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Government Procurement



Procurement takes center stage

How the financial crisis
has put the profession
in the spotlight

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Procurement takes center stage



With states facing epic budgetary challenges, procurement is playing a lead role in driving savings – and challenging the status quo.

BY DAVID YARKIN

It is widely believed that the economic crisis that America now confronts is the worst since the Great Depression. Businesses, politicians, central banks and families all are working feverishly to devise plans to weather the storm that no one expects will pass anytime soon. This month, we interviewed procurement directors from five states to learn how this environment is affecting procurement operations in their states, how they are ensuring operational continuity in the face of severe budget cuts and what silver lining, if any, can be found amid the dark economic clouds.

Through these interviews, it became apparent that the crisis is affording procurement directors a rare opportunity to make systemic changes in government contracting, with the possibility of tipping the balance in favor of dynamic changes over a status quo that resisted adoption of best procurement practices.

Reading the state-of-the-state speeches or budget addresses from the nation's governors is enough to sober even the most wide-eyed optimist. Nearly universally, states face staggering budget deficits that threaten government's ability to maintain its critical infrastructure, protect its citizens, care for the needy and educate its children. Just as this article was going to press, President Obama signed a \$787 bil-

lion stimulus package into law. While the package may mitigate some budgetary challenges, for states the picture is bleak from coast to coast. Forty-three states are running budget deficits. California's \$42 billion deficit has been well-publicized, but smaller states are equally impacted. Arizona and Nevada's deficits are roughly 30 percent of their entire budgets.

Vikings helping Packers

Against this backdrop, states are taking actions today that few would have thought possible even six months ago. Government employment, once perceived as a lifetime guarantee, is no longer sacred. As of February, 11 states had announced layoffs totaling more than 7,000 positions to deal with budget deficits in the current fiscal year. As governors and legislators negotiate budgets to deal with even more crippling fiscal year 2010 deficits, those numbers will only rise. Twenty states have implemented hiring freezes, and nine have dipped into rainy-day funds. Education funding has been cut for the first time in years, with 18 states cutting higher education and 14 cutting K-12 budgets. Most states have asked or required their agencies to make significant cuts, either through an across-the-board cut or more targeted cuts.

A number of governors have mandated purchasing moratoriums. Brad Douglas, commissioner of the Georgia Department of Administrative Services, reports that Gov. Sonny Perdue has put a hold on the purchase of vehicles, equipment and supplies, and travel and conference attendance has been curtailed except for meetings deemed vital to the state's business.

States have become increasingly creative in dealing with their budget deficits. Among the more innovative concepts was an announcement by the governors of Minnesota and Wisconsin to find opportunities to consolidate and share services between the two states. That the announcement was made by Minnesota's Republican Gov. Tim Pawlenty and Wisconsin's Democratic Gov. Jim Doyle makes the initiative even more remarkable.

Minnesota's Kent Allin, the state's chief procurement officer, is optimistic that the initiative will bear fruit.

"The impact of the two governors' new directive has been to proactively review existing and pending contracts within the two states to identify additional short- and longer-term options for greater collaboration," Allin said. "We are finding that, as neighboring states, our proximity may create some opportunities, particularly for services and for those commodities with unique shipment and distribution challenges."

Allin noted that new joint contracts are under discussion in areas including vehicle maintenance, software, salt and law enforcement vehicles. The states also may pursue sharing existing contracts established by one of the two states in areas such as software licenses, courier services, tires, desktop computers, institutional food, copiers and purchasing cards.

Both governors have directed their cabinet secretaries to report back to them with cost-saving ideas. Highlighting the need to drive savings in the very short-term, Pawlenty and Doyle have asked for reports back by Feb. 27. The country will be watching to see how successful these two states are in finding efficiencies across borders. As Pawlenty said, "We're not proposing to merge the Vikings and Packers, but we are going to seek out every area where we can save money and improve services by working together across state lines. This is an historic agreement between our two states that can serve as a model for the rest of the country."

Added leverage

There is no question that the financial crisis has caused enormous pain for the American people and threatens to cause additional hardship for the foreseeable future. But procurement professionals, to a person, expressed much hope and optimism about what the crisis means to the procurement profession in the public sector. Every procurement director I spoke to told me that the crisis helps to create an environment that is conducive to good procurement practices.



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– Alice Small, acting director, New
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A number of states have begun renegotiating existing contracts as a way to drive immediate savings. With spending by the private sector drying up, government contracts have become all the more important and attractive for suppliers. Procurement directors have recognized that this fact tilts the balance in the government's direction, giving them more leverage in negotiations.

Alice Small, acting director of the New Jersey Division of Purchase and Property, explained that the state has launched an aggressive negotiation strategy with its incumbent suppliers, negotiating every renewal.

"I say to my staff now, "You have more leverage than you know," Small said.

Florida's Charles Covington, director of state purchasing, echoed Small's belief that the current environment makes renegotiation a successful strategy.

"Renegotiating contracts has been a lot more successful now and wouldn't have been in other budget times," Covington said. "Any opening in our contract, we are jumping on it, trying to get better deals, better

service and better cost avoidance. The suppliers' business has fallen off so badly, they want to increase market share in government to compensate for lost business elsewhere. This gives us more leverage."

Covington warned that renegotiating an existing contract is not as simple as demanding a price reduction.

"At renewal time, we are telling our suppliers that we are considering re-bidding rather than renewing. This is a real possibility, not just an idle threat," Covington said. "However, to be successful, it requires us to get much more knowledgeable about the market and to fully understand the risks involved for both the state and the supplier."

Rob Wynkoop, deputy commissioner of the Indiana Department of Administration (IDOA), encouraged procurement professionals to view renegotiations from the supplier's perspective as well as the government's side.

"It has to be seen as a win-win rather than just the state demanding lower prices," Wynkoop explained. "Can we extend a contract for a longer period in return for savings now for the taxpayers? Can we ask the suppliers to help us find cost savings in our existing contracts?"

As an example, Wynkoop pointed to his office supplies contract.

"We have been working to have our agencies buy the supplier's branded product rather than the name-brand product. They are comparable quality and a lot less costly."

Georgia's Douglas points to wider adoption of the state's procurement card as another procurement-led initiative that has helped to drive savings in this budget environment. As the state has reduced employees statewide, it has fewer staff available to process time-consuming and costly paper payments, making P-cards a more attractive option.

"It takes less manual effort and administrative cost when the P-card is used instead of the traditional requisition, purchase order and a single-check request for a given purchase," Douglas explained. "More oversight is available on these purchases, and along with increased efficiency, the P-card is our preferred method to purchase goods and services."

In New Jersey, the budget crisis has changed the dynamic between state purchasing and other state agencies, Small noted. Whereas agencies historically have been able to make purchasing decisions without being questioned, now the Division of Purchase and Property has begun playing a more active role.

"Every expenditure is now scrutinized, and all discretionary spending has been cut off to the best of our abilities," Small said. "The Office of Information Technology is reviewing individual purchase orders to ensure that funds are spent only on true needs. We are scrutinizing every sole-source request. Before we start a procurement on behalf of an agency, we make sure the purchase is appropriate. This is not a role we played previously."

"Now we ask if the procurement meets the criteria of criticality and necessity. For example, we cut off the purchase of calendars since nearly everyone has calendars on their computers. There was some pushback, but we say, 'Come on guys,' and the agencies generally understand."

State contracts gaining attention

A number of procurement directors noted that the challenging economy has hit local governments harder in some cases than the state government. As a result, some local governments that otherwise thrived on their autonomy and preferred managing their own procurements are using state contracts more regularly.

In his state-of-the-state address in January, Minnesota Gov. Tim Pawlenty encouraged greater use of state contracts by local governments.

"Minnesota has 490 school districts and charter schools, each of which purchases IT, food services, textbooks and supplies," Pawlenty said in the address. "We should require them to come together for bulk purchasing in order to lower costs and eliminate waste. This will put more money in the classroom, exactly where it belongs."

"... We should also require local units of government to use the leverage of the state's buying power to purchase commodities such as road salt,

paper and IT services at a reduced price, unless they can find a better price themselves."

Minnesota's Allin pointed out that the "better price" exemption is important, since state contracts may not always be the lowest-priced contract in the market, for a number of reasons. First, the state may have standardized on specific items, driving down the cost on those items but potentially driving up the cost of other items that local governments may need. Allin also noted that the state may have specific terms and conditions that are intended to add value to the state or protect the state, or that are statutorily required. Some of these clauses may add to the overall cost of goods and services on state contract. Still, Allin believes that on many occasions, the state contract is the best option for Minnesota's local governments.

Allin noted that the state's publicly funded colleges and universities that historically tended to assert their independence from state government have recently exhibited "an encouraging degree of willingness to look at use of state contracts and other collaborative procurement opportunities."

Fewer barriers to strategic sourcing

Procurement directors also cited the budget crisis as enabling wider adoption of strategic sourcing. In years past, procurement directors found that sourcing commodities such as office supplies or vehicles – items used by every agency – was relatively easy to implement, but that for contracts that were viewed as more agency-specific, there often was enough resistance put up by agencies to stop projects in their tracks. Today, however, with states desperate to find savings, arguments such as "We've always done it this way" are falling more frequently upon deaf ears.

Wynkoop cited an innovative sourcing project that the Indiana Department of Administration is leading as an example of the renewed leverage that procurement has over once-powerful agencies. The effort will be geared to choosing a single supplier to provide law enforcement prod-

ucts such as armor, ammunition and uniforms through a single bundled procurement.

"Historically, each agency would procure each of these buckets through separate, one-off contracts," Wynkoop said. However, by aggregating the buying power of all agencies that purchase these products and consolidating contracts for related products, IDOA expects to see significant savings and service enhancements. In better budget times, central procurement likely would not be able to wrest control of these procurements from the agencies. But, in today's economic climate, "the budget pressure gives IDOA a lot more clout," Wynkoop noted.

Small seconded Wynkoop's assertion that the budget crisis has empowered state purchasing to delve into areas that were once the protected domains of the programmatic agencies.

"Treasury has taken the lead in organizing a groundbreaking effort in setting up cross-agency teams to procure goods and services together, rather than having agencies buying things like uniforms separately," Small said. "This effort is truly unprecedented in New Jersey."

Procurement's profile

Clearly, these challenging economic times have led to a pendulum swing in the relationship between central procurement and agencies. As state deficits have widened, state procurement offices have gained a greater ability to implement sound procurement practices enterprisewide. They are driving greater savings at a time when savings are so badly needed. And they are raising their profiles within state government, demonstrating to senior managers that procurement is a function that adds enormous value in a government's operations.

So in that sense, this budget crisis has been a blessing for state procurement operations. However, as was noted earlier, many states are laying off workers, implementing hiring freezes, slashing budgets for travel and training and putting off investments in technology. How do these cuts impact procurement operations and what steps are procurement directors taking



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— Rob Wynkoop, deputy commissioner of the Indiana Department of Administration

to maintain their operations in light of these cuts?

One finding in a number of states is that procurement operations may be less impaired than other agencies. One principal reason is that in many states, the state procurement office is funded not through general government operations dollars but through a number of different special-fund mechanisms. Some states charge suppliers a small fee on every purchase off state contract by state agencies and local governments.

"We do not need a direct appropriation to expand our level of service to local governments. Consequently, we do not have to compete with education, social services, transportation and other compelling needs for limited state resources," Allin said. "We rely on modest contract fees that can support the staff that develop and manage the contracts."

Brad Douglas pointed out that Georgia's State Purchasing Division "had all state-appropriated funds pulled from it, making the unit self-funded."

"The unit creates its own funding through the collection of rebates and administrative fees placed on its state-wide contracts," Douglas explained. Impressively, the transition to a new funding mechanism was completed a full 18 months ahead of schedule.

State purchasing directors also said that hiring freezes and unfilled vacancies forced them to accelerate the adoption of strategic sourcing by consolidating multiple contracts into single procurements.

"With a statewide hiring freeze, normal attrition and a retirement incentive, we now have a skeleton crew," Small said. "However, we are using this opportunity to reduce the number of contracts we have, requiring fewer buyers to manage fewer contracts."

For states that are able to fill vacancies, today's labor market may create a once-in-a-lifetime opportunity to enhance the skills and talent of the government procurement work force. In January, employers slashed nearly 600,000 jobs – the worst hemorrhaging of jobs in the United States in 34 years. Among those losing their jobs in the private sector are scores of highly talented and well-trained procurement professionals.

"The résumés coming in over the last four weeks have been remarkable," Indiana's Wynkoop said. "The talent pool is better now than ever with procurement people leaving private-sector jobs."

While we are still in the early days of the budget crisis that afflicts all sectors of American life, it appears that the crisis offers significant advantages for public-sector procurement managers. It has tilted the balance of power to central procurement offices and has helped catalyze cost-saving initiatives led by innovative procurement managers such as Alice Small, Brad Douglas, Charles Covington, Kent Allin and Rob Wynkoop. And while hiring freezes and cost-cutting measures have created challenges for every agency, procurement departments seem to be well-positioned to weather the storm. □

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