



The Cruellest Month

Optimism fades among North American CFOs.

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By Dave Lindorff | From the September 2003 Issue

There was a time when even buying paper for a copy machine was an involved process. There had to be a requisition, an invoice, a check and a receipt, all of which required at least one and often two or more people's time and effort. All of these pieces of paper had to be matched up and reconciled at the end of the day, checked for accuracy, entered into a ledger and ultimately audited.

Ah, the good old days--tedious, costly and wildly inefficient, to say the least. While most companies are light years beyond those bureaucratic nightmares, most would also concede they have a long way to go before they squeeze out all unnecessary costs in managing their payables. Some, however, like BP plc, have been leading the charge.

Save the Trees, Go Plastic

Running an oil company--one that extracts oil from the ground, refines it, transports it around the globe and then sells it retail--is an enormous exercise in record-keeping. At BP, there are more than two million invoices out of the U.S. operation alone. That's a lot of paper to store, log into record books, match up with purchase orders and check for accuracy. It's also a big expense--about a quarter of a billion dollars a year. Two years ago, BP decided that the only way to reduce expenses and inefficiencies was to go plastic.

Pursuing a program started by Arco before its merger with BP in 2000, the oil giant began directing employees to use cards of all varieties--purchase cards (P-cards), fleet cards, payroll cards and of course, the already long popular travel and entertainment (T&E) cards--for most of their corporate purchasing. The results have been stunning. Today, according to Virginia Pope, BP's corporate card manager, a combination of American Express Co. card products and, for T&E, the Diners Club International card, handle 750,000 transactions worth a total of about \$120 million--setting the firm well on the way to a corporate goal of putting one million transactions a year on the cards. The savings? "We estimate that we're saving \$75 to \$100 per transaction," says Pope. That's a total reduction in costs of between \$56 million and \$75 million a year for BP in North America.

BP isn't stopping there. First, it is moving to expand the program to replace paper with card transactions beyond North America. BP is also looking to extend the cards available to its employees and recently adopted a new American Express product called the Corporate Defined Expense Program. This new type of card is designed to be used for purchases related to a specific project, allowing companies to monitor more effectively--and presumably control--costs.

For finance departments, the gradual move to using plastic for corporate purchases of services and supplies is nothing short of a revolution. It has changed the way costs are monitored, data is collected and accounts are reconciled. Admittedly, cards themselves are far from a new phenomenon. What is new are the number of people using them, the size of transactions for which their use is authorized and the types of services and products being purchased. Today, there are P-cards that can buy anything from a stapler to a Lear jet, fleet cards for fuel, repairs and tolls for company cars and trucks, cards to pay temporary employees and cards with pre-set limits to cover the hotel, travel and other allowable costs of relocating executives. These days, an advertising campaign for a product might be completely funded through use of cards with a pre-determined limit.

According to a 2003 study of corporate card use published by RPMG Research Corp., which was co-authored by Eastern Illinois University Professor Richard J. Palmer and Washington University Professor Mahendra Gupta, annual purchasing card use by U.S. corporations alone doubled from \$40 billion in the year ending January 2001 to \$80 billion in the year ending January 2003. Palmer and Gupta expect spending on cards to double again--to more than \$160 billion--by 2008.

But spending isn't the only number on the rise. Annual savings to corporations that have switched purchasing from paper to plastic transactions is already estimated at \$23 billion a year, and Gupta and Palmer predict that by 2007 that number will be closer to \$40 billion.

All three of the major card issuers--Visa International, MasterCard Inc. and American Express--are offering extensive corporate card programs, and for good reason. With the consumer card business at the saturation point, they see B-to-B business as a big growth area. "The B-to-B payment market is about \$11 trillion a year in the U.S.," says Dave Costa, vice president of Visa's commercial solutions group. "Office equipment and supplies, etc., are a significant part of that amount." He adds, "Right now, 86% of that \$11 trillion is still being paid by check."

Steve Abrams, senior vice president for corporate payment solutions at MasterCard (by all accounts, the first to offer a corporate card product outside the travel & entertainment area), reports that MasterCard's corporate card business overall has been growing at a 30% clip since 2001, and he expects it to continue to expand at that pace.

Why? The advantages of cards go well beyond simple transaction cost savings. "Purchasing cards contributed to reductions and redeployments of headcount to higher value-added activities. In addition, [they] resulted in, on average, a 74% reduction in procurement cycle time, a 57% reduction in the number of petty cash accounts

and a 42% reduction in number of suppliers," write Palmer and Gupta. Beyond that, the data gathered via the use of purchase cards, T&E cards and project cards, which the card companies and their issuing banks make easily accessible in all kinds of aggregates and disaggregates, give managers new leverage in negotiating discounts with their suppliers, whether it's an office supply chain or an airline. "Gone are the days when a supplier can get away saying to you that you only spent \$1.5 million this year on office supplies. Now, we can just check the records on card use and say, 'No, we spent \$4 million,'" laughs BP's Pope.

Sky-high Limits

For NCR Corp., that kind of leverage has meant savings, even in Japan, where the company's switchover to purchase cards is only in the early stages. "We have already taken 75% of our suppliers out of the data base," reports Jay Taradash, NCR's manager of global procurement and supplies. "That has allowed us to have more intimate relationships with the remaining suppliers."

One of the most significant innovations in card usage has been in the size of expenditures being handled by cards. Visa's Costa, for example, says the association is offering a product called Visa Commerce that is designed to handle purchases of up to \$10 million. He says the advantage of using cards for large purchases--such as raw materials or capital equipment--is that payment is buyer-initiated. "The card allows you to control the timing and amount of payment--say partial payments in 30, 60 and 90 days, and on receipt of satisfactory delivery," Costa explains.

Ordinary P-card limits for more mundane expenses are also being raised. Two years ago, a company might have set a \$1,000 limit on the cards distributed to office workers for use in purchasing supplies; today that limit may be \$5,000 to allow for purchases of such items as computers or office copiers.

Another major breakthrough that has helped companies realize more savings has been the notion that cards should not be restricted to use by supervisors only. In their study, Palmer and Gupta concluded that high-performance card programs have "a greater number of allowable spending opportunities," have "fewer restrictions on use of the cards," and are "more diligent about training to facilitate purchasing card use."

From the Admin to the CEO

This is when employees making the 5% to 10% of the budget expenditures that account for 80% of a company's paperwork make purchases with cards because there is an administrative cost savings and it allows a company to take advantage of any cost savings the company is able to negotiate with its suppliers. "We started out with a very restrictive card, but it caused so many problems," concurs BP's Pope. "You need to let people make their own buying decisions. It may seem strange, for example, to see a charge for Joe's Scuba Supplies, but it turns out that our people actually use scuba equipment to clean tanks!" She adds, "It's insulting to tell your people that they have to go to a supervisor to get permission to use the card. And we've found that the cards are most effective when they're used at the lowest level of employment--admin and clerical.

Fear of fraud is usually the excuse most finance managers offer when asked why they oppose wider distribution. But the evidence indicates that this is a minor problem. In their study, Palmer and Gupta found card misuse averaged only 0.027% on purchasing cards. Moreover, they found that 70% of card misuse spending occurred at just 4% of the companies surveyed, suggesting, they said, that the problem was with the companies, not the cards. "There is still a fear of having less controls," says Gary Schneider, global business manager for corporate cards at Citicorp, "but actually you have more controls with cards--front end blocks in the codes on what the card can and cannot be used for, and greater reporting at the rear end. You can also look at who's spending more on staples and find out why."

In fact, BP's Pope says that the company's auditors, after looking at BP's card programs, are now encouraging the company that "people should be using the cards more." And let's face it, how often these days do you get that kind of advice from your auditor?

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