

## **In Confidence**

**OFFICE OF THE MINISTER  
FOR ECONOMIC DEVELOPMENT**

The Chair

**State Sector Reform and Expenditure Control Cabinet Committee**

### **Procurement Functional Leadership Quarterly Report, October to December 2013**

#### **Proposal**

- 1 This paper reports on the progress of the Procurement Functional Leadership programme from October to December 2013. It includes savings results from all-of-government (AoG) contracts as at 31 December 2013 and agency participation data as at 31 January 2014.

#### **Executive Summary**

- 2 Savings achieved through the AoG contracts have now reached \$107.3 million since the first set of AoG contracts were established. The savings realised continue to grow as further agencies participate and as the Ministry continues to establish more AoG contracts.
- 3 The Ministry has assessed the potential benefit from AoG solutions for Building Materials, Consultancy Services and Banking Services. Significant value for money and improved consistency of practice can be achieved through AoG contracts for these categories. These are large and complex categories. The government will take a staged approach where it will go to market for sub-categories of Building Materials and Consultancy Services. This will enable the Ministry to quickly establish AoG solutions and progressively add subsequent sub-categories. The Banking Services contract activity will be focussed on establishing contracts for core transactional banking services, purchasing cards and possibly foreign exchange.
- 4 Officials continue to consult agencies about a whole of government approach that would extend the mandate of the Functional Leadership initiatives and the Minister of State Services will report back to us later in March. Agency feedback received to date has generally been positive.
- 5 A pilot project has been established to consider how the government can engage with its strategic suppliers. The pilot will run for a 6 month period. Officials will work with four pilot suppliers to consider how the government can better coordinate its relationships in order to achieve improved public services.

#### **Unlocking cost savings**

##### *Current AoG contracts*

- 6 Savings realised through the AoG contracts continue to grow. By 31 December 2013 total savings realised reached \$107.3 million. This is a significant step and can be attributed to the number of agencies actively using the contracts.

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- 7 The AoG contracts allow agencies to reinvest savings made into other parts of their business. Figures reported by the Ministry are savings realised directly by the agencies in the unit price paid and do not account for other efficiencies realised through the contracts such as improved processes or headcount changes. The total forecast savings realised over the life of the contracts established to date has grown from \$330 million reported last quarter to \$347.9 million. This has been driven by:
- growth in the forecast savings from the Reticulated Gas contract that I announced in October 2013. Forecast savings have been updated from \$4.1 million to \$8.6 million as the Ministry now has an improved understanding of agency participation in the contract.
  - a reduction in the admin fee charged to agencies for the External Recruitment from 1.5% to 1.0% of spend. This has meant that agencies will now realise a greater levels of savings.
  - the Ministry continuing to review the cost savings methodologies used to track and forecast savings.
- 8 It is pleasing to see that during the period from October to December there was a significant lift in the number of schools sourcing goods and services from the AoG contracts. In particular there has been growth in the number of schools accessing the Desktop and Laptop and Office Consumable contracts. The Ministry is now working closely with the Ministry of Education and Genesis on a gas for schools initiative. The initiative is likely to result in savings averaging around 20% for participating schools. This will build on the reticulated gas contract that I announced in October 2013 that will deliver \$8.6 million in savings over the next three years.
- 9 The Ministry is currently considering responses from electricity panel suppliers for a fourth tranche under the AoG Electricity contract from April 2014. The fourth tranche is made of up 29 agencies, some of which participated in the first tranche in 2011.
- 10 I announced the establishment of an AoG contract for Advertising services in May last year. To provide a broader government wide solution across all aspects of media purchasing the Ministry is currently progressing two further AoG contracts for Media Buying and Design. The Media Buying contract will complement the existing AoG Advertising contract which covers the creation and management of services.
- 11 Some contracts established at the start of the government procurement reform programme are shortly up for renewal. The Ministry undertook detailed analysis of the supply markets and agency satisfaction for office consumables and print; and considers that at this point it is appropriate to extend the current contract arrangements. New contracts will be retendered in 2015.
- 12 Audit New Zealand recently assessed the Ministry's procurement practices. The audit reviewed the methodology and savings calculations for the AoG contracts and specifically tranche three of the AoG Electricity contract. The review commented that the Ministry's activity was robust and in places exemplifies best practice.

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### *New AoG contracts*

- 13 I reported in the last quarter that the Ministry has been investigating the potential for AoG contracts for Building Materials, Consultancy and Banking Services. The Ministry has been assessing how the government can reduce construction costs by targeting the cost of building materials used for our procurement activity. Building Materials typically account for 30-60% of construction project costs and are likely to account for \$3.3 billion in costs to government per annum. Approximately \$1.7 billion per annum can be attributed to the Canterbury rebuild.
- 14 A discussion document was issued to industry in late 2013 which received 75 responses. The response was mixed with some respondents supportive of an AoG solution for Building Materials. Withheld under S9(2)(gi) of the Official Information Act 1982
- 15 Officials have designed an approach using sub-categories of building materials targeted through iterative tender processes. Timber and steel will be the first sub-categories for which the government will go to market in April and May respectively. These sub-categories account for between \$500 million and \$600 million per annum, and are areas where the market is currently experiencing some pressure. The Ministry will be working closely with key agencies such as the Canterbury Earthquake Recovery Authority.
- 16 A similar approach will be taken for consultancy services, where AoG contracts will be established as contracts for sub-categories of consultancy services. This is a dynamic sector so contracts will be open where suppliers will be able to enter through the life of the contract if they meet set standards. The procurement focus will be on the quality and value for money of services provided recognising suppliers for strong performance. The first AoG consultancy contract will cover audit and assurance, accounting, procurement / logistics, taxation, finance and economics. This will be followed by contracts for IT Consultancy and professional services related to construction where agencies have strong demand.
- 17 The Ministry has been working with the Treasury to progress the development of an AoG contract for Banking Services. The contract activity will focus on establishing a new contract for core transactional banking services, purchasing cards and possibly foreign exchange. School banking services, offshore foreign currency accounts and wholesale cash management facilities will be out of scope of the current AoG banking activity. The Ministry will go to market in the second quarter of 2014 for a contract establishment in the first quarter of 2015.
- 18 By establishing a single lead for the relationship with provider(s) of banking services the government will achieve improved consistency, manage risk and provide greater innovation. Withheld under S9(2)(gi) of the Official Information Act 1982

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### *Other collaborative contract opportunities*

- 19 In addition to the AoG contracts there are a number of other areas of spend where clusters of government agencies could further leverage their aggregated spend to realise improved pricing and performance.
- 20 Several syndicated and common capability contracts<sup>1</sup> are currently being progressed. As I have previously commented these contracts continue to be led by the same small group of agencies. It is pleasing to see that Land Information New Zealand and Statistics New Zealand are leading syndicated activities. I have asked the Ministry to encourage further agencies to lead collaborative procurements and to identify appropriate incentives. Figure 1 below provides an overview of the collaborative procurement in progress.

*Figure 1: Collaborative contracts in development*

<b>Category</b>	<b>Lead agency</b>	<b>Progress</b>
Construction consultancy	Ministry of Social Development (MSD)	Currently being reviewed
Geospatial data	Land Information New Zealand	Initial planning documentation to be reviewed
Dog Food	Ministry of Primary Industries	In market
Drug Testing	New Zealand Defence Force (NZDF)	Contract finalisation
Furniture	MSD (Property Management Functional Leader)	Common Capability – initial planning stages
Contact centre knowledge and case management	Department of Internal Affairs (DIA) – ICT Functional Leader	Common Capability – early stages
Office Productivity as a Service (OPaaS)	DIA – ICT Functional Leader	Common Capability – preparing final contract
Optimise HR	DIA/MBIE	Initial stages of development
Security services (card access, guards, CCTV)	NZDF	Initial planning stages
Meeting room technologies	Statistics New Zealand	Contract negotiation

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<sup>1</sup> Syndicated contracts involve a lead agency establishing a contract that can be accessed by other government agencies. Common capability contracts may allow private sector suppliers to purchase under the contract when acting on behalf of an agency, and the lead agency may charge participating agencies a levy or fee.

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### Increasing performance, adding value and maximising results

#### *Building Capability*

- 21 The Ministry continues to consult agencies about a whole of government approach that would extend the mandate of the Functional Leadership initiatives in regards to procurement. The whole of government approach would see the Government Rules of Sourcing extend their current application to include a further 109 government agencies including Crown Entities, District Health Boards, and Crown Agents. This will bring improved consistency and practice across government and support procurement functional leadership. The Minister of State Services will report back in early April summarising the feedback from the consultation with these agencies, but there has generally been support for the extension.
- 22 A new measure introduced through the Rules of Sourcing is that public service agencies are required to submit their significant business cases<sup>2</sup> to the Ministry for review. The reviews focus on commercial and procurement planning aspects of business cases and are aligned with the Better Business Case function led by the Treasury. It is pleasing to see that some Crown Entities and healthAlliance have submitted significant business cases to the Ministry for review – even though they are not required to. Within three months the review function has touched over \$1 billion worth of procurement activity.
- 23 Already the reviews have provided some insight to government agency procurement practices. In particular while agencies are performing well in terms of their tendering approach, they need to improve their analysis of the supply market and current spend activity, as well as better defining the business needs driving their procurement.
- 24 Over time, this review will provide important insight into where capability building effort should be focussed and help identify opportunities for government to better coordinate its procurement activity. A number of initiatives currently in place will overtime improve this practice. For example the Procurement Academy continues to provide procurement education to public servants. Procurement guidance, tools and templates developed to date have focussed on a number of issues identified through the review of significant business cases.

#### *Commercial Pool Initiatives*

- 25 The Commercial Pool is currently working on 20 projects. Detail on some of these projects is provided in Annex 1.
- 26 Cabinet recently tasked the Ministry with assisting CERA in the establishment a construction centre of expertise, to support CERA in procurement activity related to the Canterbury rebuild [CAB Min (11) 13/9 refers]. This work is being completed by the Commercial Pool. It's focus will be to provide specialist assistance and advice to CERA and other public sector organisations responsible for government funded projects, to help them bring innovation to procurement that is appropriate to the situation and market conditions developing in Christchurch.

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<sup>2</sup> The significant business case reviews apply to procurements worth over \$5 million that are not subject to the Treasury's Gateway Review and Better Business Cases processes.

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- 27 The Pool is also providing specialist procurement support to the selection of new Default Providers for Kiwisaver. This saw a Request for Proposal released to the market in late December 2013. Evaluations and moderation were completed in February. Following Ministers approval negotiations will be completed with successful respondents. Final appointment remains on track for 31 March 2014.
- 28 The NGO Streamlined Contracting work continues to progress well. The Ministry has agreed transition plans with all key government agencies who contract with Non-Government Organisations (NGOs). Training materials have been developed and the supporting programme commences on 13 February and runs for two months with a target to train key personnel within government agencies and NGO providers who are having their contracts transitioned to the new contracts by 1 July 2014. The Ministry will be supporting agencies during their transition.

### **Create environment for New Zealand businesses to succeed**

- 29 We were clear when we established PFL that we wanted the Ministry to not only lift procurement capability across government and realise further savings, but to enable opportunities for New Zealand businesses to succeed.

#### *Strategic supplier engagement*

- 30 Suppliers tell us that government fragmentation is a major source of frustration and means that the government is not getting best value from its supply base. As part of the Procurement Functional Leadership programme the Ministry has recently begun a pilot project to consider how the government can increase value from its supplier base by better engaging its strategic suppliers [SEC Min (12) 10/2refers].
- 31 The strategic supplier engagement project will seek to influence relationships with suppliers in areas that are considered high value and /or high risk. This might in some cases be to develop a relationship with a supplier that has a minority market share but is an emerging player in order to improve competition and drive innovation.
- 32 The pilot will run for a 6 month period. Four suppliers have been selected for the pilot project based on the size and spread of their activity across government or because they are an emerging supplier that could be developed to improve competition and drive innovation. These are Hawkins, Fulton Hogan, Datacom and Fronde. The pilot project will involve the Ministry, DIA, New Zealand Trade and Enterprise and New Zealand Transport Authority.

### **Consultation**

- 33 The Treasury, State Services Commission, Property Management Centre of Expertise and Government ICT Supply Management Office have been consulted in the preparation of this paper. The Department of Prime Minister and Cabinet has been informed.

### **Financial Implications Human Rights and Legislative Implications**

- 34 This paper has no financial, human rights or legislative implications.

### **Regulatory Impact Analysis**

- 35 A regulatory impact analysis is not required for this paper.

### **Publicity**

- 36 A redacted version of this paper will be published on the Ministry's website.

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### Recommendations

It is recommended that the Committee:

- 1 **Note** that savings from the all-of-government contracts grew to \$107.3 million by 31 December 2013;
- 2 **Note** that the Ministry will go to market for all-of-government contracts for media buying and design in the fourth quarter of 2013-14 respectively;
- 3 **Note** that the Ministry will go to market for all-of-government contracts for timber and steel in April and May 2014 respectively;
- 4 **Note** that the Ministry will go to market for an all-of-government banking services contract by May 2014;
- 5 **Note** that the Ministry will go to market for an all-of-government contract consultancy services for audit and assurance, accounting, procurement / logistics, taxation, finance and economics at the end of April 2014;
- 6 **Note** that a pilot project is underway to consider the government can engage with its strategic suppliers to realise improved performance in key areas of spend.

**Hon Steven Joyce**  
**Minister for Economic Development**

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