

Smart commodity management

by Patti Magee

FedWatch: Reforming Federal Procurement



PUBLIC WORKS AND Government Services Canada (PWGSC) has started to implement its transformation agenda, *The Way Forward*. Part of that agenda is 'Buying Smarter,' an unprecedented procurement reform initiative aimed at saving \$2.5 billion over five years by leveraging PWGSC's purchasing power; consolidating what the department buys on behalf of the government; and using technology to reduce administrative, compliance and reporting costs. These savings have already been accounted for in *Budget 2005* and reinvested in core federal government programs, placing considerable pressure on PWGSC to 'deliver the goods.'

The establishment of an effective commodity management framework will be critical to PWGSC's ability to harvest the promised savings.

Underpinning 'Buying Smarter' are four main elements: mandatory use of existing standing offers; better pricing; stronger management tools; and modernization of travel. Effective April 1, the use of PWGSC standing offers, where they exist, became mandatory for 10 broad commodity groups or categories of goods and services – information processing and related telecom services and furniture being two examples. In addition to mandatory use of standing offers, all departments have been directed to use their acquisition cards only to make payments and not to procure items. PWGSC expects to have in place standing offers and other such arrangements for over 40 of the most commonly purchased categories of goods and services within eight years.

To realize the savings promised by PWGSC (the \$59M earmarked for 2005-06 has already been removed from departmental budgets) the department is seeking

other departments' support in identifying opportunities for standardization and consolidation. Part of PWGSC's strategy involves working with each department to conduct a spend analysis of their purchasing data in order to generate what PWGSC is calling a 'Harvesting Strategy Action Plan.' Departments in turn will be heavily dependent on PWGSC's ability to negotiate better deals for the government as a whole, make good on the promised functionality of the Government of Canada Marketplace (GoCM) – an e-purchasing tool designed to automate the procurement process and give departments access to an approved catalogue of common commodities at pre-negotiated prices – and strengthen its current commodity management framework.

'Buying Smarter' represents the recognition by PWGSC of the linkages between value for money and effective commodity management. Also recognizing that the department needs to strengthen its current commodity management framework, departmental officials identified the following critical success factors:

- working with client departments to develop plans;
- a rigorous framework for achieving objectives;
- strong governance;
- measuring achievement of objectives and continuously improving processes;
- knowledge of commodities, the industry and its capability; and
- effective commodity councils.

The introduction of commodity councils is an innovative approach to commodity management and a concept that should be actively pursued. The construct, suc-

cessfully adopted in the private sector, offers many fascinating possibilities and at the same time a number of challenges, chief among these being that councils must operate in a complex government environment, characterized by many and often conflicting objectives. But these challenges are worth tackling in the name of improved commodity management.

The councils will comprise industry and government representatives. According to PWGSC, they will be tasked with determining the right balance in purchasing decisions for various commodity groups, taking into consideration efficiency, effectiveness, and impacts on small and regionally based businesses.

One critical challenge in terms of private sector participation on the councils will be ensuring appropriate representation while maintaining the integrity of the process. Another will be in determining how the commodity "pie" should be sliced. For example, will information technology (IT) constitute one commodity group, comprising hardware, software, systems, systems integration, and services, or will more than one commodity group be created? Also, what will the process be for dealing with procurements that by their very nature cannot be standardized, such as procurements that are unique to a department's program needs, e.g., a software requirement that cannot be met through the use of commercial-off-the-shelf software available on a standing offer? These are just some examples of the issues that PWGSC will need to grapple with in designing an appropriate framework for the commodity councils.

When looking at the governance structure, to be effective it must include a clear

mandate aligned with the strategic objectives of both PWGSC and the government as a whole, membership that is representative of both departments and the industry, a clear accountability structure, an effective decision-making protocol – for example, who has the final say; how “exceptions” will be dealt with – and a solid commitment at the highest levels across the bureaucracy as well as the commitment of ministers.

In addition to the critical success factors identified by PWGSC, the success of commodity councils will be predicated on:

- appropriate expertise in areas such as government procurement, law, policy, risk management, economics and finance;
- the integrity of the data used to draw conclusions about supply and demand;
- rigorous data analysis (factoring in data limitations); and
- a process that is transparent and is seen to be transparent.

The councils will collectively need to have a solid handle on both the supply side and the demand side of the equation, and how to strike an effective balance so that price equilibrium is achieved and departments receive the goods and services they need to deliver their program mandates. As mentioned earlier, a spend baseline for each department will be established at the outset by PWGSC, who will be working in conjunction with each department to do a ‘deep dive’ into each department’s spending data – a necessary but massive undertaking given that more than 90 departments are involved – to discern patterns and identify harvesting opportunities. That said, ultimately GoCM data will facilitate the on-going analysis of spending by automatically capturing spending data (the trick for PWGSC will be to treat data in a dynamic rather than static fashion). Information on the supply side such as product intelligence, industrial strategies and emerging goods and service offerings, should derive from PWGSC’s commodity management work as well as from the industry representatives on the councils.

In initiating the work of the commodity councils, PWGSC should focus on quick wins, i.e., examining those commodities amenable to consolidation, where economies of scale can truly be leveraged. Well-

defined, commercially available goods and services are the best candidates for standing offer agreements. As well, in determining the appropriate method of supply for a given commodity or group of commodities, the councils should consider:

- the benefits and risks of aggregation both from a demand and a supply perspective;
- unintended impacts such as barriers to entry and creation of monopolies or oligopolies (and the attendant upwards pressure on prices);
- the marketplace and the effects of different methods of supply on price;
- that potential for economies of scale varies among different markets;
- utilizing PROC analysis (see sidebar) to examine life-cycle costs and optimize the total cost to government (not just the initial purchase price).
- establishing minimum guarantees to reduce the uncertainties associated with standing offers and thus eliminate possible premiums;
- that long term arrangements might not always be appropriate for all commodities, IT information technology products;
- how business should be rotated where more than one arrangement has been established;
- the niche expertise frequently offered by small and medium-sized enterprises, often at a more reasonable price;
- geographic considerations in aggregating supply;
- the form of competition relative to the value and complexity of the requirement;
- establishing capability requirements that strike an effective balance between the essentials necessary to provide assurances that the Crown will get what it needs, and ensuring that criteria are not so stringent as to exclude many SMEs (requirements such as insurance and ISO certification may create barriers to entry for SMEs and could ultimately translate into higher unit costs to the Crown, regardless of the type of private sector participation);
- factors other than just the savings in product cost, such as cost avoidance, cost to acquire;
- the socio-economic implications of the various methods of supply;

PROC analysis considers:

Product cost – direct cost of goods/services, including basic contract price, transportation costs and installation, as applicable.

Resource cost – indirect cost associated with acquiring the goods/services.

Operating cost – the cost of operating, maintaining, repairing, and disposing of the asset throughout its useful life.

Contingency cost – the cost to the end user of not having the right goods/services provided at the right place at the right time.

- various selection methods other than strictly lowest price, which often does not result in best value overall when considering, for example, the total life-cycle cost of a product or the quality of services (“you get what you pay for”);
- utilizing rigorous and consistent methodologies to conduct economic and market analyses and determine the appropriate method of supply; and
- sustainable development issues and methods to acquire the commodity in a manner respectful of the environment.

Given the nature of the ‘Buying Smarter’ initiative in terms of the linkages to broader initiatives and clients’ program objectives, the level of risk and the dollars at stake, PWGSC should consider developing a results-based management accountability framework (RMAF) to facilitate a focus on measuring and reporting on outcomes throughout the life cycle of the initiative. Such a framework would guide the department’s commodity management efforts by providing a roadmap for planning, monitoring, evaluating and reporting on results throughout the life of the initiative. In addition to providing a basis for evidence-based reporting and effective decision-making, the process of developing an RMAF would assure that sound program design takes place by developing a logic model; intended results are clear by developing outcomes statements; and a performance measurement strategy exists by identifying key performance issues and meaningful indicators.¹

Also, what should be added to PWGSC’s list of critical success factors is a compre-

hensive transition management plan – a blueprint for getting from here to there – including, among other things, a human resources plan comprising of a recruitment strategy, a revitalized training program, new competency profiles and gap analyses and learning plans for current staff.

The current cadre of PWGSC contracting officers may not be fully equipped with the skill sets needed to function in the new world order and should not be expected to “morph” into commodity managers in the absence of the appropriate training. In addition, the few individuals who have been dedicated to traditional

commodity management activities in PWGSC generally have not been required to do analyses such as return on investment (ROI), life-cycle costing and cost-benefit, so they too will need to bolster their capabilities. The new competencies for the federal government procurement, materiel management and real property communities reflect the need for procurement specialists to possess functional competencies in these knowledge areas, and Treasury Board Secretariat’s Professional Development and Certification Program intends to develop appropriate training to support these competencies.

PWGSC needs to commit serious funds to the development and delivery of new training initiatives, and to dedicate the time and money necessary to support the community in taking this training. This commitment will be essential to the success both of the certification program and to the department’s ability to leverage its commodity management activities to achieve the desired savings. ~~~

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