

# **Chapter Eleven**

## Rethink Government Purchasing and Supply Chains

By Raj Sharma

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## The Opportunity

The federal government purchases more than \$500 billion of goods and services each year, buying everything from pens and paper to engineering services and fighter jets. Most experts agree that the government purchasing process is cumbersome and inefficient; hundreds of purchasing offices work independently with little or no coordination. The term “purchasing” is used throughout this chapter to refer to what is more commonly referred to as “acquisition” within the federal government.

Without greater transparency into all transactions or supplier relationships, purchasing staff by necessity focus on tactics to reduce price and manage individual transactions, as opposed to strategically managing cost and supply chains. The result of the present system is redundancy of a high order and billions of taxpayer dollars wasted every year.

One recent analysis, conducted by the Center for American Progress, estimates that the federal government can save in the range of \$400 billion over 10 years by applying practices already proven to work in state and local governments, and in private and public sectors. Many other analyses, including studies conducted by McKinsey & Company and the Technology CEO Council, have come to similar conclusions.

For those who may say these estimates are fictional, think again. To take just one private-sector example, IBM internally consolidated purchasing and restructured its supplier network, resulting in over \$25 billion in cost reduction and overall improved supplier performance. The same approaches, applied within the context of government, have proven to work in the public sector as well. The Commonwealth of Pennsylvania, for instance, implemented a strategic sourcing program, resulting in roughly eight-percent savings of the state’s \$4 billion in annual purchasing.

The good news is that within the Washington beltway, some have recognized this opportunity and have been pushing reforms into agency purchasing practices for years. However, these initiatives have only incrementally moved the needle toward a more efficient and effective system. Why?

The primary reasons previous reform efforts have delivered marginal results are:

- Besides the goal of reducing waste, there is no clear vision for what is required or expected of the purchasing system (or acquisition system as it is more commonly referred to). The lack of an end-state vision has resulted in a patchwork of reforms with no clear end goal or outcomes, sowing confusion and frustration on the part of those who can help drive the change.
- There is a narrow focus on basic commodities and an even narrower focus on negotiating better deals, as opposed to managing and reducing

total costs across supply chains. It should be noted that some of this has started to change, especially with the broader information technology (IT) reform agenda laid out recently by the Office of Management and Budget.<sup>1</sup>

- Necessary changes to organizations, processes, and policies are not made, thereby allowing inefficiencies to creep back into the system.

### **Why Many Purchasing Reform Initiatives Deliver Marginal Results**

All government agencies purchase common items like office supplies, software, and furniture. In most cases, these items and services are purchased independently, often by multiple offices within each agency. Not only does the current method mean that government misses out on the efficiencies that result when buying collectively and managing suppliers together, it also means there are numerous, redundant resources. Does it really make sense for hundreds of contracting officers to be buying office supplies across the government?

To fix this, many agencies have launched well-intentioned strategic sourcing initiatives to coordinate purchases and better manage suppliers. In many cases, agencies or government as a whole, through programs like the Federal Strategic Sourcing Initiative, have been able to negotiate better deals and drive changes to other behaviors that lead to substantial savings. However, because these initiatives are layered on top of fragmented processes and decentralized budgets where each office controls its own money, getting everyone across an agency or government to leverage these deals remains difficult. In many cases, compliance remains very low and savings have been slow to come by.

## **A Pragmatic Approach to Transforming Government Purchasing and Supply Chains**

Given the current fiscal environment, there is an unprecedented opportunity to not only transform the way government purchases but also the way it manages its supply chains. Based on lessons learned from previous initiatives, input provided by various experts, and on-the-ground experience of some of the world's leading companies, the pragmatic plan proposed below can drive efficiencies in the near term while transforming government purchasing and supply chains over the long term. While most elements of the recommendations proposed in this chapter require no formal policy or legislative changes, all will require the partnership and input of key stakeholders including the White House, Congress, agencies, and suppliers. The overall intent of the following recommendations is to broaden the discussion beyond tactics and help inform the agenda for purchasing reform going forward.

The chapter presents nine recommendations, with the first focused on redefining the role of government purchasing. Recommendations two through six focus on initiatives that can be implemented in the near term and begin to drive immediate benefits. Recommendations seven through nine require broader transformational and structural changes that can be implemented over the longer term.

### **Recommendation One: Re-Envision the Role of Government Purchasing From Managing Purchases and Price to “Managing Supply Chains and Total Cost”**

The role of government purchasing, as defined today within the Federal Acquisition Regulation (FAR), is to “deliver on a timely basis the best value product or service.” This definition can best be described as tactical and inward-looking, focused primarily on managing individual transactions and negotiating best price or value. This myopic view has also led to purchasing being perceived as a back-office function that gets in the way more often than it adds real value.

Many leading private-sector companies, meanwhile, define the role more expansively and strategically. Purchasing is viewed as critical to achieving corporate mission since it focuses on key activities such as cost management, supplier alignment, innovation, and risk management. Indeed, many purchasing executives have earned a seat at the (leadership and boardroom) table by bringing expertise on supply chains, and advising internal customers on how to best align capabilities of suppliers while reducing overall cost.

Going forward, the Office of Management and Budget (OMB) should propose a new vision for purchasing, one that goes beyond current definitions. The new vision must bring forth a fundamental shift in thinking on the role of purchasing, from managing purchases and price to managing supply chains and total cost. More specifically, the role should be redefined as helping government agencies *achieve their policy priorities by aligning and managing supply chains to deliver capabilities at lowest total cost*.

This new vision has profound implications on everything from the alignment of purchasing staff and processes to key capabilities required of purchasing organizations. Government agencies now need to anchor their resources around three key capabilities fundamental to world-class purchasing:

- **Modeling total cost:** Instead of focusing solely on price, world-class purchasing organizations develop an understanding of total internal and supply chain costs. Going beyond their own costs, world-class purchasing operations understand the cost breakdown for any purchased item or service (e.g. labor, materials, transportation, etc.). With that knowledge, they work with suppliers to take out waste and reduce total system costs. McDonald’s Corporation, for instance, has worked with suppliers to create a sophisticated model for optimizing the cost of chicken.<sup>2</sup>

- **Strategic sourcing and category management:** Second, we must shift emphasis from managing individual purchases to managing supply chains. This can be best accomplished by restructuring resources and processes to manage categories of goods and services (e.g. IT hardware, professional services). The obvious benefit is leveraged buying power. Even more important is the improved visibility into transactions, performance, and costs, as well as an overall reduction in resources required.
- **Supplier performance and relationship management:** Third, we must move from managing individual suppliers to managing entire supply chains. This shift implies the need for new capabilities with regard to understanding supplier performance and managing supplier relationships. It also requires more advanced capabilities, such as supplier development, that will drive down costs across the supply chain.

### **Recommendation Two: Appoint a Chief Federal Supply Chain Officer to Lead a New Office of Federal Supply Chain Management**

Elevating the role of purchasing to manage supply chains must begin at the top. Currently, the top purchasing position in the government is the administrator of the Office of Federal Procurement Policy. While important, the current scope of the office limits the office's ability to make the broader changes required to streamline and efficiently manage government purchasing and supply chains.

A new position of chief supply chain officer (CSCO) should be established, analogous to the creation of the federal chief information officer position. The Office of Federal Procurement Policy should be renamed the Office of Federal Supply Chain Management. The CSCO should head the new office and focus on gaining visibility, improving coordination, and reducing costs across the largest and most critical government supply chains. The CSCO should also be empowered to coordinate new initiatives, facilitate the sharing of best practices, and coordinate management and collaboration with government's largest and most strategic suppliers.

### **Recommendation Three: Strengthen the Role of Departmental Headquarters and Redefine the Role of Departmental Chief Procurement Officers**

Private-sector, corporate world-class purchasing departments wield significant clout. By building strong capabilities, corporations are able to help set standards, deploy critical capabilities (such as cost modeling), facilitate knowledge-sharing, and manage the sourcing of non-critical common categories. Benefits include reduced duplication, improved buying power, and enhanced coordination.

Unfortunately, the federal government has failed to realize many of these benefits. Often, federal agencies' purchasing offices, located in headquarters, are weak or powerless and provide limited capabilities beyond writing and

administering policy. In cases where some operational capability is present within headquarters purchasing offices, it often does not have the power to enforce compliance due to decentralized organizations and budgets.

Going forward, the role of headquarters purchasing functions within departments should be redefined to go beyond policymaking to include centralized management of non-critical common categories, management of supplier performance and relationships, and centralized capabilities in key areas such as cost modeling. Merely redefining the role will not be enough, however.

The headquarters function should be further strengthened by redefining the role of the departmental chief procurement officer (CPO) to encapsulate the current roles of the chief acquisition officer and senior procurement executive. The CPO should have a seat at the executive table and build a strong link with the chief financial officer to enable any budget-related decisions. Ultimately, to gain trust as a value-added partner to customers within their respective departments and agencies, headquarters will need to build world-class capabilities that can be more efficiently deployed in a centralized manner.

#### **Recommendation Four: Strengthen Strategic Sourcing and Centralize Management of Common Categories**

Strategic sourcing, while not new to the federal government, is still in many ways in its infancy. Most initiatives are being run with limited resources and no real integration into business processes. Many initiatives remain focused on consolidating contracts rather than focusing on all value drivers, including managing demand and improving supplier relationships. Even when some initiatives are able to generate value, compliance is low due to the decentralized nature of agencies.

While there have been challenges, there have been successes as well. The Department of Commerce, for instance, has been able to rapidly scale up strategic sourcing while it begins to build out capabilities for the long term.

Going forward, government departments should:

- **Establish strategic sourcing functions.** Current strategic sourcing initiatives should evolve into permanent organizations, led by an executive with significant experience in strategic sourcing. It will be important to ensure that people with the right skills and expertise are put in place to facilitate the sourcing process and engage stakeholders and suppliers.
- **Centralize management of non-critical common categories.** At the outset, one of the key priorities for strategic sourcing should be to centralize the management and sourcing of all non-critical common categories. Support from top leadership, including the Cabinet secretary and chief financial officer, will be critical to building buy-in from all stakeholders and making necessary budget and financial decisions, if needed. When possible, these organizations should leverage and coordinate with efforts such as the government-wide Federal Strategic Sourcing Initiative (FSSI).

- **Establish category managers for the largest and most critical categories.** In addition to managing common categories, the strategic sourcing organization should establish category managers to coordinate the management of the largest and most critical categories. Each category manager should bring significant experience in each respective category and be chartered to develop a holistic plan for reducing costs and optimizing supply chains. Additionally, category managers should have full lifecycle responsibility for managing spending across a category, from strategy development to performance management and delivery.

### **Recommendation Five: Establish Supplier Performance and Relationship Management Programs**

In spite of being the largest purchaser in the world, the federal government lacks the most basic capability when it comes to managing supplier relationships. For instance, most departments have no enterprise-wide view of their supplier performance.

Private-sector organizations that understand the value of supplier relationship management start with the basics, establishing performance scorecards to gain enterprise-wide visibility into supplier performance across all contracts. They use that visibility to identify opportunities for improvement, whether with specific suppliers or with groups of suppliers (e.g. all small businesses).

Building on recent initiatives such as Past Performance Information Retrieval System (PPIRS) and OMB Mythbusters initiatives, the federal government should establish formal supplier performance and relationship management programs in order to:

- Gain full visibility and transparency into supplier performance via performance scorecards
- Develop improvement roadmaps, identifying specific initiatives that lead to overall improvement in quality and supply chain costs

### **Recommendation Six: Implement TechStat-Style Reviews of Major Acquisition Programs**

The history of government purchasing is littered with stories of the colossal failures of major programs, from the Secure Border Initiative to the much-maligned Virtual Case File system for the FBI that was shut down after spending nearly \$100 million. To minimize such failures, all agencies should rapidly adapt the highly successful TechStat review process, established by the federal CIO for the area of IT program review and governance, for all major acquisition programs.

The largest government acquisitions should be scrutinized at the OMB level and the next tier of programs should be evaluated at the agency level. To be sure, changes will be required to the TechStat review process for broader

adoption. For one, there is no single focal point for all major acquisition programs. Therefore, it will be important to ensure the appropriate leadership is present and held accountable for major acquisition programs. Ideally, reviews should be led by the deputy secretary and the chief procurement officer, along with the program executive and other relevant parties.

Ultimately, the goal of the acquisition program reviews should be to improve overall program performance while reducing total cost in coordination with key suppliers. If done correctly, benefits such as those accrued through the TechStat reviews are possible.

### **Recommendation Seven: Restructure the Workforce and Transform the Culture**

While there is significant discussion of increasing the number of contracting officers and other purchasing-related positions within the purchasing workforce, there is limited discussion on how best to reorganize and realign the staff. There is an enormous amount of redundancy and inefficiency within the current purchasing workforce that can be eliminated through a well-structured realignment.

To improve productivity and effectiveness of the workforce and to realize the redefined vision of purchasing, the Office of Management and Budget, along with purchasing leaders from the departments, should build on current workforce initiatives and develop a workforce transformation plan that addresses the following key issues:

- **Alignment of workforce.** In the current environment, the purchasing workforce is primarily focused on tactical execution of hundreds of transactions while following the complex set of regulations within the FAR. Furthermore, most purchasing personnel are aligned by process, instead of by category or supply chain, leaving them little time to become experts in any particular area. Moving forward, government agencies should develop a plan to realign the workforce in order to strategically manage critical supply chains, efficiently manage transactions, and centrally deploy critical capabilities.
- **Skill sets.** The shift envisioned, from management of transactions to strategic management of categories and supply chains, requires a significant change in skill sets. Key skills required of world-class purchasing organizations include problem-solving, strategic thinking, financial analysis, and relationship management.<sup>3</sup> In addition to training and developing the current workforce for these skills, government should redefine position descriptions and recruiting practices to ensure that any new personnel brought into the government workforce already exhibit these key skills.
- **Culture.** The culture of government purchasing has traditionally been defined as risk-averse. Many government personnel prefer to take the safer route and check every box prescribed in the FAR than to pursue innova-



tive ideas. It also may seem much easier to work in silos and conduct handoffs rather than work collaboratively with customers and suppliers to solve problems. It is critical that government purchasing leadership, starting at the top, begin to establish a culture that promotes collaboration and some level of risk-taking.

### **Recommendation Eight: Streamline the FAR and the Procurement Process**

While the intent of the Federal Acquisition Regulations is to ensure stewardship of taxpayer dollars and a level playing field for suppliers, the morass of acquisition policies and regulations in many ways works against that very noble intent. Instead, purchasing processes have become so complex that only those in the know can compete for government purchases.

“The [purchasing] process and unique government requirements work to create significant barriers to entry, potentially inhibiting many suppliers from competing,” according to a paper by the FAIR Institute. “Those suppliers that do choose to compete for federal business incur significant costs that ultimately get passed on to government.”

Following the example of the Federal Acquisition Reform Act of 1996, which resulted in substantial streamlining of the federal purchasing process, the federal government should once again undertake a review of purchasing regulations and processes. The primary goals underpinning any future reforms should be to:

- Simplify and streamline regulations including the FAR
- Rationalize the legislation and policymaking apparatus that currently results in conflicting rules issued by different parts of the government
- Standardize and streamline common processes, tools, and forms that impose significant costs on both government and industry
- Gain complete visibility into each government supply chain through an integrated data model that tracks key supply-chain metrics
- Define the role of technology in streamlining and standardizing processes

### **Recommendation Nine: Leverage Technology to Improve Transparency, Maximize Competition, and Drive Down Cost**

One of the biggest opportunities lies in the government's ability to leverage proven supply chain technologies to enhance productivity and decrease overall cost of managing each supply chain. While the government has spent enormous amounts of money to automate the purchasing process, results have been at best lackadaisical. As an example, government has very limited visibility into its spending, cost, and performance metrics related to each supply chain. Furthermore, while contract writing systems have been implemented, they remain un-standardized and fragmented. Even when they are standardized, they are seldom used to drive overall user compliance, resulting in significant loss in potential savings.

Going forward, government should develop an integrated supply chain technology strategy, building on activities such as the Integrated Acquisition Environment, an ongoing presidential e-government initiative managed by the General Service Administration, with the goal of leveraging proven technologies already resident within the marketplace. Specifically, a holistic supply chain technology strategy should seek to:

- Leverage commercial sourcing and marketplace platforms that maximize competition and open up the federal market to more qualified suppliers
- Gain complete visibility into each government supply chain through an integrated data model that tracks key supply-chain metrics
- Standardize government contract writing systems
- Integrate end-to-end processes with suppliers

**Raj Sharma** is a visiting fellow at the Center for American Progress and the founder of the Federal Acquisition Innovation and Reform Institute.

## Notes

1. Vivek Kundra, U.S. Chief Information Officer, *25-Point Implementation Plan to Reform Federal Information Technology Management*, December 9, 2010. (<http://www.cio.gov/documents/25-point-implementation-plan-to-reform-federal%20it.pdf>)

2. Dr. Timothy M. Laseter, *Balanced Sourcing: Cooperation and Competition in Supplier Relationships*, Jossey-Bass, 1998, p. 7.

3. David Litman and Raj Sharma, "Building an IT Acquisition Manager Community," June 2011, FAIR Institute.