at the end of it, you’re the one left holding the proverbial bag. As a result, procurement risk management is a key part of effective and strategic sourcing.

Managing risk within your supply chain might seem daunting. But with the proper procurement processes in place, the right technological tools at your disposal, and a well-informed, carefully planned risk mitigation strategy, you can take control of your supply chain management, reduce or eliminate dangerous potential risks, and generate both cost savings and measurable value for your business.

Procurement Risk Management Builds a Better Bottom Line

Whether you’re ordering raw materials, processing purchase orders, revising terms through contract management, or onboarding new suppliers as part of a strategic growth initiative, chances are the choices you make will involve varying degrees of, and possibilities for, exposure to internal and supply chain risk. The potential risks will vary by both vendor and business, but procurement organisations of all sizes understand that both process and supplier risk must be kept to a minimum.

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to support both the health and efficacy of procurement and the ambitions of the company as a whole.

Effective risk management strategies are focused on continuous improvement, and supported by clear, constant communication and collaboration with both your internal staff and stakeholders and the vendors in your global supply chain. By establishing and communicating your expectations and requirements to all parties, you can gain their engagement and help ensure they’re focused on meeting your company’s requirements for accuracy, efficiency, and orders filled at the greatest speed, best prices, and highest quality available.

Collaborating gives your staff and suppliers the time and resources they need to develop solutions to the common challenges related to capacity, price, and timeframes. In turn, your company:

- Uses resources more effectively—less waste, more profit
- Enjoys improved production, distribution, and customer service supported by a surprise-free supply chain
- Gains versatility in pursuing innovation
- Spends less time correcting exceptions and errors and more time on high-level strategic initiatives
- Develops rich data for analysis and smarter decision making at all levels

As an added benefit, your procurement organisation has a chance to identify your strongest potential partners, and streamline your supply chain to reduce bloat without sacrificing capacity.

**NOTE:** One of the best ways to approach procurement risk management is with the aid of a software solution. Driven by artificial intelligence (AI) and enabling easy, effective automation, these centralised procurement solutions give you the tools you need to handle everything from vendor relationship management to procure-to-pay (P2P) processing to deep-level spend analysis and strategy. With an automation-empowered software tool, all stakeholders gain access to the data they need, in real time, and every piece of information related to every single transaction is collected, and connected, for total transparency and more accurate predictive analytics.

“While it would be wonderful to simply check off your procurement risks and forget about them once they’re solved, the truth is that risk is a constant and ever-changing threat to your procurement team and your entire company. Consequently, you need consistent, and constant, risk monitoring to ensure your risk exposure is as low as possible.”

**The Procurement Risk Management Process**

As with many procurement processes, procurement risk management benefits from an organised,
multi-stage approach—in this case, four stages.

1. **Identifying Risk**  
2. **Risk Analysis**  
3. **Controlling Risk**  
4. **Monitoring Risk**

Each stage of the process can be further refined into specific tasks.

**Identifying Risk**

The goal here is to gain an understanding of the potential risks associated with a given task, process, or supplier. In general, potential risks can be identified as coming from one (or more) of these sources:

- Strategic/Process-Driven Risk  
- Project-Specific Risk  
- Compliance Risk  
- Quality Risk  
- Logistical Risk  
- Cost Risk  
- Fraud Risk

For example, the absence of effective supply chain management creates an internal process-driven risk that also creates cost and fraud risk, since it can permit both rogue spending and fraud to flourish.

When evaluating supplier risk, a vendor who fails to deliver on time, creating delays in both production and distribution of your own products, is a logistics risk. A vendor whose products fail to meet quality standards, or whose practices fail to comply with safety laws, is a compliance risk.

As you identify potential risks, it’s a good idea to document them in what’s known as a risk register. This project management tool lets you identify risks and record their impact, frequency, and optimal resolutions as you move through the risk management process.

**Risk Analysis**

Having identified potential risks, you can move on to analysing them to determine how likely they are to occur—and the effects they’ll have on your operations, efficiency, and bottom line.

Using a risk assessment matrix, you can chart the overlap between the likelihood of risk and its potential impact. Often referred to as a 5 x 5, it gives you a visual reference that’s useful in identifying the risks most in need of immediate correction. You can assign each level a value and

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score a given procurement process, vendor, or other risk accordingly.

For example, your 5 x 5 might look like this:

<table>
<thead>
<tr>
<th>Probability of Occurrence</th>
<th>Severity of Impact</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Negligible</td>
</tr>
<tr>
<td>Frequent</td>
<td></td>
</tr>
<tr>
<td>Probable</td>
<td></td>
</tr>
<tr>
<td>Occasional</td>
<td></td>
</tr>
<tr>
<td>Remote</td>
<td></td>
</tr>
<tr>
<td>Improbable</td>
<td></td>
</tr>
</tbody>
</table>

As you can see, costly or dangerous risks that occur with great frequency can be catastrophic, and therefore need immediate attention, while unlikely events with little or even no impact on your company’s health, profitability, or reputation can be handled in a more leisurely fashion.

**Controlling Risk**

How you address each procurement risk depends on its severity. Approaches vary, but as a rule of thumb you can control risks using one of the following methods:

- **TOLERANCE**: Ideally, no risk is the correct amount to tolerate. But for low-risk items, the cost of removing it may exceed the value gained from doing so. That said, all risks should be constantly monitored, and reduced or eliminated whenever it is both cost-effective and reasonable to do so in order to avoid escalation.

- **TREATMENT**: Most risks will likely require this level of attention, which is simply an action taken to remove the risk or reduce its threat to a safe (i.e., tolerable) level.

- **TRANSFER**: Some risks may be best handled by third parties. However, make sure you’ve accounted for the potential costs and additional impacts that can result from shifting responsibility to another party. In some cases, taking a more direct approach (e.g., working with a valued but underperforming vendor to bring them into compliance) can generate value and intangibles that won’t be created by simply pulling the plug or allowing a third party to handle the issue.

- **TRANSFORMATION**: When risk reaches critical or even catastrophic levels, it might be time to take a step back and develop an entirely different solution. Rolling with the punches is fine, but if disaster looms, stepping out of the ring and finding a new strategy can help you win the day.

**Monitoring Risk**

While it would be wonderful to simply check off your procurement risks and forget about them once
they’re solved, the truth is that risk is a constant and ever-changing threat to your procurement team and your entire company. Consequently, you need consistent, and constant, risk monitoring to ensure your risk exposure is as low as possible.

Using the risk register you created in stage one, ensure every risk has a complete entry containing the following relevant information:

- Risk ID number or code
- Detailed description of the risk
- List of parties responsible for monitoring and controlling the risk
- Risk analysis data, including probability, impact, and date of analysis
- Actions taken, including any ongoing actions necessary to remove or control the risk
- Scheduled review date

As you monitor your procurement risks, be sure to update the risk register at each stage and review ownership roles regularly to ensure each risk is being handled with maximum efficiency and efficacy.

**Track and Tame Your Procurement Risk**

Into every company a little risk must fall—but that doesn’t mean you have to take it lying down. From the supply chain to the C-suite strategy meetings, managing risk empowers your team to grow, innovate, and thrive. Get a firm grip on the procurement risks that threaten your organisation’s profitability and performance to slash costs, build strong supplier relationships, and make procurement strategy a key component of your company’s success.

Manage Procurement Risk, Relationships, and ROI with PurchaseControl

[Find Out How](https://www.purchasecontrol.com/blog/procurement-risk-management/)
About PurchaseControl

PurchaseControl is cloud based procurement software for business spend management. We empower businesses by providing greater transparency and oversight into the purchasing process. With PurchaseControl, you have the flexibility to manage how spend actually happens instead of how you wish it would happen.

The entire PurchaseControl team has experience within a range of businesses, and as such, we bring a practical, holistic approach to purchasing. We understand what it takes to run a business and apply that knowledge to make PurchaseControl as effective as possible for all users.

Learn more at www.purchasecontrol.com

Contacts

EU Office Information
UK: +44 845 591 27 24
Ireland: +353 1 513 4623
enquiry@purchasecontrol.com

US Office Information
US: 800 737 5605
inquiry@purchasecontrol.com

Connect With Us
Facebook: https://www.facebook.com/PurchaseControl/
Twitter: https://twitter.com/purchasecontrol/
LinkedIn: https://www.linkedin.com/company/purchasecontrol/

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