

Review of the eProcurement Marketplace for Government Organisations

Introduction

There are many myths about eProcurement that have been generated by software vendors and consultants with motivations that are likely to be based on sales targets rather than the benefit of the individual client. The following is therefore an attempt to provide an independent view of the marketplace in order to facilitate a better understanding of the realities.

One of the overriding beliefs in eProcurement, was that put forward by software houses was that the average cost of a transaction was between £70 and £100. By moving to eProcurement, it is possible to reduce these costs by between £30 – £60 per transaction. Oracle have been one of the leaders in this in respect of quoting in their advertising that they have saved £1bn within their own organisation. In general, the proponents of such benefits fail to differentiate between efficiency gains and realisable cash releasing savings. Moreover, broad generalisations need clarification through a robust business case and Return On Investment (ROI) that should be ideally included in the contract if it is based on the supplier's figures.

But what is eProcurement? A possible answer is “Whatever one wants it to be”. Whatever the definition that is used (and there are many) it is simply:

“Technology that enables best price and processes”.

The purest view of having every part of the purchasing cycle for all suppliers undertaken in a paperless environment fully integrated into respective back end systems will be, for many years yet, an expensive dream. In the real world technologies that provide benefits now at a reasonable cost is the way to manage the high level of risk with the current level of maturity of eProcurement tools and general technological development.

Current Situation

The Marketplace for eProcurement is still very immature for a number of reasons. The overall effect, however, is that relatively few organisations are actually using much enabling technology. And those that are tend to be in the piloting stage or have limited use. In government, the Office of Government Commerce (OGC) decided to “kick-start” eProcurement by paying for seven eProcurement pilots to be run in Government Departments and Agencies in order to learn lessons about the approach, impact and benefits. These only lasted about six months and were completed at the end of June 2002. The systems were taken out and the Departments concerned started again from scratch to acquire an eProcurement system.

In local government, the IDEA:marketplace has come on-stream (but not with the full suite of functionality that is intended to be delivered). As at November 2004 it has approximately 14 Local Councils using the system but the throughput is very low (5%?) compared to the overall spend of the Councils. The marketplace offerings of Best Value Procurement/LloydsTSB including Roses Marketplace and London Marketplace are having reasonable success but the throughput is still relatively low. The business model approximately replicates the Public Marketplace concept that has achieved little success in the private sector despite many millions of pounds being put into it. It is also similar to OGC's Shopping Mall concept that was discarded in mid 2000.

Following the e-tendering piloting with Trustmarque OGC decided not to continue with eTendering due to the current lack of readiness of the supply-side. This caused some confusion to the status of various local and Central Government initiatives in online tendering that were aimed at meeting the 2002 target of all Government tendering to be undertaken online.

In respect of Government organisations the "2005" target of having all Government Services available electronically has focussed attention on using enabling technology for eProcurement. But there is a lot of confusion as to what "eProcurement" means; what benefits can be derived from using it; what costs are likely to accrue; and how appropriate is it for the particular organisation given their spend and the type and number of suppliers in their unique supply chain. OGC view is that "There is currently no policy specific to eProcurement" (OGC Website FAQ's).

The use of the Government Procurement Card in its own right and as a vehicle to "close the loop" (i.e. deal with payments) in online purchasing either in virtual "embedded" form or more conventionally has been relatively successful. The time lag of the take-up of the GPC since its introduction in October 1997 means, however, that many government organisations are still striving to meet GPC targets that are out-of-date with enabling technology and best value in the marketplace. While the GPC can be the most appropriate tool in many instances, for regular low value/high volume ordering, consolidated and/or electronic invoicing is likely to be more cost effective and efficient and therefore represents better value for money.

Part of the overall confusion may stem from the level of procurement development within an organisation. The move up the "best practice" learning curve through iterations of decentralisation - centralisation to decentralisation, through desk-top ordering using centrally contracted framework agreements has required, over the last ten years or so, substantial change management to keep up with the pace. Ironically, organisations that have not kept up with the pace and currently have decentralised purchasing, face far less cultural change issues than those that currently operate a largely centralised system.

One of the issues has been with senior managers in government organisations who are aware that their current financial management systems are unable to provide the management information and flexibility to manage their financial requirements in

respect of, for example, commitment accounting or Modified Historic Cost Accounting (MHCA) under the Resource Accounting and Budgeting (RAB) regime. The response has been to go out to the marketplace and seek more up-to-date and more comprehensive financial management software. Inevitably the response from the larger software companies is to offer a modular system that can be introduced incrementally and provide a full suite of integrated software products to cover the entire needs of any government organisation. This can typically include HR, Payroll, General Ledger (GL), Account Payables (AP) and eProcurement. These are now marketed as Enterprise Resource Planning (ERP) systems in order to differentiate them from the Financial Management Systems that organisations possessed.

As a result, a number of government organisations are determining their overall eProcurement requirements on a strategy influenced by the major integrated software vendors as this is seen as providing a long-term “once and for all” solution to their entire financial/Commercial related requirements. This means that competition is restricted to a small number of suppliers and tends, in practice, to be limited to SAP, Peoplesoft, Oracle and JD Edwards. The technicalities of cost and benefit in relation to interfacing rather than integrating can be blurred and confusing to buyers of such solutions. The ability to have “live” management information from a single source with “one version of the truth” can be persuasive if “the cost” and “best of breed” (which means ease of use and comprehensive functionality) are viewed as lesser considerations.

A report by Gartner earlier in 2001, suggested that very few companies would be providing eProcurement software by the year 2004. This served to further confuse and frighten the buyers of enabling technology. Moreover, the lack of truly independent advice means that proper sourcing methodology is being supplanted by buying decisions based on brand and reputation (see “The E-Business Report 2001” Andrew Cox et al). There tends to be substantial deference paid to the integrated software suppliers, for guidance on what the solution should be, without perhaps a full appreciation of the organisation concerned. Given the resource and time constraints on moving forward, decisions are being taken by the Public Sector that are likely to have long term cost, effectiveness and efficiency implications that may not have been appropriately considered.

It is relevant that the Private Sector, as a whole, is now taking more time to “justify” the contribution of new IT applications in terms of the benefits that will accrue rather than follow what appears to be the current “flavour of the month”. There has been a number of unpublished (because of the likely effect on stock market valuations) examples of expensive forays into the software market for eCommerce that have failed to deliver hardly any benefits while costing many millions of pounds. Three recent cases that have come to light in press reports are the Ford motor company that has tried to implement Oracle and has returned to its previous legacy system after four years; Sainsbury’s who have decided to write off millions of pounds invested in supply chain management; and Avis that has recently discarded an ERP implementation at the cost of millions.

Part of the reason for the confusion in respect of using enabling technology is the lack of understanding of where it fits in with purchasing. This is in no way surprising as the information on it is mostly derived from the software vendors who are keen to sell software that provides substantial theoretical benefits but have not, in many cases, managed to deliver them. Moreover, in respect of government, this is further confused by the view that PFI or PPP has been the accepted way of financing ICT deals. This policy was changed in June 2003 by HM Treasury for the reasons given below but there are many Government organisations that remain locked into long-term deals.

The reality is that expensive technology today is (almost) worthless tomorrow as hardware and software prices reduce and performance and functionality increase almost exponentially. This in turn results in the banks managing the risk of having an asset of marginal worth, by securing a heavy financial premium for providing the initial finance (Second Review Of The Private Finance Initiative By Sir Malcolm Bates 19 March 1999 refers). Such organisations have little option but to pay the level of costs, as it could be argued that there is a virtual cartel in the marketplace brought about by the small number and size of the companies involved and the management of risk by the financial institutions.

The situation is further exacerbated by the increase in the number of outsourced “Partnering” arrangements in central and local government. With the outsourcing of strategic decision-making and the supply of ICT infrastructure there has been a substantial decline of competition in the marketplace. While this not only goes against the “competition is the cornerstone of Government procurement” (Setting New Standards” Government White Paper May 95) there is, in relation to eProcurement, less choice and a higher risk of an expensive, slow and unsuccessful outcome.

Key to managing the inherent risks associated with Partner arrangements are the initial terms of the contract; the seniority of the individual with ultimate responsibility for contract management; and the experience and knowledge of that individual concerned. In practice, optimisation of the three areas has been difficult to achieve. Changes brought about by government departmental reorganisations and restructuring that were not anticipated, when the initial contracts were agreed, is becoming a real issue as many of the contracts are “binding” for several years.

An eProcurement project is a high risk, though potentially, high benefit complex project. It affects most parts of any organisation and the supply chain. The fact that it is difficult to achieve has slowed the pace of take-up as the least risk option is to “wait and see” how the early adopters, or other centrally resourced projects, get on.

The supply side is also, on the whole, adopting a “wait and see” attitude to on-line trading. The reality of the cost implication of another “route to market” that may not be used or may not be the right solution for its customers has limited the take up. RS Components, one of the leading exemplars of on-line trading only transacts approximately 9% of its business online. It is not currently invoicing any customers electronically and had, at one time, about 100 pilot eProcurement projects running

with customers. None of these customers (with the exception at of UKAEA) had fully rolled out an eProcurement system. Moreover, the number of expensive failures in the marketplace of various business models has not helped the take-up. Commercial organisations are therefore wary of the benefits as was discovered by OGC when trying to adopt stationery suppliers for their eProcurement pilots project.

The current trend in the market is for eProcurement software to be stretched at both ends in terms of functionality. It is, for example, moving into the financial management area to include invoice settlement as part of the procurement cycle. At the other end, it is moving into contract management and supplier appraisal. With more reporting tools being added in order to improve management information on procurement spend i.e. "Spend Management" together with auditing tools to manage better, the risk of fraud.

Security

There is no clear way forward on security. The predicted take up of smart cards has not happened. Public Key Infrastructure has also enjoyed minimal take up. Using the Government Secure Intranet (GSI) has, so far, not been exploited by eProcurement and it is unlikely to be the case for some time (if ever) because of the cost/benefit analysis. The requirements of Privacy, authenticity, integrity and non-repudiation are being managed by conventional IT and are tending to become the defacto standard. The accreditation to BS7799 security standards has also been slow. The security issue is thus being used as an inhibitor to eProcurement rather than an enabler.

Project Zanzibar the OGC eHub for Government Organisations and suppliers to Government will have an architecture that sits outside of the GSI. This is expected to come on stream in April 2005 once the contract is let in December 2004. OGC's sourcing project was expected to be delivered around September 2004 although the business case for the system has yet to be proven.

It is too early to say whether the use of "Government Secure Unrestricted" (GSU) which allows the supply side access to the GSI, will make much difference. Interpreting the risk, costs and benefits tends to vary on a departmental basis depending on the perceived risks, the argumentation and understanding of the various interested parties and the quality and motivation of external advice. Establishing value for money criteria can be difficult. A manual intervention solution i.e. an air gap with information transferred via a disc/CSV file regime, may prove to be an appropriate short-term cost-effective solution, pending the maturity of the various technologies involved or, possibly, acceptance of de facto use.

Integration and Interfacing

There is a fallacy among the market that integration and/or integration is difficult. While integration will (on the whole) be expensive and difficult, interfacing is usually straightforward. Many software companies and indeed consultants talk in terms of

integration possibly because it enables them to charge substantial costs. The reality these days is that the cost of interfacing modern systems should not be exorbitant and it can be done relatively quickly.

In respect of integrated suite vendors, whatever is provided in the current version of their eProcurement solution will almost certainly need other components, which are not yet available in the ERP suite. In a report by Gartner it was noted that they have not found any organisation that only uses one software solution to cover all of their eProcurement requirements. Additional third party software is required. Whether additional functionality is bought in as third party software, built to order/bespoke, or incorporated as part of a government localisations package at some future date, remains to be seen. What will have to be done to make the whole system work to meet a functional or other specification will vary. In practice, each requirement tends to be unique and most eProcurement base products are not sufficiently functionally rich to meet the requirements though configuration alone. Unlike mature financial management systems, eProcurement functionality is only now really starting to develop through customer requirements based on actual use.

The relatively few organisations that are using eProcurement tend not to have integrated them into their back-end systems. However, the ones that have tend to interface with their current systems, especially in the private sector, as they do not want to throw out their legacy Financial Management systems in order to take advantage of eProcurement. It is simply not value for money (Public Sector) or commercial sense (Private Sector) to do so in many cases.

The advent of eProcurement has heralded a different approach to integrating legacy systems. This is known as Enterprise Application Integration (EAI). The view is that the pace of change of mergers and de-mergers, means that it is not VFM to keep changing and discarding expensive software applications, to accommodate structural reorganisation. There is a need, however, to have integration in “real time” and this is achieved through middleware applications that legacy systems are plugged into (or unplugged from in the case of a de-merger) in order to achieve integration at a reasonable cost. This also allows flexibility in incorporating “best of breed” products rather than suites of products. This technology is still (Nov 2004) relatively new but could become the future of IT systems strategies.

Electronic Invoicing

While electronic invoicing is available there are no industry standards and the supplier adoption costs to implement it tend to be prohibitive. The reality is that about 90% of supplier’s invoices are still in paper form. The Government Procurement card can be used to “close the loop” but is expensive and still not ubiquitous amongst the supplier community. The revision of Article 21 of EC Directives effective from January 2004 effectively disallows the use of standard Microsoft Outlook email tools for online invoicing for Government organisations.

Conclusion

The take-up of eProcurement is approaching a crossroad with the requirement for government organisations to have everything online by 2005. Many organisations are, quite understandably, unsure of how to approach the adoption of enabling technology. Key requirements are good procurement practices e.g. eProcurement strategy, proper specification of requirement or outcomes, business case including a ROI, robust risk transfer and management. Add to this supplier competition in the marketplace for an appropriate solution that, may not be the “state of the art”, coupled with complex project management, the risks need full evaluation.

Before choosing the software, one should ask the supplier three questions:

- a. Is the functionality that is required, in the current version of the software?
- b. Who is using it in an organisation that is similar to our one?
- c. Can we speak to the person who is using it and (preferably) visit them?

Above all it is important to realise that the technologies are still relatively new, changing fast and generally not fully tested, in the Public Sector. Therefore it is essential to ensure that there is at least one person in the cross-functional project team who has had real experience of the eProcurement environment who is on the side of the client and who can challenge the assertions of the supplier.

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