A guide

Do you have effective cost control in your company's procurement procedures?

CostTracker

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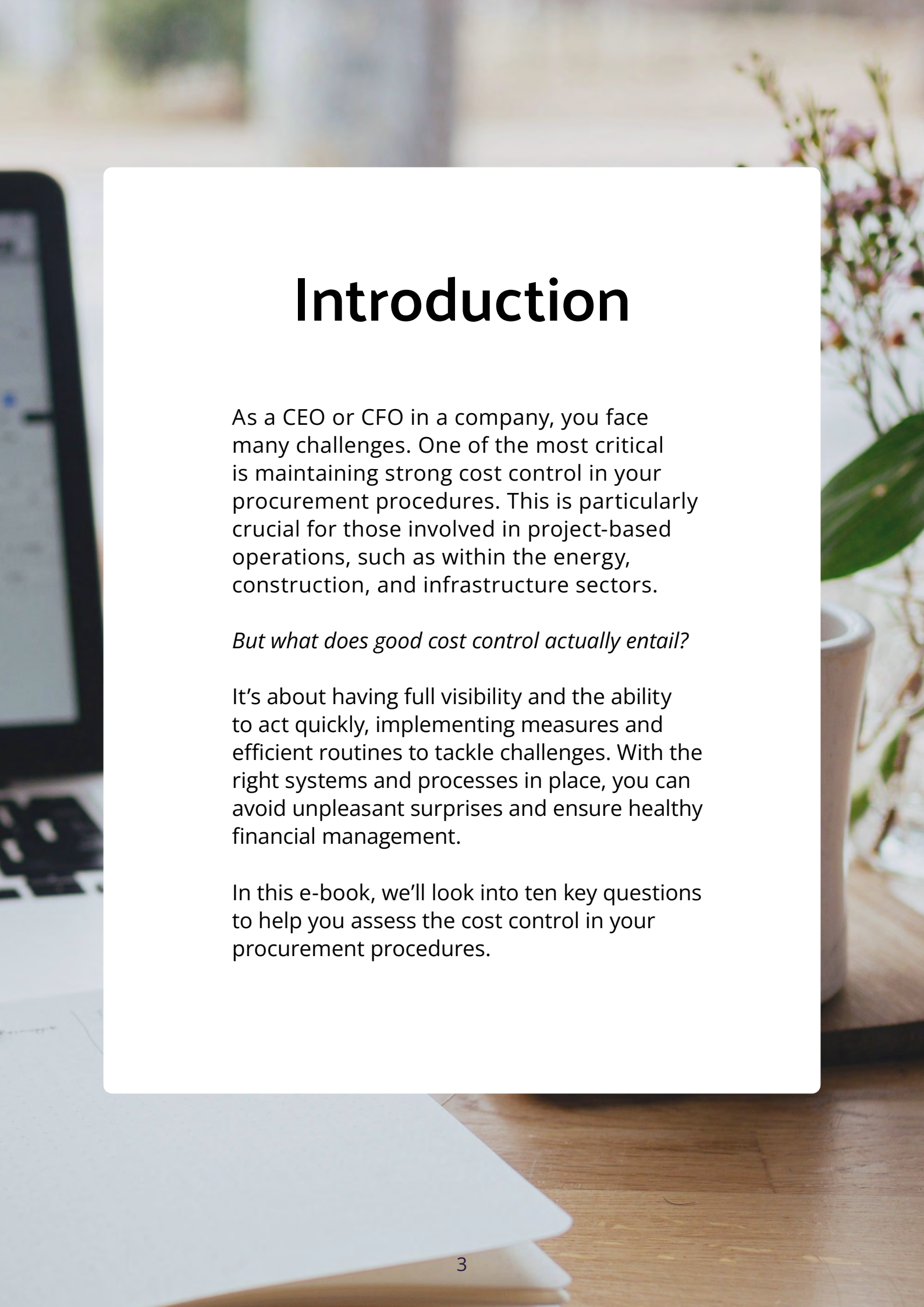

Introduction

As a CEO or CFO in a company, you face many challenges. One of the most critical is maintaining strong cost control in your procurement procedures. This is particularly crucial for those involved in project-based operations, such as within the energy, construction, and infrastructure sectors.

But what does good cost control actually entail?

It’s about having full visibility and the ability to act quickly, implementing measures and efficient routines to tackle challenges. With the right systems and processes in place, you can avoid unpleasant surprises and ensure healthy financial management.

In this e-book, we’ll look into ten key questions to help you assess the cost control in your procurement procedures.

About the author

Torstein Floden has over 20 years of experience as a CFO/Financial Manager and Controller in various industries such as biotechnology, oil and gas, as well as greentech. His extensive experience in financial management and technological innovations has been central to his role as a co-founder of **CostTracker**. Where he contributes to transforming procurement and cost management for project-based companies globally.

Torstein Floden,
co-founder of CostTracker.

Did you know research from **Menon and Concept** indicates that the cost of an average public construction project increases by 40% between the concept selection (KS1) and investment decision (KS2) stages?

While the cost of an average public building project rises by up to 60% between KS1 and KS2?

Can you imagine why?

The research shows that unclear goals and requirements (40%) are the most common cause of project failures. Additionally, lack of resources (25%), scope changes (25%), lack of management support/involvement (23%), and differing roles and responsibilities (23%) are mentioned.

In other words, clearly defining the scope can be the difference between *success* and *failure*.

1. What is the project scope?

You're hosting a party. Who will handle the decorations, how many will give speeches? Wait, who was in charge of the cakes again?
As the organizer, your job is to ensure clarity and understanding among all involved.

Scope.

Why is it important? Well, because a clearly defined scope reduces the risk of misunderstandings and errors, laying the groundwork for a successful project execution.

The goal is to clarify objectives and delivery expectations.
In customer-oriented projects, work begins with a bidding process to define the project's scope and ensure success. This process is less relevant for internal projects.

You should consider the following points:

- **Definition of goals and delivery expectations:** Collaborate with the customer to clearly define what the project aims to achieve and the expected deliverables.
- **Communication and alignment:** It's important to ensure that all stakeholders understand and agree on the project scope. Ensure effective communication and alignment throughout the process.
- **Stakeholder clarification:** Identify all relevant stakeholders and clarify their roles and responsibilities in the project to ensure no crucial aspects are overlooked.
- **Change management:** Develop clear change procedures within the project scope. This involves assessing the consequences of changes as well as thorough documentation and approval from relevant stakeholders.
- **Learning and continuous improvement:** Evaluate past projects to reduce risks through better procedures and checklists. Incorporate this knowledge into the project scope to optimize future outcomes.

By focusing on these key factors in the project scope, you establish a solid foundation for success and reduce the risk of cost overruns and other challenges along the way.

2. Do you have a robust plan for project entry?

Some slogans are so simple they're genius: **"Fail to prepare, prepare to fail."**
Thorough and thoughtful planning is crucial to ensure that your projects run smoothly from start to finish. A solid plan not only provides clarity on what needs to be achieved but also identifies resource requirements, milestones, and potential risks in a systematic manner.

Key points for you to consider:

- **Goals and milestones:** Define clear objectives for the project and identify milestones that mark important progress points. This provides you with a framework to measure progress and ensures that the project is moving towards its overall objectives.
- **Resource allocation:** Identify the resources needed to execute the project, including human, financial, and material resources. Ensure that the resources are available when needed and address any bottlenecks beforehand.
- **Quality control:** Incorporate mechanisms for quality control into the plan to ensure that project outcomes meet expectations for quality and accuracy. This may involve regular review and testing of the products or services delivered.

- **Change management:** Implement procedures to handle changes in the project's scope or requirements. This may include a formal change control process that requires approval from the project stakeholders before changes are implemented.

- **Monitoring and reporting:** Establish systems to monitor the project's progress and generate regular reports that provide insight into the project's status. This enables the identification of any deviations from the plan early on and the implementation of corrective actions. Ensure that everyone who needs it has easy access.

  By investing effort in a comprehensive planning process, you can strengthen the foundation for success and increase the likelihood of delivering your projects within schedule, budget, and quality measures.

3. Do you have a risk management plan?

Hypochondriac or just well-prepared? You should identify potential threats and opportunities for the project. Develop a plan to handle and minimize risks, including alternative measures if unforeseen events occur.

Define which risks you can mitigate and how, and which risks you are willing to accept.

Here are some key aspects to consider:

• **Risk identification:** Through a thorough review of the project's scope, goals, and operating environment, you should identify potential risks that could affect the project's success. This could include anything from technical challenges to changes in market conditions.
See examples on the next page.

• **Risk assessment:** Following the identification of potential risks, you need to assess their probability and impact. This will help you prioritize the risks and determine which ones require the most attention and resources to manage.

• **Risk mitigation**:
Develop strategies to reduce or eliminate the risks.
This may involve implementing controls, backup plans, or alternative action plans to address unexpected events.

• **Change management:**
For projects involving complex changes, such as construction projects, it's essential to have clear guidelines and procedures for managing changes. This may include approval procedures for change requests, contract revisions, and assessment of the implications on the schedule and budget.

• **Monitoring project progress:**
Implement systems and procedures to continuously monitor and measure the project's progress. This may include regular reporting, progress meetings, and the use of project management tools to keep stakeholders informed about the project's status.

• **Currency:** Within risk management, it's important to consider foreign currency trading. Changes in exchange rates can lead to significant cost variations, which may exceed the initially estimated expenses.

Examples of risks:

- **Resource risk:** Do you have access to essential resources for project implementation?

- **Time risk:** What could lead to the risk of delays, which may result in liquidated damages?

- **Technological risk:** Do you have the right tools to ensure successful project execution?

- **Legal risk:** Is there a risk of changes in laws and regulations that could affect your project?

- **Communication risk:** Do you have good procedures in place for communication, both internally and externally, or is there a risk of misunderstandings?

- **Market risk:** Is there a threat of market changes affecting the project? This could apply to both the supply and competitive sides of the market.

4. Are your contracts crystal clear?

Clarity in agreements between you and your suppliers or customers is crucial to ensure smooth project execution and to avoid misunderstandings that can lead to cost overruns or delays.

Here are some key factors to consider:

- **Price and payment terms:** Specify exact pricing for products or services, including any agreed-upon discounts or additional services. Also, clarify payment terms, including any deadlines for payment and fees for late payments.

- **Defined delivery terms:** Ensure that all relevant delivery terms are clearly stated in the agreement, including time, place, and payment terms. This will help avoid misunderstandings about delivery expectations and ensure that both parties agree on the terms.

- **Quality requirements:** Clearly specify the expected quality standards for the products or services to be delivered, including any tests or approval processes that need to be conducted. Attachments such as technical drawings and the company's terms & conditions should accompany the order. This will help ensure that you receive products or services of sufficient quality that meet your needs.

- **Change orders:** Implement a clear process for handling change orders, including how changes in scope or requirements will affect costs and timelines. This will ensure that any changes to the project are carefully considered and documented before implementation.

- **Consider purchase order system:** Quality, timing, price, and payment terms are all elements you'll find in a purchase order system.

- **Communication and reporting:** Establish regular communication and reporting channels with suppliers or customers to ensure that both parties are informed about the project's progress and any changes in scope or requirements.

- **Contract management:** Have clear procedures in place for contract management, including how any conflicts or disagreements should be resolved. This will help ensure that both parties adhere to the agreement and that any changes are resolved efficiently.

By ensuring that your agreements are clear, comprehensive, and well-understood by all parties, you can minimize the risk of misunderstandings and conflicts that may occur during the project.

5. Can you trust your suppliers?

Of course, you're expected to do your job, but part of it is ensuring that your external suppliers are reliable and deliver top quality. Assemble a great team to ensure smooth progress, quality deliveries, and minimize the risks of unforeseen costs.

Key points to consider:

• **Supplier evaluation:** Conduct a thorough assessment of potential suppliers before entering into agreements. This includes evaluating their reputation, past performance, references, and ability to meet the project's requirements. Also, ensure they have the appropriate certifications if it's an internal quality requirement (e.g., ISO).

• **Contract negotiations:** Ensure that contracts with suppliers are clear and comprehensive, including all relevant terms and conditions. This includes delivery terms, quality requirements, payment terms, and procedures for change management.

• **Monitoring supplier performance:** Keep careful track of supplier performance throughout the project. This may involve monitoring delivery times, product or service quality, and communication effectiveness.

• **Communication and collaboration:** Maintain open and regular communication with suppliers to address any issues or concerns early on. This enables the quick resolution of potential challenges and helps avoid delays or quality issues.

• **Supplier base diversification:** Consider working with multiple suppliers to spread risk and ensure you have alternatives available if one supplier cannot meet the requirements.

• **Supplier relationships:** Invest time and resources in building and maintaining strong relationships with your suppliers. This may include providing regular feedback, rewarding good performance, and resolving any conflicts or disagreements constructively.

• **Consider a purchase order system:** To ensure you choose the most reliable and optimal suppliers for your projects, having a system in place is essential. This system enables you to evaluate factors such as error reports and delivery punctuality. With **CostTracker**, you can access historical cost data and track all relevant information, including quality metrics and timing. In short, a purchase order system will help you keep track of which suppliers you can rely on to deliver what you need.

By choosing reliable suppliers and maintaining strong relationships with them, you can reduce the risk of delays, quality problems, and other challenges that may affect the project's success.

6. How do you measure and evaluate?

It's great that you have a clear direction, but sometimes it's wise to make a quick pit stop to ensure you're still on the right track. Use regular measurements and evaluations to ensure resources are being used effectively and that you achieve results according to the plan.

Here are some key aspects of measurement and evaluation:

• **Budget measurements:**
Continuous monitoring of costs compared to the budgeted amount is necessary to ensure that the project stays within financial limits. By comparing committed costs to budgeted igures, any deviations can be identified, and actions can be taken to correct them.

• **Progress tracking:**
Assessing the project's progress compared to planned milestones and timelines is essential to ensure timely delivery of results. This may involve monitoring work progress, resource utilization, and achieved milestones to identify any delays or bottlenecks.

• **Deviation management:**
It's crucial to identify and address deviations from the plan as early as possible. This may include changes in scope, cost increases, or other unforeseen events impacting project execution. Detecting these early allows for prompt action to minimize their impact on project success.

• **Commitment management:**
Maintaining control over open commitments and invoices is vital to prevent unexpected expenses and ensure accurate financial reporting. This includes regular review of supplier agreements, approval of invoices, and monitoring of payment terms.

• Consider implementing a purchase order system:
By utilizing tools like **CostTracker**, you can streamline the process of measurement and evaluation by providing functionality for budget tracking, progress reporting, ordering, and deviation management. The system captures commitments, helping you avoid being left with a long tail of costs. You'll also be able to see the financial status of the project immediately upon completion.

By measuring during the implementation phase, you can improve control, efficiency, and results in your projects while ensuring you meet your planned goals and requirements.

However, upon project completion, it's important to ask yourself a new question;
Do you have effective procedures to enhance project delivery?

And how effective are you really at integrating lessons learned from previous experiences?

Having clear goals and established procedures to capture and apply this learning in future projects is important. This includes assessing whether the scope was sufficiently defined, if the goals were clear, if the budgeting was realistic, and if resource allocation was appropriate. Continuous measurement and evaluation of projects should be a continuous process. You take the lessons from each implementation into new projects, ensuring you don't repeat the same mistakes and continuously streamline and develop your routines.

7. Do you have liquidity under control?

"Show me the money!" as Jerry Maguire famously said. Liquidity, or cash flow, is vital to ensure that projects can be carried out without delays or interruptions due to lack of financial resources.

To control liquidity in the project, you need to have control over everything from procurement plans, deliveries, and agreed payment terms. Sometimes this also involves milestone payments, adding further complexity. With a purchase order system, you can easily track your commitments, including payments to suppliers and delivery times for goods and services. By using **CostTracker**, this information can be managed automatically, freeing you from having to manually gather information from various sources.
In the worst-case scenario, without sufficient control, you may find yourself in a situation where your project cannot be delivered as planned. By digitizing and automating the process with a purchase order system, you can minimize the risk of such scenarios and ensure that the project progresses smoothly and efficiently.

8. Still using spreadsheets, like Excel?

While spreadsheets can be a useful tool for certain tasks, it has limitations when it comes to the complexity and management of procurement processes. As you have seen in the previous 7 points, there is a lot you need to keep track of.

You can actually make your everyday life a *little* easier!

By using dedicated purchase order systems like **CostTracker**, you can streamline processes, reduce the risk of errors, and gain better control over your procurement routines.

Here are some considerations regarding the use of spreadsheets in projects:

Benefits of using spreadsheets:

• **Low cost:** Spreadsheets are often available and does not require additional expenses to use.

• **Flexibility:** Users can customize their spreadsheets to meet specific needs and requirements.

• **Wide range of features:** Spreadsheets offers a broad range of functions for data manipulation, analysis, and reporting.

Disadvantages of using spreadsheets:

• Often limited to fewer users and lacks features such as role management and real-time data, which are common in dedicated procurement systems like **CostTracker**.

• The risk of version control issues, including overwriting and data loss, is also significant.

• Automating processes is often more difficult using spreadsheets, and cross-project analysis is limited by the need for separate sheets for each project.

• Not always intuitive or user-friendly for everyone, and complex worksheets can become a bottleneck if only a few people understand them. This increases the risk of dependence on individuals, which can be problematic when support or training is needed.

• What if you need help? Unlike the spreadsheets like Excel, several procurement systems offer support that you can rely on when needed.

Mowing forward:

• Carefully assess the needs of your organization to determine if using spreadsheets is still the most suitable tool for your project management.

• Explore alternatives and assess the costs and benefits of migrating to other platforms, systems, or tools. By using dedicated procurement systems like CostTracker, you can streamline processes, reduce the risk of errors, and gain better control over your purchasing routines.

• Involve relevant stakeholders and team members in the decision-making process to ensure that the choice of tool or system supports the organization's goals and needs in the best way possible, and that it is actually utilized.

9. How to simplify purchase approval in your company?

Like driving a car; it can be fun to drive a manual sometimes, but it's far simpler and there's much less to think about with an automatic. Efficiency in the procurement process within projects is vital for cost reduction and workflow enhancement. By implementing tools that automate the approval process, you can save time and resources while ensuring accuracy and compliance with guidelines.

Three main aspects to consider are:

1. Approval of purchase: Clear guidelines and criteria for approving purchases are essential to ensure that only necessary and relevant purchases are approved. By using dedicated tools, you can establish a structured approval process that ensures all steps are followed and there is traceability throughout the process.

2. Process automation: Automating the purchase order processes helps reduce manual errors and enhances efficiency. This includes automatically matching project needs with available suppliers, generating orders based on predefined criteria, and updating information in real-time to ensure all stakeholders have access to up-to-date data.

3. Real-time budget tracking: Some systems also provide real-time budget tracking, where approvers have access to cost commitments within the budget as they approve them. This ensures informed decisions and an efficient process.

By investing in efficient tools for procurement approval and process automation, your company can achieve better control, reduce risk, and ensure a smoother and more efficient execution of projects.

10. How to avoid unforeseen costs?

”The early bird catches the worm.” To avoid unforeseen costs in projects, it’s important to have robust procedures and systems in place to identify and address deviations early. Procurement systems like **CostTracker** can be a valuable resource in this regard. By implementing good practices and utilizing dedicated tools, you can better manage the complexity of project execution and reduce the risk of unexpected costs. As we’ve seen in the previous nine points, successfully completing a project within budget isn’t necessarily straightforward.

It’s also important to acknowledge that even with thorough planning, things can still go wrong. Therefore, maintaining vigilance and having mechanisms in place to swiftly identify and address potential challenges is essential. Communication, information sharing, and regular monitoring of project progress are key components to minimize the risk of unforeseen costs and ensure successful project execution. These are aspects you can easily manage by using a purchase order system!

Summary

We hope this e-book has been helpful in exploring the topic of cost control in procurement practices.

Feel free to reach out to us for more information or assistance in implementing these principles in your business, if you have any questions regarding procurement systems, or if you'd like to test our procurement system. Best of luck in strengthening cost control, and we wish you success in your projects!

CostTracker