

# Local Government e-Procurement Strategy Report – Management Summary

April 2003



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## Acknowledgements

**This strategy report was written with the assistance of a cross-functional team comprised of local authority staff from the e-procurement pilot sites of Cork County Council, Cork City Council, Dublin City Council, Kerry County Council in conjunction with staff from the Department of Environment and Local Government. The first draft was completed by the Local Government Computer Services Board and was reviewed by a working group that included a number of County/City Managers. Following a quality assurance exercise, the final report was drafted by IBM Global Services and approved by the CCMA on 17<sup>th</sup> April 2003.**

## 1 Overview

Arising from the national eProcurement strategy for the public sector in October 2001, the local government sector initiated a project to develop a sector level eProcurement strategy. The purpose of the strategy is to identify a set of key changes and an implementation plan that will guide the development of eProcurement in the sector so that significant savings can be achieved by exploiting the opportunities for improving procurement performance.

In order to reap the benefits of eProcurement, it is essential that there is a base of good procurement practice in place. Much of the focus of this project has been on procurement practice, and the organisation and systems needed to support it.

It is estimated<sup>1</sup> that the total revenue expenditure in the local government sector in 2002 is approximately **€3bn**. Of this total amount, the net procured expenditure (with staff costs and non-procured items removed), is estimated<sup>1</sup> at **€1.3bn**.

The financial benefits to be realised from the successful implementation of the initiatives in the report are considerable. It is estimated that achievement of the targets set in the strategy will achieve a cumulative saving in revenue expenditure alone of about **€172 million** over the implementation period of the strategy with recurrent savings in excess of **€60 million** per annum once the strategy has been fully implemented. The savings will arise primarily from

- More effectively leveraging the buying power of the sector through aggregation of demand
- Increasing the proportion of expenditure procured under contract,
- Reducing transaction and supply chain costs.

Successful implementation of the eProcurement strategy will be of benefit to the sector as a whole, to individual local authorities, and to our suppliers:-

- Improved procurement will result in savings for each local authority which will be available for reinvestment to improve and increase the services provided.
- Improving, standardising and automating procurement processes will be of benefit to local suppliers, as more efficient communications will make it less expensive and less complex for them to do business with local authorities, especially for those who deal with many different authorities.
- Suppliers doing business with local authorities will benefit from the introduction of eProcurement by local authorities through the development of their eCommerce capabilities, enabling them to compete more effectively in the modern economy.

Realising the potential benefits will require a quantum change in the way procurement is organised and managed, and in the skills and disciplines used for procurement. It is essential that local authorities are provided with the support and advice needed to achieve this. The strategy recognises the need for this to be co-ordinated at sector level to ensure that the required practices, processes and systems are developed and then rolled out in a consistent manner across the sector. To meet this need, local authorities will establish a unit to provide procurement co-ordination and support services. This unit will be called the Local Government Procurement Support Service (LGPSS), and it will be located initially in the Local Government Computer Services Board.

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<sup>1</sup> Full details of the process used to calculate the estimate can be found in Appendix 3 of the main report

For the strategy to be successfully implemented, each local authority will be need to participate in local, regional and sector level initiatives. Each authority will designate resources to take responsibility for procurement at local level, and to liaise with the LGPSS. In conjunction with the LGPSS, each authority will prepare its own action plan setting out the key initiatives to be undertaken at local level as part of the strategy.

Change on the scale required cannot be introduced overnight. The strategy envisage a timeframe of seven years for completing the transformation. The changes will be introduced on a gradual, incremental basis, with individual initiatives being carried out on a pilot basis by individual authorities, and rolled out across the sector as the benefits are proven. In this way, savings generated through early initiatives, can be used to fund the further investments required. An initial 'Demonstration and Capacity Building' phase will be incorporated into the implementation plan to ensure effective communication of the strategy to local authorities and to show the benefits to be achieved from the proposed approach to procurement prior to the full implementation of the strategy across the sector.

### **Scope of the Strategy**

While the scope of the study embraced the procurement of supplies, services and capital works, the main focus of the recommendations is in the area of supplies and services. While some of the principles and conclusions in the report are applicable to capital works, the report recommends that further study is required in order to address the specifics of procurement in this area, and to develop a detailed improvement plan.

### **Approach to the Project**

The project was divided into three main phases, the first of which involved a review of the current procurement environment in the local government sector to identify the issues and opportunities that should be addressed. In the second phase, these issues and opportunities were analysed, priorities were established, and a set of principles agreed in relation to the procurement practices, organisation and systems which would be required to support the development of procurement in the sector. In the final phase an implementation approach and actions plans were developed.

To support the analysis and development of recommendations, a consultative group was established. The group comprised representatives from four pilot local authorities, well as representatives from the LGCSB and the Department of Environment and Local Government.

## **2 Current Procurement Environment**

The review of the procurement practices and processes in the sector indicates that there are significant opportunities for improving procurement performance. The following are some of the review's main conclusions:

### **Procurement Organisation and Management**

- Dedicated procurement structures are not generally in place in the local government sector and where they do exist they are concerned primarily with regulatory compliance rather than the provision of strategic value adding procurement activities such as strategic sourcing and contracting. No one is responsible or accountable for leveraging the significant purchasing power of the sector or for managing the effectiveness of procurement performance at either a local authority or sector level.

- There is a severe shortage of procurement skills and expertise in the sector, particularly in the areas of supplies and services. Most local authorities do not have dedicated procurement staff, and no programme currently exists for the training and development in procurement-related skills.
- In general there is limited coordination of procurement between local authorities and outside of large projects, the existing structures are not equipped to facilitate cross-agency co-operation. This has led to an avoidable duplication of activities, resources, structures and systems.

### Procurement Practices and Processes

- While procurement policies and procedures exist, they focus primarily on ensuring regulatory compliance and there is a need to produce comprehensive guidelines to ensure that good procurement practices are being developed and implemented by staff involved in procurement activities.
- Local authorities recognise that there is a need to adopt a strategic approach to the analysis of categories of spend across projects, programmes, local authorities, regions and the sector as a whole and that the planning of revenue expenditure could be improved ensuring that effective linkages exist with the planning process for service provision.
- In general there is very limited aggregation of procurement requirements although there are some examples where aggregated contracts have been put in place (e.g.: PCs and software) which have demonstrated real savings (up to 65% saving on some software costs) to the sector. There is significant opportunity to more effectively leverage the buying power of the sector through aggregation of demand requirements within and across local authorities at project, programme, local authority, region or sector level.
- Approaches to tendering and contracting are inconsistent across the sector and there is a more integrated approach to the evaluation of 'make versus buy' decisions needs to be adopted across the sector.
- The review has identified the need to improve the approach taken to contract monitoring, so that the level of off-contract or 'maverick' buying taking place can be understood and measures taken to address it as necessary.
- In general more attention needs to be paid to proactively identifying the most appropriate ways to increase levels of competition in the supply base where this is an issue.
- Local authorities have developed coding and classification standards on an individual basis and it is recognised that this approach is not adequate to ensure the required visibility of procurement management information or to provide a mechanism for allowing local authorities to access combined contracts.
- Formal approaches to the management of supplier performance are not generally in use.
- The management of inventory in many cases appears to be determined based on historical usage and not directly linked to any planning processes associated with service delivery. Inventory management and logistics infrastructure appears to be fragmented across the sector with little coordination at programme, local authority region or sector level.

### Systems and Technology

- There has been significant investment in financial management systems within local authorities over recent years and in general, manual activities such as raising purchase orders have been automated. However, it would appear that the full benefits of this technology are not being realised in all areas.
- A pilot undertaken to automate the request for quotation process has been successful in demonstrating potential cost savings and the willingness of suppliers to participate electronically.

- Electronic integration exists between suppliers and local authorities to varying degrees and in general, capabilities for electronic payment are available, with pilots being undertaken in other areas such as the transmission and receipt of electronic invoices.
- The national eTenders solution is being used by buyers across the local authorities for publishing tender notices and this has proved successful, resulting in significant savings (up to 75%) over the traditional newspaper based advertising process.
- An extranet is in place which allows all local authorities to access centrally hosted applications, but as yet, there are no central applications to support the collation of information for procurement.
- The local authorities are in a good position to exploit the opportunities that technology provides to maximise the benefit from eProcurement, and the Financial Management Systems (FMS) in place are in general capable of providing the building blocks for e-procurement with extra required functionality such as catalogue management provided through specialised solutions.

### 3 Strategic Objectives

The development of the strategy was guided by a set of agreed objectives for procurement in the local government sector.

The overall strategic goal for procurement is to effectively support the provision of local authority services. The major objectives of the procurement function are to provide the quality of service required to support local personnel in the provision of services, to make the most effective use of available funds and to ensure compliance with relevant national and European procurement legislation.

In line with the eProcurement Strategy for the public Sector, further objectives have been identified as follows:

- To improve service levels to buyers, suppliers and users involved in procurement.
- To minimise the transaction costs associated with procurement
- To develop a more integrated approach to procurement across local authorities.
- To maximise value for money by enhancing the buying power of the local authority.
- To promote competition among suppliers while maintaining reliable sources of supply.
- To optimise inventory levels through the adoption of efficient procurement practices.
- To make effective use of human resources in the procurement process.
- To improve the auditability of public procurement expenditures.
- To be progressive in the adoption of procurement Information and Communication Technologies (ICT).
- To encourage the supply base in the adoption of eProcurement practices and technologies.

### 4 Targets for Procurement

The report recommends targets for improvement in procurement performance, which the local government sector should set out to achieve over a seven year period. The key targets proposed are as follows:

- Reduction in the average unit cost amounting to 3% of total expenditure
- Reduction of 25% in the total transaction cost
- Reduction of 15% in the total number of procurement transactions

Other more detailed targets have also been set out in the strategy, and in particular targets are proposed for the degree of procurement carried out through eProcurement

The significant potential savings identified in the report below are based on the assumption that, by the end of the seven year period of the strategic plan, these targets will have been achieved.

The targets chosen are considered realistic and achievable and are based upon international experience. They reflect the low-end range of cost reductions claimed, or projected in both the private and public sectors internationally.

## 5 Benefits

The financial benefits realised from the successful implementation of the strategy recommendations arise primarily from increasing the proportion of expenditure procured under contract, leveraging the buying power of the sector and reducing transaction and supply chain costs. It is estimated that achievement of the targets set in the strategy will achieve a cumulative saving of about **€172 million** over the implementation period of the strategy with recurrent savings in excess of **€60 million** per annum once the strategy has been fully implemented (from FY2009).

In addition, the non financial benefits associated with the implementation of the strategy include:

- Improved quality of services arising from more efficient and effective requisitioning and ordering processes
- Improved job satisfaction through reductions in the time required for procurement administration tasks
- Greater efficiencies in the supplier base from improved and automated procurement processes for suppliers
- Significant contribution to overall national competitiveness as a result of the more effective use of funding
- Promotion of the use of eCommerce for both local authorities and their suppliers

The national eProcurement strategy, approved by the Government, has recommended that budget savings from exchequer funds arising out of a coordinated and committed approach to improved procurement should be available for use in augmenting and improving front-line services provided by the agencies concerned. This will provide local authorities with a clear incentive to achieve or exceed the proposed targets.

In order for this approach to be successful, it is necessary that these savings are clearly identifiable and can be shown to genuinely improve value for money in the provision of services. The mechanisms for tracking procurement performance set out in this report should be used as the basis for ensuring that this is achieved.

## 6 Key Changes Required

The report identifies many changes required in the areas of procurement practices, organisation and technology which are focused on leveraging the buying power of the sector, improving transaction efficiency, creating a sustainable and competitive supply base, and providing effective inventory management and logistics arrangements. The strategy recognises the requirements of the regulatory and economic environments in which procurement operates, particularly the need to ensure consistency with national economic policies in relation to regional development and the SME sector. The key changes identified in the report are set out below:

## Procurement Organisation and Management

- It is essential that resources exist at sector level in order to ensure the effective implementation and coordination of the eProcurement strategy. A sector level unit (working title Local Government Procurement Support Service - LGPSS) will be established with responsibility for leading sector level initiatives and the provision of expert procurement support and advice across the sector. Initially this will be set up as an interim unit with minimal resources in order to mobilise the implementation of the initiatives contained in the report. Any increase in the size of this unit will be justified based on the savings and benefits realised.
- The LGPSS will contain a small number of skilled procurement practitioners who will provide services to local authorities, probably on a regional basis, to support them in implementing professional procurement approaches, particularly in the area of category management and contracting. This approach will be piloted in one region prior to rollout to the rest of the sector.
- Local authorities will designate a resource to coordinate procurement activities. While in many authorities this will not be a full time role, some of the larger authorities may require more substantive arrangements.
- An integrated approach to training, change management and communications will be put in place by the LGPSS and maintained across the local government sector to promote and support the development of the procurement skills and behaviours required to effectively implement the strategy.

## Procurement Practices and Processes

- The LGPSS will be responsible for the development of strategies and priorities for procurement in the sector. It will determine the relative significance and priority of each category of procurement, so that they can be appropriately managed, either at sector or local authority level.
- In identifying the most appropriate way to purchase a particular category, an individual category strategy will be developed which identifies the objectives to be achieved for the category as well as the procurement approach to be taken in order to maximise value, quality and service.
- In developing category strategies, opportunities to aggregate demand requirements at programme, local authority, region and sector level will be explored
- Category strategies will seek to optimise the supply base for the relevant category and will incorporate measures to ensure that an adequate level of competition exists in the supply market.
- Sector level policies will be developed and rolled out to local authorities to provide a framework for implementing good procurement practices across the sector.
- Strong linkages will be developed between procurement and the planning processes for the provision of local government services so that demand for categories of spend can be more effectively identified.
- Coding and classification standards will be developed and implemented as category strategies are rolled out across the sector.
- Frameworks for procurement performance management and supplier performance management, incorporating appropriate objectives measures and targets, will be developed and implemented.
- A continuous improvement programme will be initiated to ensure that the efficiency and effectiveness of procurement processes are maximised on an ongoing basis.
- A programme will be developed and implemented to educate suppliers and encourage their participation in local authority procurement.
- A sector wide review of inventory management and logistics will be carried out to identify opportunities for rationalisation and integration in order to optimise service and quality and reduce unnecessary costs.

## Systems and Technology

- An eCommerce and Catalogue Management hub will be provided to support local authorities in providing electronic ordering, invoice transmission and payment facilities. This will link existing financial management systems directly to suppliers' systems, and allow local authority staff to select items for which contracts exist from an online catalogue.
- The local government sector will continue to use the national tender management facility
- An automated request for quote (RFQ) facility will be provided to increase the efficiency and effectiveness of the existing quotation process.
- A local authority Procurement Portal will be implemented, consistent with any national portal being designed and implemented to provide access to procurement information and systems.
- Procurement processes will be automated where possible and systems support for procurement activities such as tendering, ordering, receiving, inventory management and supplier payment will be maximised
- The national supplier register proposed in the eProcurement Strategy for the Public Sector will be utilised for gathering supplier information and providing a single supplier identifier.
- A central management information system will be implemented to support reporting and analysis of procurement information across the sector.

## 7 Costs

The cost of implementing the initiatives recommended in the strategy is estimated as **€17 million**. This is the amount which will require to be spent over the seven year period of the strategy. It includes the salary and overhead costs for new positions recommended, as well as the hardware, software and external resources required. The cost estimates related to technology solutions are based on limited information since the nature of the solutions, and the costs of hardware, software and implementation can only be determined following further detailed study.

## 8 Investment and Funding

Based on the level of savings identified in the first four years of the strategy, the report indicates that an investment of **€22 million** could be justified and would reach breakeven over that four year period. This is significantly greater than the costs identified over that period. However, as highlighted above, there is a degree of uncertainty in relation to the technology solution costs and consequently it is important that any investment proposals take this into account. If the savings projected in the first four years of the strategy are achieved, then it is anticipated that further investment at the same rate (**i.e. €10 million per annum**) would achieve the savings projected in the final three years of the period (2007 to 2009). However any investment beyond the initial period should be based on a review of the initiatives implemented during the initial four year period and should assess the cost effectiveness of these initiatives by looking at the actual savings delivered in relation to the costs incurred. The strategy also needs to recognise that priorities and circumstances can change and it must be flexible enough to adapt to any such changes and ensure that investment is being used in the most effective manner to generate savings.

With this in mind, the following approach is proposed to the funding of the strategy:

- A fund of **€22 million** be set aside and ring-fenced to cover the first four years of the strategy
- Costs of recommended new positions, in the first four years of the strategy, be borne by this fund
- Allocation of funds for the initiatives recommended in this report be on the basis of individual business cases, showing their contribution to the achievement of the savings and other benefits envisaged in this report;

- Determination of the size of the fund for years 5 – 7 should be based upon a review of the progress in achieving savings to the end of year 4
- The annual programme budget to be based upon the totality of approved business cases, and the cost of resourcing the new positions recommended;
- Overall programme funding should be inextricably linked to the delivery of savings

As part of the demonstration and capacity building phase of the strategy, the local authorities will identify the most appropriate funding mechanism to put in place for the sector. This will need to address the following key issues:

- Determination of the basis for contribution to the fund at central level and by individual local authorities
- Identifying the degree to which savings obtained through improved procurement performance will form an element of contributions to the fund
- Assessment and prioritisation of initiatives to determine the most cost effective use of available funds
- Development of structures and mechanisms for managing the fund on an ongoing basis

It is proposed that the local authorities will contribute €1 million (50%) of the costs of the demonstration and capacity building phase and that the most appropriate mechanism for implementing this would be through the use of a general or central source of finance. At the end of this phase an evaluation of the eProcurement strategy will be carried out and it is proposed that the nature and extent of further funding would be based on the outcome of this review.

## 9 Implementation

The strategy incorporates a set of initiatives which are designed to ensure that the key changes identified in the report are effectively implemented over the specified timeframe. The implementation approach to be adopted for this strategy is incremental with investment and roll out of initiatives based on proven results and savings realised.

The implementation plan is based on pilot projects which will be used to prove concepts such as category management and supplier management as well as testing technical solutions such as the request for quote system. These pilot projects will be used to demonstrate the savings that can be achieved and to justify the roll out of procurement practices, processes and systems across the sector. In general, new procurement practices will be incorporated and piloted as part of category strategies and will be implemented in a phased approach as the category strategy is adopted by local authorities and as more categories are managed in this way.

The report incorporates an integrated implementation plan which outlines the initiatives required to implement the strategy including the timing and sequencing of the initiatives. It also highlights the immediate actions required as well as the risks, assumptions and challenges associated with the implementation of the strategy.

The implementation of the strategy will be divided into three main phases as follows:

### Demonstration and Capacity Building

A key element of the implementation plan for the strategy is the demonstration and capacity building phase which will last until the end of 2004 and which will be focussed on creating awareness across the sector of the

opportunities and benefits of the procurement strategy. During this period, key concepts and solutions will be piloted and reviewed to demonstrate benefits and optimise approaches. This phase will lay the foundation for the subsequent mobilisation and implementation of the projects and initiatives incorporated in the overall plan

This initial 'Demonstration and Capacity Building' phase will be used to demonstrate the benefits arising from key concepts in this report such as the use of category strategies. An evaluation will be carried out at the end of this phase to identify the benefits achieved and to determine if the implementation of the strategy will proceed as planned. The immediate actions required during this phase are identified below

- Establishment of the interim LGPSS
- Approval of strategic objectives and targets
- Obtaining and setting aside the recommended funding
- Recruitment of resources
- Sector communications
- Capital works procurement study
- Local authority action plan
- Key technology pilot projects (e.g.: RFQ, catalogue management, data warehouse)

### **Mobilisation**

Following the review point at the end of the 'Demonstration and Capacity Building' phase, the mobilisation phase is designed to put in place the main elements of the strategy so that it can be rolled out across the sector. During this phase, procurement standards, policies, procedures and performance management frameworks will be put in place and further category strategies will be developed at sector and local authority level. The organisational arrangements will be developed to provide the required levels of support at regional and local authority level. Technology initiatives will be developed based on a review of the pilots implemented during the demonstration and capacity building phase. It is anticipated that the mobilisation phase will last until the end of 2005.

### **Implementation**

Once the mobilisation phase has been completed, the implementation phase will concentrate on further development of the procurement environment in the local government sector by ensuring that the proven concepts and benefits are rolled out across the sector.

The implementation plan on the following page provides an overview of the key initiatives to be implemented in each of the phases

