

Using the power of public procurement

Recommendation:

- The approach to public procurement, both for central government and local bodies, should be adapted (in the ways listed below) to encourage more innovative solutions from suppliers.

The public sector is estimated to spend around £125 billion each year on goods and services, of which local authorities spend around £47.5 billion. The public sector therefore exerts a huge influence over the tens of thousands of companies, indeed over whole industries, that supply it. The extent to which it allows, encourages or even demands creativity from its suppliers therefore has a huge influence on the UK business environment. At present, this power to stimulate creativity is not being used effectively. Indeed, in many cases, it is having the opposite effect. If we want to change the business culture in the UK, making it more enterprising and innovative, creating services and products that are world leaders, the vast domestic market that the public sector represents has a major role to play in becoming a more enlightened and more demanding buyer.

Much work has been done to review public procurement. There have been the *Gershon*, *Innovation*, *Kelly*, *Byatt* and *Better Regulation Task Force* reports and, more recently, Lord Hollick has been asked by the Prime Minister to look at innovation within procurement. It has certainly suffered no lack of attention.

The general focus has been on value for money – which no-one could argue against. For example, Sir Peter Gershon's report, *Releasing Resources to the Frontline*, sought to improve productivity in the public sector by means of more effective procurement and resource allocation. It led to proposed improvements such as aggregating demand and better use of regional centres of procurement. Moreover, the definition of value for money has been commendably widened. The Office of Government Commerce's (OGC) and National Audit Office's (NAO) guide to auditors says that value for money can be gained by, "Optimising the cost of delivering a service or goods over the full life of the contract rather than minimising the initial price".

However, the issue is not simply whether a proposed solution offers value for money, or even the best value for money of the options considered; it is whether greater value could be obtained from a more innovative solution, perhaps allied to looking at the problem in a wider context.

This is particularly important when one recognises that all of the major problems facing society today – such as healthcare, education, security, transport infrastructure or sustainability – require a high degree of innovation if they are to be addressed effectively. The demands cannot be met simply by pouring in more resources. In many instances, innovation represents the *only* route to genuine value for money.

At present, procurers aren't routinely seeking out more imaginative solutions to needs and requirements. There are times when true value for money means taking into account wider issues than quantified savings, and exercising a degree of personal judgement. How, for example, do you quantify the fact that something makes life more comfortable for the patient, or makes it possible to teach more effectively? The taxpayer has every right to demand the most effective and efficient services, sourced from wherever is most appropriate, but a high degree of innovation, exploiting the latest advances in knowledge and technology, is a key to delivering those services.

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There should be pressure on suppliers to come up with new ideas and innovative solutions to problems, while still meeting the requirement to show value for money. There should be more opportunity for unsolicited novel approaches to meeting public sector needs, particularly where new technology is involved.

For example, John Leighfield, the Chairman of RMplc, the UK's largest supplier of technology to schools, says, "Public procurement can drive innovation, but only if the procurement process recognises the specific needs of users. The RM One pc is a very good example of this – it's designed for education, but educationalists only recognise the benefits when they see them. If central and local government encouraged such innovation through their procurement processes, then more UK suppliers would invest in innovation that both helps education and opens up UK export opportunities".

There should be wider acceptance that while innovation involves a higher degree of risk, the right response lies in becoming more skilled at assessing and managing risk, not in its avoidance. The public interest is not always served by going for the safe and proven option.

Many of these arguments have been recognised. The OGC, which has overall responsibility for public sector procurement, issued a guidance paper in 2004 entitled, *Capturing innovation: nurturing suppliers' ideas in the public sector*. The foreword from the Secretary of State at the DTI says, "This guidance challenges government procurers to 'think innovation' and become intelligent procurers". The Chief Secretary of HM Treasury makes a contribution, saying, "Public procurement is generally more effective if it is open to innovative ideas. Supplier innovation has the potential to create better-quality public services, reduced costs and faster achievements of benefits". Absolutely right.

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But such declarations and the accompanying guidance aren't sufficient to overcome years of ingrained thinking and behaviour or a lack of necessary skills to put policy into practice. This is compounded by the fragmented nature of procurement, carried out not just by the many different central government departments but by thousands of local bodies. It is possible for government to set overall rules that constrain practice but much more difficult to mandate positive behaviour. It is an area where there is no firm connection between the bridge and the rudder.

Despite the difficulties, I believe that things can be done to accelerate the necessary change. Acknowledging that the approach to public procurement is under continuous review, I make the following seven recommendations.

Allow and require more discussion pre-specification

Purchasing specifications are generally tightly drawn around a fixed, minimum-capability requirement, to be achieved at minimum cost. By the time they are produced, there is often too little scope for innovative solutions or for solutions that challenge the breadth of vision of the specification.

There should be greater discussion around the nature of a requirement, long before the specification is produced. In the modern world, new developments often offer quite different approaches to a problem, or even change the nature of the problem itself. This is one of the areas being explored by Lord Hollick, who is taking the interesting – and potentially highly instructive – approach of looking at a small number of prospective major projects and demonstrating how such discussions can lay the foundations for success, including the better management of risk.

The OGC recognises the philosophy: “Innovation from suppliers should be encouraged throughout the procurement contract lifecycle but the greatest potential arises from the earliest stages”. But, again, it is not being translated into widespread practice.



The UK is spending ever more on public services – but how much on innovative solutions...?

UK expenditure on education and the NHS
(£ Billion)



Source
HM Treasury Spending
Reviews 2002, 2004

“Public procurement is missing the opportunity to take full advantage of advances in technology.”

**Sir John Chisolm, Executive Chairman,
QinetiQ Group plc**

“There is no reason why public sector projects should be any less successful or less innovative than the best in the private sector.”

Lord Hollick



Identify project needs more holistically

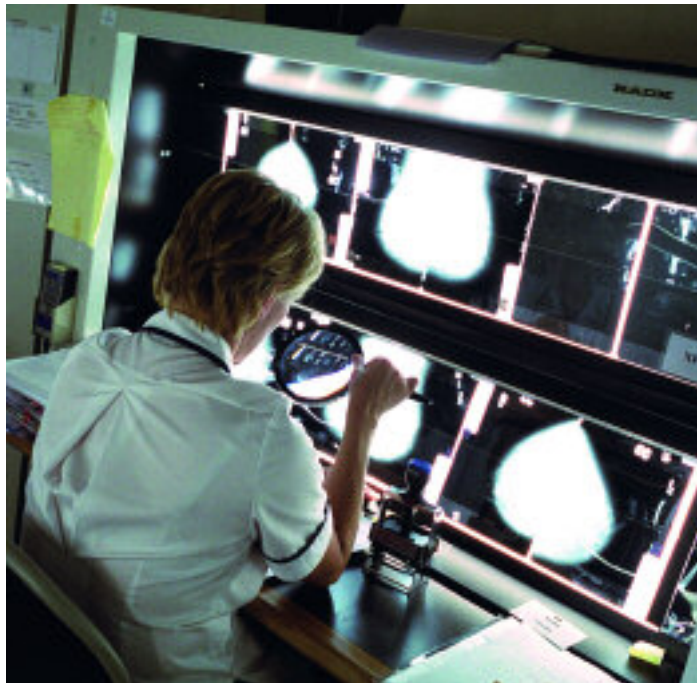
Purchasers too often take an excessively narrow view of individual project requirements, losing sight of the broader context. Minimising spend on individual projects minimises *overall* spend only if projects are entirely unrelated – which is rarely the case. Too often, agencies seek value for money simply at the level of individual units of equipment. This isn't due to short-sightedness on the part of those doing the purchasing; it's an organisational and systemic problem that limits their scope.

Procurers should broaden their assessment of value for money to take in wider considerations and to allow – indeed, to demand – judgement to be exercised on qualitative considerations such as impact on members of the public (in terms of, say, convenience or accessibility), effect on the working environment, benefits (or costs) in areas outside the project itself, and the platform for the longer term.

There also needs to be clearer distinction between different classes of project. In the private sector, there has been a growing recognition that 'projects' vary greatly in nature and have to be evaluated by different criteria. Some are mandatory (in that they simply have to be undertaken), some opportunistic, some infrastructural (in that they open the way to future benefits but have none of their own), some reduce costs, others give new capabilities. If they are pushed through the same 'cost benefit' analysis, the answer is usually a fudging of figures to get the desired result, disguising both the nature of the decision and the judgement involved. Projects should be categorised at the outset and treated accordingly.

Considerations such as risk profile, potential upside, and effect of failure should all be factored into the assessment of value for money, along with a recognition that best use of resources, scalability and delivery time are all important for large projects. Inappropriate metrics can have unintended consequences. Contract assessment metrics should be expanded beyond delivery cost to include parameters like lifetime costs and benefit values, and impact on the broader market. Such parameters could be both as envisaged at contract time, and as actually achieved post-installation.

Differentiation also needs to be made between straightforward commodity purchasing ('pencils and paperclips') and those decisions where innovation is a realistic consideration. In terms of procurement, one size does not fit all. However, care also needs to be taken not to classify as commodities items where innovation has not figured largely in the past but could in the future – for example, hospital beds or school furniture.



Improve purchaser capability through better training

If the public sector is to become more open to, indeed to seek, more innovative solutions to its needs, more demands will be placed on those charged with procurement. An openness to new ideas is not, of itself, sufficient. An awareness of trends in technology, and the ability to assess radical approaches and the capabilities of new suppliers are all essential.

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With greater innovation inevitably goes a higher degree of risk. More attention should be paid to equipping managers to identify, evaluate and mitigate that risk. The majority of innovative projects that go wrong (in the private sector as well as in the public sector) do so because of oversight or wrong expectation at the outset, not because of subsequent mismanagement. The emphasis has to be on how the problems can be spotted early, often through a series of exploratory stages. There should be an understanding that a good contract is one where risks are shared and understood, not where the blame for failure is pre-defined at the outset. There should be more hand-in-hand working with selected suppliers, on a competitive basis, to resolve risks and develop staged development plans.

The Chartered Institute for Purchasing and Supply (CIPS) reported, in various surveys and studies, that a lack of skilled and trained staff consistently heads the list of factors adversely affecting performance. Only 50 per cent of local government procurers have a formal qualification from the professional body. Although qualification does not equate to good working practice, it does reflect a basic degree of training and professionalism. The CIPS's training programme now puts innovation at the centre of its courses, rather than making it an add-on. It is interesting to note, in the light of earlier discussions, that the Institute has already accredited over 1,000 professionals in China. I recommend that more training be made available – indeed, it should be mandatory for anyone above a certain level of procurement authority.

Take into account the impact on future supplier capability

Government purchasers, who have the power at times to kill off or sustain suppliers, should be required to evaluate and consider the consequences of their actions on the supply industry. The existence of a competitive indigenous supply industry can often deliver long-term benefits that outweigh added costs in the short term.

Help smaller innovative companies to bid

Smaller companies, often with a unique proposition, are sometimes put off bidding by the fear that they are too small to be given the contract and that their submission will simply point the way for the others. Where the purchaser likes the innovative proposal but has a justified concern about the capacity of the bidder to deliver, a way should be found to team the smaller company with a larger partner. This shouldn't be an *ad hoc* response; it should be an intrinsic part of purchasing policy.

Require the NAO and the Audit Commission to monitor innovation

The NAO is a powerful entity hovering in the background of every central government procurement decision, as is the Audit Commission for other public sector bodies. Their remit should be widened, from ensuring that the current procurement rules are followed, to embracing the above principles. They should routinely ask whether more imaginative solutions have been considered, whether wider benefits and costs have been taken into account, what the longer-term impact might be, and how fully the risks have been evaluated and are to be managed. The NAO and the Audit Commission are custodians of the taxpayer's interest; that interest is not always best served by the lowest-cost, least-risk response to a narrowly defined need.

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What is required is not a softer or more lax approach to public procurement – just the opposite. The public sector, whether this be central government or local body, should be an intelligent and demanding buyer of goods and services, not simply looking for long-proven products and yesterday's solutions at the lowest prices. That would help ensure real value for money from the extra investment going into public services and, as a by-product, would stimulate far more innovation within industry.

I recognise that the NAO and Audit Commission report to the Auditor and Comptroller General, who in turn is accountable to the Public Accounts Committee (PAC). That means the PAC would need to endorse this recommendation.

Define accountability for central government implementation

At present, if anyone in central government transgresses the rules for procurement, he/she can expect to be called to account. If he/she fails to follow the policy of seeking more innovative solutions, there is no such comeback. This inability to ensure that policy is pursued contrasts strongly with the private sector; widespread change in big corporations is not easy, particularly when there is a multinational dimension, but the chain of accountability is clear and policy gets implemented. The answer is not to have a 'procurement czar' but to make the Cabinet Secretary and the Permanent Secretaries clearly accountable for ensuring that the policy is understood and pursued.