

Procurement Profiling - A Guide for Agencies

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Purpose of this guide

This document provides guidelines to assist agencies in compiling a procurement profile to enable the compilation of baseline data to support the development of appropriate procurement strategies.

What is a procurement profile?

A procurement profile allows an agency to place its expenditure on goods and services in the context of its total expenditure for a given period. It provides a snapshot of the value, range and characteristics of an agency's total expenditure on goods and services, and is an integral step in reviewing the efficiency of its purchasing practices.

The profile provides information on:

- what types of goods and services the agency purchases;
- how much the agency spends on various types of goods and services;
- how the goods and services are purchased;
- who the goods and services are purchased from; and
- the geographical location of suppliers.

For the purposes of this guide, “goods and services” refers to all the goods and services purchased by an agency, including those used in building and construction.

Why develop a procurement profile?

Profiling of procurement expenditure enables the development of an understanding of an agency's purchasing habits and patterns. It is the first step in re-engineering procurement processes and adopting best practice, enabling agencies to fully exploit their procurement potential to:

- add value to service delivery;
- contain costs; and
- contribute to broader policy objectives such as industry development.

The procurement profile identifies areas for improvement and provides a benchmark against which improvements can be measured. For instance, a procurement profile can help an agency identify those areas of its purchasing that are best suited to electronic procurement, or improve practices that will lead to efficiencies.

The completed profile provides key management information to assist agencies in procurement related decisions such as determining the structure of procurement, including delegations and processes, and the allocation of resources.

Developing a procurement profile

Who should compile the profile?

Officers responsible for compiling the agency's procurement profile will require knowledge of the agency's:

- chart of accounts;
- activities and programs;
- financial management information system, including the skills necessary to extract data from the system; and
- procurement processes, and an understanding of Government procurement policies and guidelines.

Determining the scope of the profile

A profiling exercise does not need to include an in-depth analysis of all procurement expenditure during a given financial year. Agencies may wish to target specific purchase types, such as those of high value, or limit the analysis to a specific business unit. However, at a minimum, agencies should extract summary information on all expenditure, in order to place procurement expenditure in the context of total expenditure.

Collection of data

The agency's financial management information system will be the main source of information for compiling its procurement profile.

Extracting the data from the Financial Management Information System

The procurement profile should be based on data that has been reconciled as part of the preparation of the agency's financial statements. Unreconciled data may contain a large number of anomalies.

General ledger codes relating to error, suspense, and intra-agency transfer codes should be excluded, as they can distort the information.

While it is necessary to extract all information relating to expenditure, only summary information (ie total value of expenditure) is required for general ledger items that are not related to the procurement of goods and services. This is to enable the expenditure on goods and services to be placed in the context of the agency's total expenditure. Expenditure types for which only summary information is required include:

- basic salary expenditure, allowances, overtime, employer superannuation contributions, etc;
- recurrent grants and other administered payments; and

- payroll tax, fringe benefits tax and goods and services tax.

Detailed transaction information is required for general ledger codes that are identified as relating to expenditure on goods and services. The data extracted should allow for the analysis of individual transactions by goods and services category, value, payment method, invoice number and suppliers.

The data items listed in the following tables are considered to be the minimum set required to construct a basic procurement profile:

Table 1 General Ledger/Transaction Information

Data items	Why the information is necessary
Natural Account Code and Description	Forms the basis of the goods and services categories, allowing transactions to be grouped and sorted.
Supplier Number	Allows the transaction to be related to the supplier from whom the purchase was made.
Invoice Number	When combined with the supplier number, allows the reconstruction of invoices issued to the agency by each supplier.
Transaction Description	Provides additional information on each purchase. This can be used in instances where the reclassification of expenditure is necessary.
Amount	Provides the value of the purchase.
Cost Centre	Allows lower level analysis of purchases by specific sections within the agency.

Table 2 Creditor Chart/Supplier Information

Data item	Why the information is necessary
Supplier Name	Provides the name of the supplier. This can be used in the construction of reports.
Supplier Number	This is the key that links the transaction and supplier information, allowing each transaction to be related to a supplier.
Supplier Postcode	For analysis of suppliers by region.
Supplier Payment Method (EFT or Cheque)	Information on the method by which a supplier is paid is important in identifying opportunities to reduce transaction costs.
Supplier Status (Active or Inactive)	Identifies inactive suppliers, that can be excluded from the analysis.

Individual agencies may decide to extract additional data items, depending on the types of analysis that they wish to conduct.

- Tips**
- Where possible, all inactive suppliers should be excluded from the analysis.
 - Remember that the data extracted from the agency's general ledger will be Goods and Services Tax (GST) exclusive, while the amounts paid to suppliers by the agency will include GST.
 - Consider the size and format of the extracted data, both for moving the file within the local area network, and in determining the application or applications that will be used for analysing the data.

Verifying and “Cleansing” the extracted data

Once the data has been extracted from the agency's financial management information system, it should be verified to ensure that:

- all of the information required is included;
- the data is in the appropriate format; and
- the sub-totals are consistent with the agency's financial statements.

Following verification, the data will need to be “cleansed”. This process involves the identification and removal of administered payments (that is, payments for which there is no consideration), allowing the true value of expenditure on goods and services to be determined.

Determining the procurement categories to be used

Once the data has been “cleansed”, the relevant procurement categories should be determined. These categories will form the building blocks of the analysis.

In most cases, the agency's chart of accounts will provide sufficient detail to commence the profiling exercise. However, in some cases, the general ledger codes may be very broad, and may not adequately represent the variety of purchases that are charged to them. In these cases, it may be necessary to examine the transactions that have been posted to each of these codes and, using the transaction descriptions, reclassify them into more meaningful groups.

For example, a general ledger code with a descriptor “Consultants” may be too broad, as the agency may have procured a variety of different consulting services, each type having differing supply markets, differing level of purchasing risk and differing applications within the agency.

Tip When reclassifying goods and services into more relevant categories, consider:

- the method of purchase;
- the complexity of the purchasing process;
- how important they are to the agency; and
- the characteristics of the market that they are purchased from.

The general ledger code, supplier information and general references such as the Yellow Pages, may assist in the reclassification of expenditure.

Result Following completion of the scoping, data extraction, verification, cleansing and reclassification processes, the outcome should be a file consisting of:

- the individual transactions comprising the agency’s procurement expenditure; and
- a detailed list of all suppliers with which the agency has dealt during the financial year.

Once the extracted data has been reviewed, verified and cleansed, it can be used as the basis for the procurement profile analysis.

Analysis

Generally, a procurement profile will provide answers to the following questions:

- What proportion of the agency's total expenditure is spent on goods and services?
- What type of goods and services are procured by the agency, and how much is spent on each type?
- Who are the goods and services purchased from and how are they purchased?
- What is the geographical location of the suppliers that the agency deals with?
- Where should the procurement effort be focused?

What proportion of the agency's total expenditure is spent on goods and services?

A high level summary report placing the value of the agency's procurement expenditure in the context of its other, non-procurement related, areas of expenditure is a good starting point, allowing quick comparison and demonstrating the relative importance by value of expenditure on goods and services.

What goods and services are purchased and how much is spent on them?

To answer this question, an agency will need to construct reports that detail all of the procurement categories by value, demonstrating what types of purchases are procured by the agency and highlighting the areas of high value expenditure.

Result The outcome of these processes should be:

- a comparison of the agency's expenditure on goods and services to its total expenditure; and
- a list of all of the types of items purchased by the agency and the actual expenditure on those items.

Who are the goods and services purchased from and how are they purchased?

For each supplier, identify the agency's total expenditure on goods and services, the number of times the supplier invoiced the agency, the value of each invoice and the method of payment.

This process will identify the agency's key suppliers by value and volume of invoices. It is these suppliers from which the greatest efficiency gains can be achieved by reviewing and, where necessary, implementing changes to improve purchasing processes and supplier management arrangements.

Tips • In cases where the Corporate Card facility has been used to pay for goods and services, the details of the suppliers from whom they were purchased may not be directly identifiable.

Result • The outcome of this process should be a list of all of the agency's suppliers by total value of expenditure on goods and services, together with a breakdown of the value and number of invoices received.

Opportunities for improvement

The aim of this analysis is to improve the efficiency of the procurement process, through reduced costs (including processing costs) and improving the way that suppliers are managed.

High value suppliers may present the agency with opportunities for reducing costs through establishing strategic supply arrangements (contracts) if they do not already exist. This can provide the agency with improved value for money outcomes through lower prices and/or increased services. Initially, efforts should be focused on those suppliers with which the agency has no existing contractual arrangement.

In addition, the agency may wish to devise a contract renewal timetable for existing contracts, to ensure that sufficient time is allocated for the establishment of new contracts and that value for money outcomes are achieved.

High volume transaction suppliers present the agency with opportunities to reduce the number of transactions through consolidating invoices, rationalising orders and exploring electronic ordering and payment solutions. Initially, efforts should be focused on those suppliers that are paid by cheque, as this is a less efficient payment method.

- Tips**
- Electronic Funds Transfer (EFT) is a more efficient payment method than cheque. Targeting those suppliers that are paid by cheque and moving them to EFT is a first step towards introducing electronic commerce.
 - Agency's financial management information systems may contain duplicate entries for the same suppliers. Where possible, these duplicates should be excluded.

Agencies may wish to determine the internal costs of processing invoices, in order to determine the value to the agency (in efficiency savings) of any re-engineering of procurement processes.

What is the geographical location of suppliers that the agency deals with?

By using the location of suppliers and the types of goods and services that have been purchased, agencies will be able to determine which types of purchases are sourced locally, or from other states of Australia, and overseas.

- Result**
- The outcome of this process should be a list of all of the agency's suppliers by location and the type of goods and services that are purchased.

Opportunities for improvement

The aim of this analysis is to improve the efficiency of the procurement process, through reviewing agency sourcing decisions with a view to reducing costs and increasing opportunities for local businesses to compete for government business.

Agencies can identify import replacement opportunities by identifying alternative local suppliers of goods and services that are currently sourced from interstate and overseas. Where there are no local suppliers, the agency may consider encouraging the development of local industries to meet its needs.

In addition, the agency may benefit from reviewing the locations from which goods and services are purchased and the areas where those goods and services are consumed within the state. This is especially important for regionalised agencies. For example, as the Department of Education has a large number of schools in remote locations, the location of a supplier can have a significant impact on delivery time, together with the timeliness of associated services such as backup and servicing.

In accordance with government procurement policy, agencies should ensure that local suppliers are encouraged to compete for government business, and that the advantages of buying locally (including regionally) sourced goods and services are taken into consideration when making purchasing decisions.

- Tips**
- Agencies should be aware that regional analysis based on postcodes will only reflect the location where the supplier's mail is delivered, and not necessarily indicate where the supplier is physically located.
 - Where possible, the agency should exclude all inactive supplier records from the data extracted.

Where should the procurement effort be focused?

The two main factors influencing how each agency purchases are:

- the total expenditure on goods and services relative to the total expenditure of the agency; and
- the complexity of the supply marketplace and its impact on agency service delivery, which is based on the following factors:
 - the dependency of agency service delivery upon particular goods and services;
 - the risk to agency service delivery arising from potential disruption, such as a discontinuity of supply or significant increase in price;
 - the makeup of the marketplace (eg many suppliers – highly competitive; few suppliers – less competitive);
 - the lead times and the complexity of the technology involved and/or the specialist knowledge and expertise required in the acquisition process; and
 - the source of the original manufacture or service supply and any related opportunities, to encourage the development of local sources.

An agency can determine where its procurement effort should be focussed, by using a procurement management tool called “supply positioning”. With supply positioning, goods and services groups are plotted according to their relative expenditure and risk, and the complexity of the supply marketplace.

A simple but effective matrix will have four goods and services groups as below:

	High	
Risk or complexity	3. Complex supply market with high risk and low relative expenditure	4. Complex supply market with high risk and high relative expenditure
	1. Simple supply market with low risk and low relative expenditure	2. Simple supply market with low risk and high relative expenditure
	Low	High
	Expenditure	

Once complete, the matrix can be used to identify opportunities and procurement strategies to achieve best practice procurement.

Low Expenditure Low Risk Group

These goods and services are generally purchased on an informal/adhoc basis, with short lead times. Collectively, these items make up a relatively small proportion of the agency's total expenditure, and will demand substantially less attention than goods and services in the other categories.

Procurement strategies include increased utilisation of EFT (eg corporate card), establishing contract arrangements, simplifying procedures, rationalising the supplier base, and negotiating medium term contracts.

High Expenditure Low Risk Group

Goods and services in this group tend to be regularly purchased and standard in nature (eg stationery). Sourcing is not a problem due to highly competitive and mature supply markets served by a few large suppliers, often with extensive distribution networks.

Procurement strategies aim to reduce processing cost and improve service, and include automating the processing of transactions through efficient interfaces with suppliers, electronic ordering and transaction processing through online catalogues, and negotiation of medium term contracts.

Low Expenditure High Risk Group

Goods and services in this group are items critical to the agency's operation that are low in relative value. Sourcing may be a problem, either because of a shortage of suppliers or long lead times.

Procurement strategies aim to reduce risk by finding alternative sources of supply. Strategic analysis will be required to identify options to secure continuity of supply. Electronic commerce can be used to monitor critical supply level, identify alternative sources of supply and give better management information for contract review and negotiations.

High Expenditure High Risk Group

These goods and services tend to have difficult markets due to few suppliers, with little competition, necessitating long term relationships with suppliers.

Procurement strategies focus on securing value for money and receiving the benefits of technology, innovation and continuous improvement through effective supplier relationship management. The cost of bidding for contracts in this category is high for both agencies and suppliers.

Where to from here?

On completion of a procurement profile, the agency will be far more aware of the strengths and weaknesses of its procurement function, together with the opportunities for efficiency savings that it presents. In addition, the profile provides the agency with valuable benchmarking information upon which any improvements in the procurement function can be measured.

Based on the recommendations arising from its procurement profile, the agency will be in a position to map out an agenda of reform for procurement, which may include:

- ensuring that strategic supply arrangements (contracts) are establish with high value suppliers;
- reducing the number of transactions the agency has with high volume transaction suppliers;
- identifying alternative local suppliers of goods and services that are currently sourced form interstate and overseas;
- examining where locally sourced goods and services are purchased from and consumed within the State; and
- reviewing agency procurement processes to ensure current procedures are meeting the agency's needs.

To measure the effectiveness of any changes the agency implements, targets should be set and indicators established to monitor progress towards achieving those targets.

Some of the goods and services areas may require additional analysis prior to the implementation of any change. However, in most cases, having completed a procurement profile the agency will be armed with the necessary knowledge to identify and implement reforms to improve the efficiency of its procurement function.

More information

If you need more information, or require any assistance regarding the analysis techniques detailed in this document, please contact:

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