

United Technologies: Outsourcing procurement yields high efficiency and tight spending control.

Overview

■ **Challenge**

With its six business units employing their own procurement processes, United Technologies (UTC) was unable to optimize its indirect purchasing across the company as a whole.

■ **Why Become an On Demand Business?**

UTC saw the need to standardize its procurement processes to gain more control over them, but a high degree of decentralization made replacing them costly and complex. Thus, UTC needed to transform its purchasing model on a companywide scale, while minimizing cost and disruption within its business units.

■ **Solution**

UTC engaged IBM to create an outsourced procurement service that fully automated order processing from requisition to invoice payment. Tight integration with business unit ERP systems gives UTC realtime visibility into and control over purchasing activity.

■ **Key Benefits**

- *80% of procurement transactions require no buyer involvement; UTC expects this share to reach 90%.*
- *UTC has saved in excess of \$250 million from its total indirect procurement transformation program.*



With some 200,000 employees, UTC is a global technology corporation with a long history of pioneering innovation in aerospace, aviation, helicopter design, climate control, elevator design and hydrogen fuel cells. Pictured: the Sikorsky S-92.

United Technologies Corp. (UTC) is by all measures an industrial powerhouse. Its six core business units generated revenues of \$31 billion in 2003, making UTC (www.utc.com) one of America's largest manufacturers. A big part of UTC's success derives from the market leadership of its core business units—Sikorsky in helicopters, Pratt & Whitney in aircraft engines, Carrier in HVAC systems, Otis in elevators, UTC Power in fuel cells and Hamilton-Sundstrand in aerospace systems. But as a global conglomerate, the company's success is equally dependent on its ability to harvest the potential efficiencies and economies of scale that lay within its

“It had become clear that we needed to transform our procurement processes, but doing it the traditional way would have been expensive and disruptive. IBM presented us with a solution that gave us all the benefits without the pain.”

—Kent Brittan, Senior VP, Supply Chain Management, United Technologies Corp.

On Demand Business Benefits

- With 80% of procurement transactions fully automated, workflow efficiency and transaction quality have risen substantially.
- UTC has saved in excess of \$250 million from its total indirect procurement transformation program.
- More productive buyers now focus more on strategic sourcing issues and less on solving problems.
- Standardized procurement processes have lowered the share of off-contract purchases, improving UTC's ability to capture volume-based discounts and rebates—and thus lowered overall costs.
- Realtime control over purchasing has raised accountability and discouraged unnecessary spending and lowered supply inventory stocks across the company.
- Procurement as a service from IBM enabled UTC to avoid the cost and effort of implementing its own new systems and processes.

“For general procurement, we needed a system to make corporate deals with strategic suppliers and to drive compliance with corporate contracts.”

—Kent Brittan

worldwide operations. With more than \$14.5 billion in annual purchases, UTC's procurement processes represent perhaps the richest vein of opportunity.

With competition intensifying in the late 1990s, UTC kicked off an exhaustive effort to identify opportunities for efficiency improvements in its procurement processes. Driving the initiative was Kent Brittan, who had been appointed UTC's first Senior VP of Supply Chain Management after serving as CFO in the Otis unit. Brittan envisioned a UTC that employed common sourcing processes across all business units. While UTC had negotiated strategic sourcing contracts for indirect supplies and services (such as travel, office supplies and MRO) across the company, the fact that there were no common control systems in place to enforce these agreements weakened their impact by making it impossible to curtail “maverick” purchasing. Thus, while cost reduction was a clear goal of the initiative, the more fundamental aim was to achieve greater control and visibility within the procurement process. Only then would the company as a whole be able to optimize its procurement processes. And with sourcing strategies optimized, cost reductions would follow.

Taking a cue from IBM

But it didn't take long for UTC to conclude that major barriers stood in the way of this vision. As a result of UTC's decentralized business model, each business unit had deployed its own procurement systems and processes. Consolidating its sourcing processes would require UTC to essentially rebuild them from the ground up and, perhaps more challenging, reshape the entrenched cultures that evolved within each unit. Seeking more palatable options, the company began benchmarking the procurement practices of other large companies. Of the companies UTC reviewed, IBM—which had just completed a sweeping and successful redesign of its own procurement processes—stood out as a near-exact parallel in terms of its core problems and—Brittan suspected—a template for how UTC effectively could address them. UTC approached IBM with a straightforward proposal: “package your procurement process transformation and sell it to us as a service.” Seeing UTC's proposal as an opportunity to capitalize on what had become a major strategic asset, IBM agreed to productize its procurement system and immediately began putting the pieces in place.

IBM's first step was to build a mirror of its own systems infrastructure, which included a mix of standard components such as the WebSphere®

Application Server application infrastructure, DB2 Universal Database and SAP R/3, as well as customized applications like IBM's ReqCat procurement requisition system. IBM eServer p and xSeries servers provided the hardware platform. These systems were then integrated with each business unit's legacy ERP systems as well as key external points such as banks. With the infrastructure and integration groundwork in place, IBM shifted its focus to the meat of the project—the end-to-end transformation of UTC's procurement operations. The goal of this effort was to fully automate tactical purchasing—with little or no involvement of buyers—all the way from requisition to payment.

Transformation through outsourcing

In this phase, a team made up of IBM Business Consulting Services and UTC staff identified and mapped out the range of existing procurement processes, and then systematically replaced them with standardized processes across all units—a process that mirrored IBM's own successful transformation. But it was the way this was achieved that makes UTC's initiative stand out. By outsourcing all elements of its indirect procurement to IBM, UTC was able to achieve a “virtual centralization” of its companywide processes without having to embark on a complex, disruptive and costly investment in its own systems. A review of the details of the solution shows just how thoroughly UTC realized its vision of a completely service-based solution. The foundation of the solution is the complete outsourcing of all hardware and applications as well as application maintenance and support. The latter covers not only ongoing customization and tuning, but also the system changes related to the addition of new companies or facilities.

The heart of the solution is a tactical purchasing service under which IBM buyers source, negotiate and execute contracts and purchase orders for indirect supplies across all UTC business units. IBM also seamlessly handles the accounts payable side of these transactions—right up to the point of payment—and also provides comprehensive support for the thousands of UTC employees using these processes. Before UTC's transformation, its purchasing processes were anything but “hands-free,” with paper-based forms, long manual approval cycles and drains on management time the rule. Now order processing is electronic and automated at every stage. After an employee selects from a catalog, the order is mapped into a requisition, routed to management and—if approved—triggers the issuance of a purchase order (PO) to the supplier. The supplier then sends an electronic invoice that is automatically posted to the SAP application at the core of the IBM system. Once the system confirms acceptable receipt of the order, it then triggers the appropriate general ledger entries into that business unit's own accounting system, and finally payment through the banking system. This tight integration—both within the IBM platform and out to business unit systems—is what makes the UTC solution truly end-to-end.

Key Components

Software

- IBM WebSphere Application Server
- IBM DB2® Universal Database™
- IBM ReqCat
- IBM Lotus® Notes®
- SAP R/3

Servers

- IBM eServer™ xSeries®
- IBM eServer pSeries®

Services

- IBM Business Consulting Services
 - IBM Global Services Service Delivery Center (Poughkeepsie)
 - IBM Business Transformation Outsourcing
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“The biggest savings inherent in this system are the things that never get bought. It forces people to consider and justify their expenditures much more closely.”

– Kent Brittan

At the top of a long list of business results are major improvements in efficiency and control. With the process flow seamless and automated, administrative costs have fallen significantly, a development driven in large part by a huge increase in transaction quality. For instance, the fact that SAP generates POs and receives invoices from the same electronic data origin has made mismatched dollar amounts a thing of the past. This frees buyers from much of the nonproductive task of tracking down blocked invoices and enables suppliers to get paid more reliably. And with buyers freed from troubleshooting, they've been able to focus their time and effort on sourcing tasks, like negotiating and managing supplier contracts. The bottom line is that a more productive procurement organization can handle more "spend" with a leaner, more focused staff. The system has also provided UTC with far greater control and visibility over its spending. In contrast to the rampant off-contract purchasing activity that characterized the old process, the new solution provides the ability to track spending activity from top-to-bottom in realtime. By encouraging purchasing accountability—and having the means to enforce buying guidelines—UTC is now far

better positioned to leverage its purchase volumes. The company's world-class expense ratios and SG&A rates attest to its success in limiting out-of-contract purchases. Another dimension of UTC's increased control is an ability to literally "turn off" spending on specific commodities in response to a management imperative (e.g., the need to preserve working capital), fluctuations in supply costs, etc. The ability to track purchasing more tightly has also enabled the company to streamline its inventory of indirect supplies, thereby minimizing its carrying costs. All told, UTC has saved in excess of \$250 million from its total indirect procurement transformation program.

With a solid track record of savings behind it, Brittan sees procurement as just one part of a larger story unfolding at his company. "United Technologies is engaged in a continuous effort to drive savings to the bottom line by transforming all aspects of the company," says Brittan. "Our partnership with IBM is an essential part of that drive, and we look forward to working in tandem with them toward this goal."

For more information

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