Building the case for centralisation in public procurement
In May 2006, CIPS Australia hosted the inaugural Public Sector Procurement Forum (PSPF). This conference was dedicated to public sector procurement and many of the current issues it faces. Over 130 people attended this successful inaugural event.

The PSPF was in reality a sequential step for CIPS Australia in pursuing its strategy of full engagement with the public sector procurement community. CIPS has a long history of working closely with the public sector in a number of countries. Most notably in the UK where thorough engagement with the public sector at many levels has led to the formation of the Public Sector Faculty (PSF) – a formal umbrella structure to support all of the public sector procurement community serviced by CIPS.

Paul Hopkins, Deputy Director-General NSW Procurement of the NSW Department of Commerce is one of the number of speakers who made a lasting impact at our PSPF event. His presentation challenged people to reconsider the prevailing public sector paradigm supporting decentralization as the best approach to effective procurement in the public sector. He argued for more balance towards centralization, resulting in greater benefits for everyone. It is rare in modern professional conferences for a speaker to receive tumultuous support as Paul did last May. Consequently, we asked him to represent his speech in the written form of this booklet.

Of course, there are lessons here that the private sector can also benefit from. There are stark similarities between the challenges faced by largely decentralized public procurement agencies within the jurisdictions and large matrix organizations in the private sector.

Finally, thank you to Paul for taking the time and trouble to present his work on several occasions for us this year. Neither Paul nor CIPS Australia see this argument as definitive, but rather the start of a meaningful debate to which we will welcome your contributions at any time.

Jonathan Dutton MCIPS
Managing Director,
CIPS Australia
What is centralised procurement?

A case for the centralisation of public procurement

The acquisition of goods and services is a fundamental activity that underpins business operations. The need for a procurement activity has never been questioned, but how and where it should take place and what influence the function should have on business is regularly discussed.

Centralised procurement is a process where one government organisation, representing the collective needs of other departments, carries out procurement functions.

The key arguments for centralised procurement include:

- The ability to leverage significant reductions in prices;
- Better services at lower costs and increased purchasing power;
- Technical and environmental standardisation;
- Improved contract management and problem resolution;
- Lower training costs;
- Easier performance management of procurement staff; and
- Improved transparency, reporting, management and audit trail.

Another major benefit of centralised procurement is that it increases the organisation’s ability to professionalise procurement, due to being able to recruit/develop its procurement people as specialists, and ensure that good procurement practices are applied appropriately.
What is decentralised procurement?

The rationale of a decentralised approach is that by placing the procurement function closer to the needs of the final user, it is more likely to be an economically efficient business, produce more effective business outcomes and better promote the development of the private sector through use of local suppliers.

The key arguments for decentralised procurement are:

- Reduced opportunities for corruption
- A closer match to end-user requirements
- Reduction in scope for large-scale error and unnecessary over-spending
- Less bureaucracy
- Shorter time frames
- More opportunity for SMEs to compete for contracts;
- More opportunities for lower prices from local producers; and
- More scope for personal responsibility and a ‘service mentality.’
Historically there has been tension between the perceived benefits of centralised and decentralised public procurement. Historically this has brought about regular changes in procurement practice. These changes are normally forced by financial realities and community pressure, as well as market innovation and change. Reacting to change has had a tendency to make the government procurement professional less focused on acting strategically.

In recent times, managing the growth in market globalisation (demonstrated by the emergence of free trade agreements), is causing a push towards a centralist approach to procurement. Continuing outsourcing trends and a focus on ‘core’ business has had an equally decentralising influence. Market theory supports the efficiencies driven by competition. Its rationalist influence heralded the rise of the Government Trading Enterprises and State Owned Corporations and, consequentially, more pressure for a decentralised approach to whole-of-government procurement. The emergence of e-Procurement has pulled procurement back to the centre again, while releasing control of the purchasing activity to the buying entities.

These trends have heralded some wild swings between centralised and decentralised approaches. Such changes have meant that the government procurement functions have tended towards a reactive rather than planned approach to their operations.

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Figure 1: The difference between a centralised and decentralised approach
What is not working effectively in the reactive decentralised public sector model today impacts negatively on costs tomorrow. Some examples of current inefficiencies are:

**Multiple instances of the same ERP software**

One jurisdiction has 24 instances of a particular brand of ERP, creating a need for a significant upgrade. That means millions of dollars of costs every eight weeks to upgrade a system. This is the result of several agencies individually being expected to manage their IT solutions.

**Individual chart of accounts**

Most governments do not have a chart of accounts across their agencies that is common. Thus making it more difficult to gather sufficient information and see all expenditure across the sector. As a consequence, opportunities to aggregate, standardise and collaborate and save money are often lost.

**Competing against ourselves**

Most local supply markets in Australia are small. This can mean that many government agencies can unknowingly compete against other government agencies for the same resources. This joint demand could force the price up as a consequence of non-centralisation.

**Fragmented recruitment levering**

A reliance on external recruitment services could reduce the opportunity to leverage governments' scale and capture information for re-use and re-analysis.

**Infrastructure sharing**

There is often a duplication of effort and cost in relation to procurement infrastructure and resourcing. Approximately 8,000 NSW public servants identify themselves as being involved in procurement at some level. 6,000 of these people say the majority of their work is in a procurement activity and 2,500 people say they undertake procurement exclusively on a full-time basis.

**Sub-optimal volume leveraging**

If one large agency tenders separately, because they believe that they can secure a 'better deal', this can reduce the 'whole-of-government volume, which in turn could result in increasing the net cost to whole-of-government for that particular area.
Poor standardisation across the sector

Non-standardised PCs, printers, copiers etc. can result in multiple interfaces and multiple costs, reduced rationalisation and reduced product leveraging.

Non-committed contracts

Keeping the option of choice alive in government heads of agreement contracts, but not committing expenditure volumes or preferring multiple vendors, can reduce the ability to negotiate and can increase tendered prices. Not being able to speak on behalf of the government in committing volume to a contract means that the supply agreement is reduced to an ‘opportunity contract’ and savings can consequently be reduced.

Because of the sorts of issues outlined above, ‘networked centralisation’ is again being considered for public procurement. The business environment has changed, due to technology and market delivery of services, which reduces the perceived reliance on a decentralised approach. The propensity towards centralisation has eventuated because it is seen as providing a greater value opportunity for all stakeholders, including the community.
Most public procurement activity today is typically decentralised, and is delivered via centrally managed frameworks. The result is a mixed procurement model - a “guided decentralisation.”

Public procurement across Australian jurisdictions follows a similar approach; with the establishment of procurement practice guidance. This occurs via legislation, policy, central governance structures, sector access to central systems and the availability of ‘common use’ whole-of-government contracts.

For example, central and eastern European governments conduct public procurement on a highly decentralised basis. Many of these countries have established public procurement offices that are not responsible for actual purchasing, but which set national policy, organise training and draft legislation. This represents a change from the ‘central monopoly’ procurement systems of forty years ago. The purchasing function itself has been decentralised to hundreds sometimes thousands of procuring entities.

Although these frameworks have a ‘centralist’ approach, it is not actually the centralisation of procurement as such. Instead, the central frameworks act as a guide or a commercial alternative; they are not a required process or mandatory activity. In other words, government is saying “we’ve set up these central frameworks to help you if you want to use them.”

For example, the NSW Government has spent millions of dollars establishing “Smartbuy” (one of the best e-Procurement solutions in the country). However, if it isn’t being fully utilised or procurement professionals do not know how to use it (or choose not to use it) it undervalues both the procurement approach and the investment. The under-utilisation of such central systems can result in procuring entities remaining

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Figure 2: Central frameworks within government procurement areas
Source: NSW Department of Commerce Survey April 2006
decentralised in the process and act as transaction management agencies.

Often agencies have invested replicating system capability. Networked access to central systems allows for greater efficiency, transparency and improved data capture for government spend and strategic analysis, while still allowing the procurement professionals to exercise their own judgement when considering the type, qualities and the timing of the required purchases.

This broad schematic, though very generalised, illustrates the following:

All Australian governments have forms of central frameworks for influencing decentralised procurement. While all are individual in their application, they are also similar (including when their frameworks operate less successfully). Also Australian governments have routinely failed to ensure that decentralised procuring agencies/entities actually possess the requisite skills and technology necessary to undertake the procurement task effectively.

Historically, there has been a failure to grasp the fundamental importance of procurement in managing organisational costs and, correspondingly, the development of the procurement skills and systems required to adequately support them.

Conversely the private sector, more recently, is adopting a more centralised procurement solution more frequently. A random web search on private sector organisations globally, reveals a consistency in private sector thinking on a move to a central approach in the management of procurement. This is because the sector has repeatedly demonstrated it saves and maintains reduced costs through improvements in the following areas:

- Aggregation
- Shipping consolidation
- Closer supplier relationships
- Uniform processes
- Leverage scale
- Corporate governance
- Internal controls
- Visibility of transactions and process
- Ethics
- Data maintenance and management

The private sector has bounced back more quickly from the economic rationalist model of the 1980s, with lower levels of central intervention, to more centrally-managed and delivered procurement services.
Private and public procurement: What is the difference?

While procurement practices overlap in the public and private sectors, the fundamental objectives underpinning those procurement practices, will often differ because the business environments in which they operate differ.

While both may use similar techniques, their applications will differ due to the fact that they each have different intents. The current public sector decentralised approach to procurement is much more directed to meeting community needs at a local level, both economically and in services delivery. This approach uses more locally tailored solutions where the output and delivery of the service is focusing on ‘speed and fit’ to the immediate community. This approach looks internally and has a business unit perspective to the needs of its customers.

The more centralised approach of current private procurement is more about working with standards at a global level to optimise pricing and achieve a level of consistent assurance for the procurement across the organisation. It has a broader external market view and operates with a more business-orientated perspective.

Frequently this comes down to the choice of ‘perceived effectiveness’ over ‘perceived efficiency’: A centralised approach is more about efficiency leading to effectiveness, whereas a decentralised approach illustrates that if your procurements are effective then they must be efficiently delivered.

This different thinking manifests itself naturally through the significant differences in the context of public and private procurement in the following significant ways:

- Breadth of requirements,
- Range of stakeholders, and
- Complexity of the processes involved.

Within public procurement, the community is the stakeholder and government is the executive office. It supports national social agendas delivered at a local level. Public procurement has greater community expectation for:

- Probity and transparency,
- Fairness and ethical behaviour,
- Community responsiveness, and
- Environmental awareness and sustainability.
Within private procurement, the shareholders are the stakeholders and the company board is the executive office. It supports financial objectives delivered through dividends to shareholders. Private procurement generally need to:

- Meet only its legal requirements under the law
- Operate more confidentially
- Operate in its own interest
- Be responsive to the community it has targeted; and
- Consider that environment management is potentially marketing.

Defining value in terms other than dollars is also a characteristic of public procurement today. If governments want to use procurement to help meet policy objectives, then these have to be factored into the definition of ‘value for money’. Examples include: sustainable development, SME policy, regional development policy and the various free trade agreements.

So, whilst both sectors seek ‘value-for-money’, it is measured differently: Public procurement success is often measured against a “triple bottom line” of financial, social and environmental performance, whereas private procurement is generally measured against a single financial bottom line performance.

Having said that, there are still core procurement competencies that are equally relevant in both the public and private sectors. These include:

- Project management.
- Analytical skills.
- Understanding of the markets (generally, as well as individually).
- An ability to define value in terms that include ethics, values and policy.
What is the right approach?

Historically, the public sector took a more paternalistic approach to management generally (before the advent of e-Procurement) and have adopted a more centralised approach for effective management of procurement. However, more recently, the public sector has moved towards the decentralised approach in order to deliver more effective procurement outcomes that directly reflect immediate community concerns. However, some things that have remained consistent in public sector procurement are the following:

- Poor information on expenditure,
- Poor procurement skills deployment,
- Poor procurement infrastructure, and
- Poor performance and contract management.

As a result of the above, public procurement is traditionally more process-based than skills-driven - with an emphasis on risk avoidance rather than outcome benefit. Public sector senior management has seen procurement as ‘functional’ rather than ‘professional’. Unfortunately this attitude can often cost the government (and therefore the community) money, as the government’s opportunities of scale are not optimised.

This can amount to a lot of wasted or duplicated effort being put into initiatives to no avail, because others within an organisation do not appreciate what procurement professionals are doing or what can be achieved. Consequently, a public procurement staff member’s opportunities may be reduced to react to issues, as opposed to building strategic forward solutions for the organisation’s businesses.

These differing objectives and support levels between public and private procurement are highly relevant when demonstrating why the centralised approach, generally employed within the private sector, has lately had a low acceptance rate in the public sector.

However, times have changed again - particularly over the last 5 years. As the technological revolution has matured, the business environment has evolved in the following ways:

- ERP (Enterprise Resource Planning) systems have improved business intelligence.
- Web technologies have opened up system access.
- Mobile technologies have sped up communications.
- Business services have been commoditised by the market.
- Operational processing has been outsourced.
- We have more information generally on markets and products.
- There is increasing professionalism in the procurement disciplines across all sectors.

That is, the contextual complexities of public procurement that once favoured decentralisation are now being addressed by factors such as IT innovation, increased information availability, an increased reach across the supply chain, increased professionalism and up-skilling of procurement practitioners, and an increased focus by executive management on procurement operations and opportunities.
However, much of centralised procurement today is the ‘tail end’ stuff. i.e. it isn’t those acquisitions that exercise the minds of the heads of departments. In other words; the centralised procurement group has an opportunity to add value in areas that heads of departments don’t consider to be ‘strategic’.

Procurement has been broken up by the profession into strategic sourcing, strategic procurement, logistics, purchasing, warehouse management, supply chain management, and accounts payable – all being undertaken in their own area with limited overlap. It is often fragmented and/or subsumed by other business disciplines such as finance or operations. The more that expense management control is fragmented, the more effectiveness and the scale of the benefits achieved from the process are diminished.

**Figure 3:** Procurement operates across business operations

**Figure 4:** Procurement is being seen as the one discipline of “expense management”
Procurement now operates fully along the length of business operations. Its core competencies and values are increasingly being recognised. Functional expertise of supply chain management has often been segmented, but now it is increasingly being seen as one functional discipline of “expense management”.

Consequently, centralised approach to procurement delivery today provides a better value opportunity for the public sector than the decentralised models. This is not to suggest that the whole procurement process should become centralised - that would be a step backwards - but rather that the pendulum is swinging back towards the increased use of centralised mechanisms. These mechanisms include: requiring the use of particular whole-of-government contracts; mandating certain process steps; compliance in the use of central e-procurement tools; and the general collective sector support of whole-of-government strategic procurement objectives.

Implementing central processes enables agencies to focus their limited procurement resources away from process management to the areas of strategy and maximum procurement benefit. After all, why duplicate? Why fund agencies resources to run separate Requests for Tender, when existing procurement units may already have solutions and resources in place? Agencies claiming: “I’m different and need different procurement solutions” are seldom accurate and not a long-term solution for the benefit of the government or the community.

The emerging change in attitude of public procurement, is for the buying units of agencies to be accredited, at some level, on their capability and capacity to undertake certain procurements, as well as to support them with approved procurement default systems and centrally-provided procurement services. If a government agency does not have the capability to undertake the procurement, then they either need to develop it, acquire it or defer it to the areas of government that do possess the capability. There is also now less tolerance of not using established central e-Procurement infrastructure, not to is simply inefficient.

Is this beginning of a new trend?

In a speech in the UK Parliament on 14 July 2004, it was stated: “In business, centralisation of procurement has gone in and out of fashion. Centralisation will be a key part of the government’s procurement process”.¹

The pendulum is swinging back to the centre. Collaboration is the key to getting things done. Many in the public sector said there couldn’t be a standard for PCs or common pharmaceutical catalogues for health administrations or central accountability for all public sector procurement staff. However, various jurisdictions across Australia have implemented these exact processes. These types of successful initiatives demonstrate the notion that a centralised approach somehow will disenfranchise agencies’ ability to do their job doesn’t hold much weight.

The complexities of public procurement that supported decentralised procurement are being erased by technology and market changes. Centralised procurement now provides greater potential for optimising value to government and the communities they serve.

¹ Quote by a UK Government spokesman.
Conclusion

Any and all procurement solutions need to be somewhat grey. There is no place for black and white thinking in professional procurement. Good procurement practice will always be situational. Nevertheless, actions do follow from first principles, so the endpoint will determine the road chosen in any procurement activity.

Increased networked centralisation can bring standardisation, increased leverage, contract management, lower training costs, better performance management, improved transparency and reduced costs. However, if governments centralise their procurement activity poorly, then government value will inevitably be the casualty. Centralise the right processes, procedures, products and services and it allows procurement professionals to deliver true value, by reducing costs to government while also working in the best interests of all stakeholders.

About the Author

This paper was compiled from a CIPSA Forum presentation given on 2006 by:

Paul Hopkins, Deputy Director-General, NSW Department of Commerce

Paul Hopkins has over 25 years of experience in procurement management in Australia and overseas, ranging from manufacturing, importing/exporting to financial services and government. Prior to his appointment to the Department of Commerce in 2003, Paul worked for a range of companies, including BHP, Qantas, St George Bank, the Southern Sydney Region of Councils and entities and consulted with PriceWaterhouseCoopers.

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