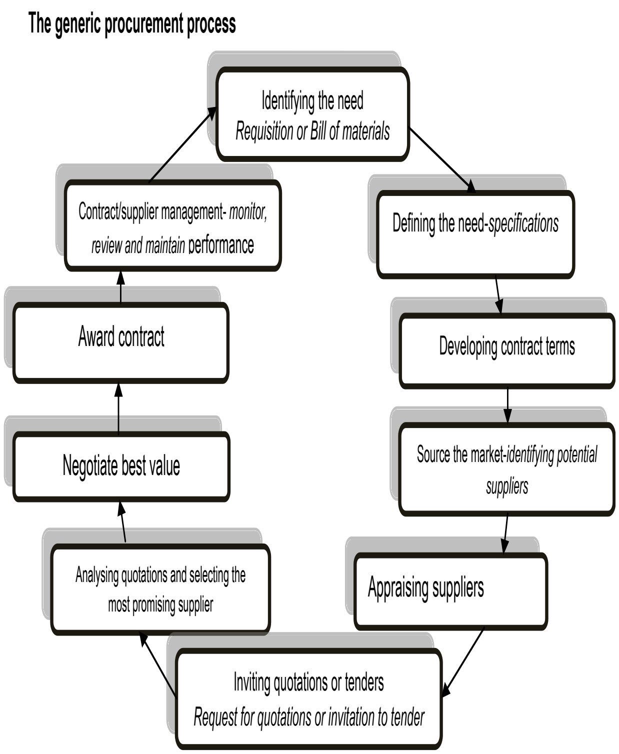
Third Issue

Procurement Principles

A Study Module for Business Administrators



By

Bukenya Peter

Chapter 1
Introduction to Procurement Management

1.0 Learning objectives

At the end of this session candidates will be able to demonstrate an understanding of the fundamental issues of procurement management by:

- *describing the key concepts of purchasing and procurement*
- *explaining the variables of procurement*
- *describing the categories of organizational procurement requirements*
- *explaining the objectives and importance of procurement*
- *appreciating the strategic contribution of procurement*
- *describing the development of procurement, and*
- *analyzing procurement in the different sectors.*

1.1 Background of Procurement

Organizations are increasingly under pressure to operate efficient and effective strategies within the national and international market. They rely heavily upon the supply of goods and services to maintain competitive advantage. Many organizations today no longer regard procurement as a supporting function because effective procurement makes a very big contribution to the organization's profitability and success.

This procurement coverage has been designed to provide students and practitioners of business management with the information and knowledge needed for an understanding of the factors that have led to the evolution and direction of the procurement function in order to develop knowledge of the specific contribution that strategic management of the procurement function can make to overall organizational success.

Since the 1970s, the role of the procurement function has gone through considerable changes. In the past, it was regarded as a clerical function with the objective of acquiring a good or service at the lowest price.

Management viewed purchasing as having a passive role in the organization with purchasing being an administrative rather than a strategic function. However, the 1973 - 79 oil crisis and related raw materials shortages drew significant attention to the importance of purchasing. Thus, the strategic importance of the purchasing function to the organization was beginning to receive recognition. This is what gives birth to procurement.

Purchasing is a function responsible for obtaining by exchange of cash, lease or other legal means, materials, equipment, works and services required by an organization for use in its operations or for resale. The classical definition of purchasing states, that;

> *"it is the acquisition of goods and services of the right quality, in the right quantity, from the right source, delivered to the right place at the right time obtained at the right price". All this should come with the right levels of service.* However, it has been observed that the term '***right***' is situational. What is *right*, changes with the purchasing environment.

Procurement is strictly a wider concept of acquisition than purchasing. It technically means obtaining goods and services by various means such as loans, transfer or hire as well as straight forward purchasing. It starts with need identification and focuses on customer satisfaction. The concept advocates for evaluation of the whole process at the end of each transaction for the purpose of increased improvement. Procurement embraces both purchasing and supply management so as to contribute to competitive advantage of the organisation and achieve its goals by adding value and minimizing costs.

The above definitions ground the key ***purchasing or procurement variables*** i.e. factors that guide procurement decision making. These are:

- ***Quality*** (value or dimensions that define a product's fitness for purpose),
- ***Quantity*** (volumes required),
- ***Source*** (supply market),
- ***Place*** (point of delivery),
- ***Time*** (when is delivery required by users?),
- ***Price*** (cost of the procurement-focus on total cost of ownership), and
- ***Service*** (meeting expectations of users).

1.2 Difference between Purchasing and Procurement

1. Purchasing is ***transactional*** with its primary concern being the mechanics of order placing on a one-off basis. While procurement is ***relational*** in that it seeks to establish where appropriate long-term collaborative relationships with suppliers.
2. Purchasing is ***tactical*** rather than ***strategic;*** that is, purchasing is focused on short-term buying while procurement is largely concerned with achievement of long-term corporate goals.

3. Purchasing is ***reactive;*** that is, it is a service activity buying what is it's instructed to buy while procurement takes a ***proactive*** approach that helps to determine policies of acquiring required supplies, services or works.

Because of this reactive and proactive nature, further differences between purchasing and procurement can be drawn to including (see table 1.a). *Note:* In spite of the above differences, the two terms are synonymous and therefore in practice are used interchangeably.

Table 1.a: Differences between purchasing and procurement

Purchasing – ***Reactive buying***	**Procurement** – ***Proactive buying***
• Purchasing uses *quality control/value analysis* as an approach to quality management - rejects defective materials.	• Procurement uses *quality assurance /value engineering* in approaching quality management - avoids occurrence of defective materials.
• Purchasing is a cost center i.e. it is involved in simply determining what is to be spent on the acquisition of required supplies, services or works.	• Procurement focus is value addition i.e. procurement is a value adding center which aims at minimization of waste throughout supply chain operations.
• Receives specifications, terms of reference, and scopes of works from user departments and designers.	• Procurement and suppliers contribute to specifications, terms of reference, and scopes of works.
• Price is a key variable in making acquisition decisions.	• Total cost of ownership and value are key variables in making acquisition decisions.
• The purchaser's systems are independent of suppliers.	• Systems of the procuring organisation may be integrated with the systems of its suppliers.
• Purchasing reports to finance, marketing or production.	• Procurement is a main management function that reports to top management of the organisation like the Chief Accounting Officer.
• Problems relating to supply of required supplies, services or works are the responsibility of the supplier.	• Problems are a shared responsibility of the buyer and supplier.
• Nature of negotiations is a 'win-lose' i.e. they are competitive.	• Negotiations are 'win-win' or even better i.e. they are collaborative.
• Many suppliers are regarded as security against risk of supply failure.	• Many suppliers are viewed as lost opportunities to minimize cost, manage quality, obtain commitment, etc.
• Holding stock is security against stock outs.	• Holding stock is waste.

Procurement describes the range of activities that are responsible for buying the materials needed by an organization. It is generally responsible for getting materials from suppliers into the organization. Many organizations use the terms purchasing and procurement to mean the same thing. Generally, though, purchasing refers to the actual buying of materials procurement has a broader meaning and can include purchasing, contracting, expediting, materials handling, and transport, warehousing and receiving goods from suppliers.

1.3 Categories of organizational procurement requirements

From the above definitions, it can be drawn that the categorization of organizational procurement requirements includes supplies/goods, services and works.

- **Supplies or goods** are tangible requirements of relatively low value compared to works and services classified as:
  - *Consumables* - obtained for consumption or short-term usage, usually are repetitive needs of relatively low value compared to capital supplies e.g. stationery, fuel, food supplies, etc.
  - *Capital supplies* - obtained for long term usage in an organization's operations usually of high value compared to consumables, they are of non-repeat nature as one item of the kind may procured over a long period of time. They include: computer supplies, vehicles, furniture, land (as classified under the PPDA Act), etc.

On the basis of purpose for which they are procured, supplies are classified as:

- *Revenue supplies* - these are either consumables or capital supplies procured for resale to generate revenue,
- *Repair, Maintenance and Operations (MRO) supplies* e.g. grease, oils, spares parts, chains, gauges, fixtures,

On the basis of state in which they are along the supply chain, supplies are classified as:

- *Raw material supplies* - inputs into the production process,
- *Finished goods* - supplies that have completely gone through the production process ready for distribution to users for consumptions, and
- *Work-in-progress (WIP) supplies* - undergoing conversion from material state to finished goods supplies.

- **Services:** Defined in the PPDA Act 2003 as amended, services are;

  'any object of procurement or disposal other than works and supplies, and includes professional, nonprofessional and commercial types of services as well as supplies and works which are incidental to, but not exceeding the value of those services.'

In Lysons and Farrington (2006) services are defined as:

> *'all those economic activities that are intangible and imply an interaction to be realized between the service provider and the consumer.'*

Lalatin has advanced different types of services to include:

- ***Personal:*** these include; *technical, editing, translation, and appraisals.*
- ***Professional:*** *consultancy services such as management, legal services, medical services, insurance services.*
- ***Support:*** *Administrative, financial information management, procurement and logistics services.*
- ***Personnel:*** *recruitment, selection, training and development, welfare services.*
- ***Construction:*** *building repair, alteration, restoration, maintenance services.*

In the broader perspective of procurement, services are classified as *consultancy* and *non-consultancy* services being those provided by professionals and non-professional individuals respectively.

Services are characterized by the following;

- *Intangibility* i.e. a service is a process or act. The result of a service transaction is not a transfer of ownership as with supplies.
- *Simultaneous production and consumption* i.e. the actualization of a service implies the presence of the service provider as well as the consumer or client. They both play an active part in the realization of the service.
- *Perishability* i.e. unlike supplies or tangible goods, services cannot be stored and used or resold at a future.
- *Heterogeneity* i.e. services are not homogeneous. Services are never the same and even within what appears to be the same, it may not be the case. There is a high risk a service being performed differently depending on factors such as the provider of the service, the client or customer, the physical setting or even the hour of the day.

From a procurement perspective, there are other characteristics. Boshoff suggests that, because of their intangibility, services are riskier to procure than physical products. This enhanced risk is due to:

- Service buyers only knowing what they have bought after the buying decision,
- The high level of human involvement and interaction, which makes the standardization of a service not only difficult but, over time, almost impossible.
- Customers differing in the amount of information they seek before procuring a service and satisfaction depending on factors such as prior experience and recommendations.

Boshoff suggests that service guarantees reduce the anxiety and uncertainty of potential service buyers.

- Specifications for goods are generally more specific than service statements of work.
- Cost analysis and negotiation are more difficult with services than for goods.
- Services are likely to become a significant proportion of total spend as many non-core service competences are outsourced.

❖ **Works:** As defined in the PPDA Act, 2003 as amended, works is;

'any work associated with the construction, demolition, repair, or renovation of a building or structure, on the surface or underground, on and under water, and includes the preparation, excavation, erection, assembly, installation, testing and commissioning of any plant, equipment or materials, decoration and finishing, turnkey projects, build own and operate projects, build operate and transfer projects, or any arrangement of this nature, or any other form of private and public partnerships or joint development activities, all or any of which may include management, maintenance, testing, commissioning and training; as well as supplies or services incidental to those works where the value of such incidental supplies or services does not exceed the value of the works.'

Procurement of works is thus concerned with civil engineering construction and the supply and installation of plant and equipment, their repair and maintenance as well as demolition or disposal of such plant and equipment. It looks at how institutions procure plant and equipment so as to provide the needed services.

Generally, there are three broad types of works: building construction, heavy / civil construction and industrial construction. However, it includes specific undertakings such as;

1. *Construction of buildings or housing blocks (building works)*: that is it looks at how school and office blocks should be constructed so that the institutions can be able to fulfill their objectives. This also includes houses/ buildings for public consumption such as public schools, hospitals, ministry houses, Airports, etc.
2. *Construction of roads (road works)*: Procurement of works looks at how the nation's entities both central and local select the best construction companies for particular types of roads within the country. For instance, major road construction works throughout the country vested in Uganda National Roads Authority-UNRA. It also treats how those potential construction companies or agencies shall be evaluated at the end of their assignments as well as monitoring any sub-contractions during the performance of their activities.
3. The *building of dams and other power generating plants*: Procurement of works looks at the best locations for dams and other power generating plants in the country. Building of dams requires a lot of assessments like the environmental

impact assessment (EIA) and the actual construction work involves engagement of highly technical contractors involving even consultancies for such works. Such highly technical contractors are usually obtained from the international supply market because of the limited domestic capacity in Uganda.

4. Construction of *sewerage works and water works* and *their systems*: that is, the management of sewage-waste water or effluent and the provision of water to the community require construction of pipelines, drainage channels, and waste water management plants with a concern for aesthetics. This is calls for engagement of those contractors will address the network or layout required during construction of structures. It should be noted that even this involves moving earth both on and underneath. Consider the sewer and water works undertaken by National Water and Sewerage Corporation-NWSC, Uganda.
5. Construction of *bridges*, *flyovers* and *tunnels*: Procurement of works looks at bridge(s) and flyover construction by identifying the best locations and the different contractors. Also, constructions that take place below the land surface like tunnels are considered as works.
6. Any Earthworks including digging of valley dams, drainage channel digging and construction works, and excavations.
7. Installation of plant, machinery and equipment for factory works and farm works.
8. Repair and maintenance services on all such works.

1.4 Objectives and Importance of Procurement

The purpose of procurement is to make sure that materials needed to support operations are available at the time they are needed. Obviously, if a process does not have the materials it needs, it cannot work properly. Perhaps operations are interrupted, customer demand is not met, costs are too high, deliveries are delayed, or productivity is reduced.

The primary aim of procurement is to obtain the correct equipment/materials, supplies and services in the management of quantity or the management of quality from the management going at the right time and cost. It has however, a whole of other duties as an organization's "*window-on-the-world*", providing any information on new products, processes, materials and services.

Procurement should also advise on probable prices, deliveries and performances of products under consideration by the research, and the design and development functions. Since the total cost of bought-out-items may form a very large proportion of the final selling price of the organizations' product or service, purchasing is an extremely important specialized function which should never be under estimated.

Specific objectives of procurement are to ensure;

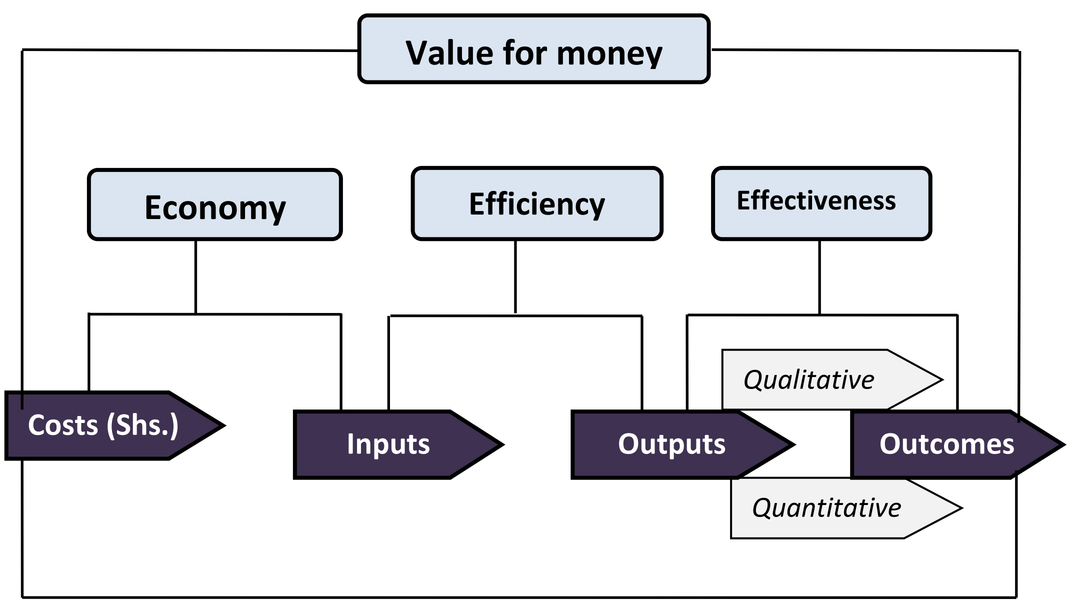
- the availability of relevant services when they are needed by the user departments,
- appropriate use of funds without fraud and corruption,
- efficient use of funds or getting the most from a fixed sum of money,
- accountability to relevant stakeholders that funds were properly utilized to realize the set goals,
- value for every shilling spent, and
- the realization of policy objectives.

1.4.1 The Value for Money (VFM) objective

It is the objective of all procurement professionals to ensure value for money is achieved in all procurements. Value for Money is about obtaining the maximum benefit over time with the resources available. It is about achieving the right local balance between economy, efficiency and effectiveness (see figure 5.a) or, spending less, spending well and spending wisely to achieve local priorities…VFM is high when there is an optimum balance between all three elements, when costs are relatively low, productivity is high and successful outcomes have been achieved."

"*Good value for money* is the optimal use of resources to achieve the intended outcome".

Figure 5.a: Defining value for money



In the achievement of value for money simply means achieving the worth of every unit currency spent or exchanged for supplies, services or works. Focus here should be on;

- ***Effectiveness***: - 'doing the right things' Qualitative and quantitative measures of increase or decrease in outcomes that show that a programme 'is effective in delivering its intended objectives'. This examines the relationship between outputs and outcomes. Thus, this requires aligning procurement and disposal activities with overall corporate goals and objectives.
- ***Efficiency:*** - 'doing things right' or 'a measure of productivity, in other words how much you get out in relation to what is put in' i.e. that is putting entity resources to the right use. This examines the relationship between inputs and outputs; for example, planned versus actual delivery of milestones by service providers, or benchmarked comparison among activities working to same or similar outcomes but using different pathways to achieve intended outcomes. Hence, funds should be allocated and used for appropriately for the allocated procurements in accordance with the set budget.
- ***Economy:*** is 'a measure of what goes into providing a service'. This costs inputs. Unit costs are typically used as an economy measure. 'The whole life costs of inputs such as the direct and indirect costs of acquiring, running and disposing of assets or resources should be considered'. Maximizing value at minimum cost should be the thinking in procurement activities.
- ***Enhancing:*** i.e. augmenting, improving, and intensifying those procurement practices that are regarded effective, efficient and promoting economy. It is about adding procurement practices that are efficient, efficient and promoting economy throughout the procurement process in order to realize greater levels of value for money.

1.4.2 Functions of the procurement function

- Identifying the needs of a particular organisation
- Identifying the right suppliers of the required goods, services or works
- Negotiation with the identified supplier of the required goods where there is need
- Placing an order upon agreement with a particular supplier
- A continuous following up; especially for complex items, services or works
- Receiving and inspecting the orders to-ensure that they conform to

the agreed specifications and conditions

- Auditing to ensure that the value for money principle is being adhered to.
- Processing payment upon satisfaction by the auditors and inspectors
- Opening and closing a file
- Carrying out research to improve future purchasing inefficiency and effectiveness.

1.5 The Evolution and Development of Procurement

The evolution of procurement has been summarized into 4 stages: -

- **Product - centered purchasing**: This was mainly focused on the product and put much emphasis on the *rights* which concentrated exclusively on the purchase of tangible products.
- **Process - centered purchasing**: This was also product focused but moved further to examine the outcomes and 'begin to measure the process through which the outcomes is delivered.
- **Relational purchasing:** This was a further refinement of the process centered purchasing. It expanded to include buyer-vendor relationships and how these could be used to manage the quality and nature of the supplier.
- **Performance - centered purchasing**: This stage focused on the best method of product management and employed a methodological integration to manage relationships, process and outcomes. It emphasized cross functional training of procurement professionals and measurement of procurement performance in terms of contribution to firm success.

1.5.1 Development of procurement as a strategic function

Today procurement has elevated to a strategic function in organisations. There are several factors explaining this drift and these factors are grouped into 3 categories; background factors, developmental factors and internal organizational factors.

Background factors

- There is an *increasing emphasis on core business*. A lot of non-core activities are being outsourced e.g. transport, security, catering, etc. This has led to increased demand in procurement related skills.
- The realization that some resources are *finite* thus the need for their proper

management.

- Organizations today need to be more *flexible and responsive*. They cannot be so unless their suppliers are also flexible. This has led to the increased attention to the procurement function.

Development factors

- *Changing partners of trade;* - Buyers today no longer need to buy locally just because of the global village concept. The development of large trading blocs like COMESA, SADAC, ECOWAS, European Union, etc. has opened up market and increased competition.
- *Government intervention*; - Globally governments have realized change in stand in terms of procurement in both local and central governments. The implications of the above have led to procurement reforms that are aimed at adopting the best practices in procurement.
- *The growth of professional bodies* like "CIPS" and "ISM": These bodies have spent considerable time and efforts at national and international levels, demonstrating the importance and contribution of effective procurement of both private and public sectors.
- The *leading-edge concept; -* The development of concepts and techniques such as Just-In-Time (JIT), Total Quality Management (TQM), Customer Focus, Lean Supply, Supply Chain Management (SCM) and Electronic Data Interchange (EDI), have had an important impact on the development of procurement. If the procurement function is not well developed, the implementation of these concepts will almost be impossible.
- *Competitor activity*; - As competition increases among organizations, the tendency of fighting-costs becomes a critical issue. The procurement function has been found to be one of the leading areas where costs can be effectively managed.
- *Customer demands*; - Globally, customers are increasingly demanding for better services at the same or even less costs. Therefore, the need to manage quality and costs right from input, through and out of the organisation- a role in which procurement is a prominent participant.
- *Technological changes; -* Technological progress necessitates that organizations should have formulated plans to handle any development taking place hence the development of e-procurement, Electronic Funds Transfer (EFT), Electronic Point of Sale (EPOS), etc.

Internal organizational factors

- *Performance measurements;* -these has been increased emphasis on Performance measurement within organizations that measure the contribution of the purchasing and supply, its status has been effectively affected.
- Top management has -become aware of its *contribution to cost reduction* and its *strategic capabilities.*
- The *level and percentage of bought-out-items;* - As the external expenditure increases as a proportion of the total, greater attention is paid to the input activities. Such expenditure is of crucial importance and needs close attention at policy level.

Chapter 2

Supply Chain Management

2.0 Learning objectives

At the end of this session candidates will be able to demonstrate an understanding of the fundamental issues in supply chain management by:

- *describing the concepts of the supply chain*
- *explaining the elements of supply chain management (SCM): materials management, logistics management, work-in-progress management, and physical distribution management*
- *explaining the objectives of SCM and procurement contribution to SCM*
- *appreciating the strategic contribution of procurement to SCM*
- *describing the concept of lean supply and how it can be achieved, and*
- *evaluating the importance of SCM.*

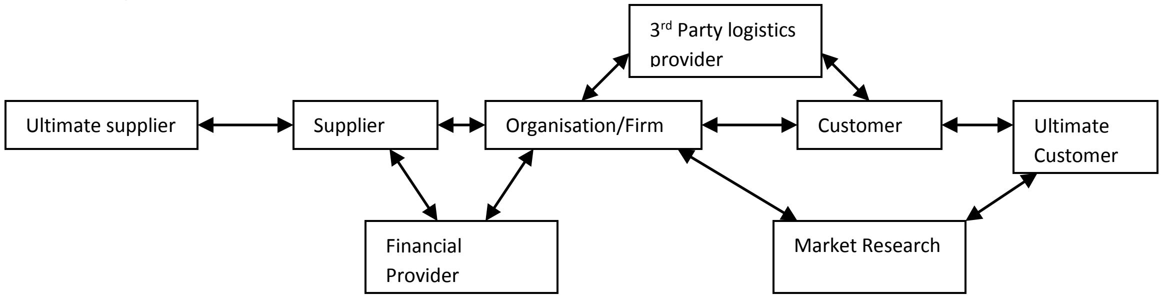
2.1 Supply Chain Management

The term **"supply chain"** is defined as the interconnected set of business procedures and business parties that manage the flow and delivery of information from the point of design to the delivery of the product or service to the final consumer.

A **supply chain** also refers to the flow of materials and information through a business from the initial function through the operation and eventually to the consumer. The organizational process of making a product and selling it stands between the supply market and the customer market.

The **Supply chain** refers to a network of organisations that are involved, through upstream and downstream linkages, in different processes and activities that produce value in the form of products and services in the hands of the ultimate customer or consumer.

Illustration:



This movement of materials can be very complicated. If you think of even a simple product, like a cotton shirt, it has a long and difficult journey **i.e.** from the farm growing cotton to the final customer. The supply chain for even a sheet of paper can involve many organizations. These include loggers, chemical companies, paper makers, transport operators, wholesalers, retailers, and many others. This journey does not happen by chance, but need careful planning and co-ordination which is the function of logistics.

Thus, the ***supply chain*** is all those specific actions required to bring specific products from raw materials to a finished product in the hands of the consumers. It should be noted that every product has got its own supply chain. Supply chain exists in every organization whether they recognize it or not.

- In a manufacturing environment, it is straight forward to trace the material and product flows that link the supply chain.
- In non-manufacturing organization, information flow and services may be traced in addition to product flows.
- Every organization has unique chains tracing distinct flows and all organizations regardless of sectors benefit by tracing their own chain and determining the supply chain management strategies that will fit best.

2.1.1 Characteristics of the supply chain

a. Supply chains are multi tied i.e. they span beyond an organization's immediate suppliers and customers.
b. Supply chains are customer driven.
c. Supply chain management is an ongoing journey and not a destination.
d. Supply chain management (management) activities are good procurement activities but good procurement activities are not necessarily true supply chain management activities.

Supply Chain = Suppliers + Logistics + Customers

Logistics and the supply chain are concerned with *physical* and *information* flows and storage from raw material through to the final distribution of the finished product. Thus, supply and materials management represents the storage and flows into and through the production process, while distribution represents the storage and flows from the final production point through to the customer or end user.

Supply chain management may be described as the integrated approach to planning and controlling the flow of materials from the suppliers through the distribution channels to the end user. It emphasizes the management of *upstream* and *downstream* relationships and the law of supply chain optimization in increasing customer value at the lowest cost.

- The interface between the operation and the first-tier supplier, is the focus of traditional purchasing and supply management activity (upstream only).
- The interface between the operation and the first-tier customer is termed as *physical distribution management* (downstream only).

Supply chain management is the term used to describe the management and coordination of all the activities both upstream and downstream.

Logistics management *is … the planning, implementation and control of the efficient, effective forward and reverse flow and storage of goods, services and related information between the point of origin and the point of consumption in order to meet customer requirements* (CSCMP, 2006).

Logistics *is… the positioning of resource at the right time, in the right place, at the right cost, at the right quality* (Chartered Institute of Logistics and Transport (UK), 2005)

For most organizations it is possible to draw up a familiar list of key areas representing the major components of distribution and logistics. These will include transport, warehousing, inventory, packaging and information. This list can be 'explode' once again to reveal the detailed aspects within the different components. Some typical examples are given in *figure 2.b.*

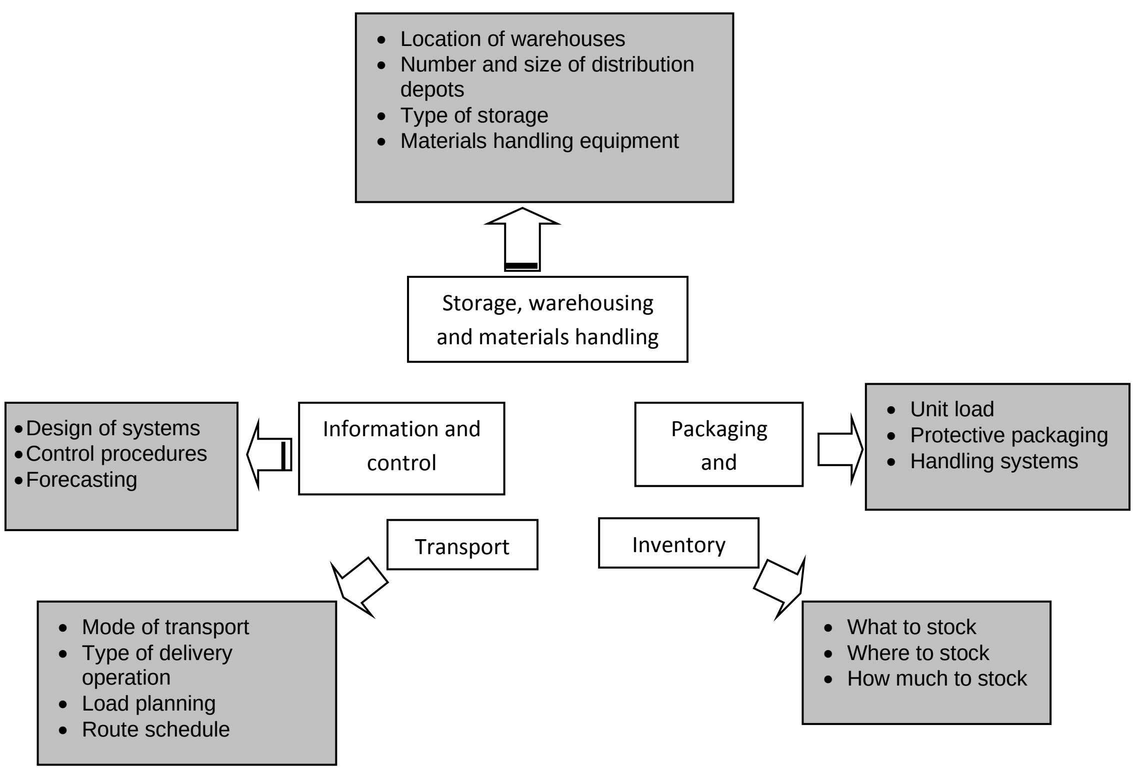
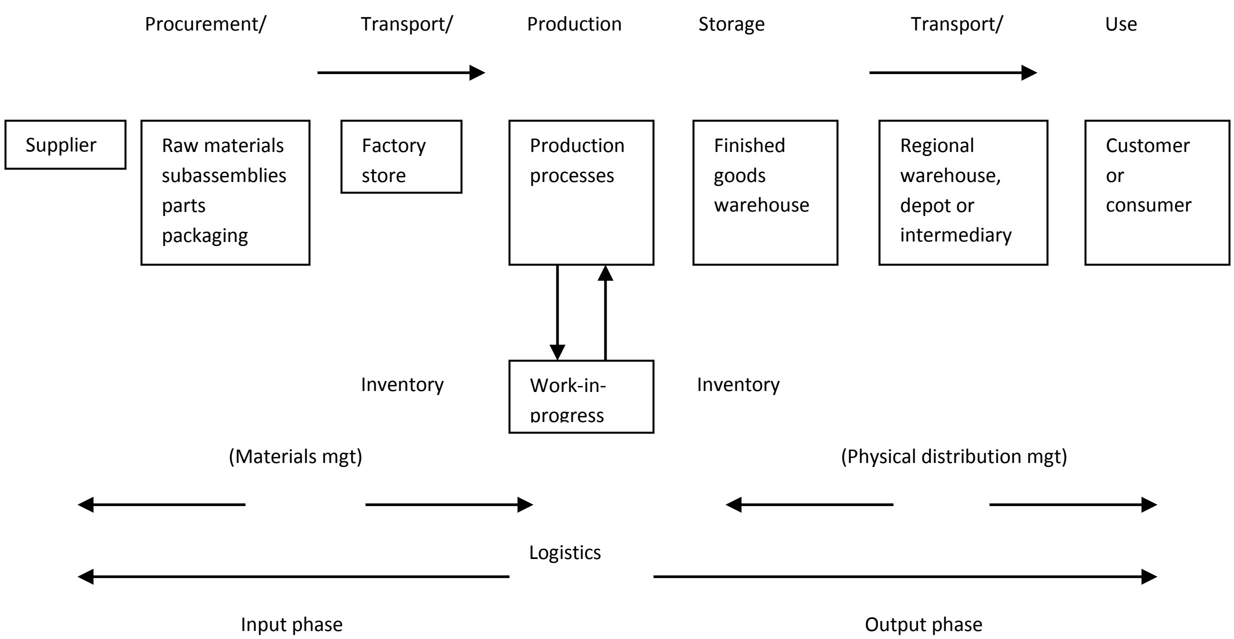


Figure 2.b: The key components of distribution and logistics, showing some of the associated detailed elements

Logistics is responsible for the physical movement of all materials through an organization. Logistics really looks at three types of movement:

- **Movement of raw materials;** where materials are moved from supplies *into* the organization. Here logistics is concerned with purchasing, inward transport, receiving, storage and retrieval of goods.
- **Movement of work-in-process;** where materials are used *within* the organization. Here logistics looks at handling, movements and storage of goods during operations.
- **Movement of finished goods;** where materials are moved from the organization out to their customers. Here logistics looks at packaging, storage and retrieval from warehouses, shipping and distribution to customers.

Sometimes it is convenient to break the logistics function into parts. Then **materials management** is responsible for the first two of these-movement of materials into and within the organization. **Physical distribution** is responsible for the third–the movement of finished goods out to customers. Unfortunately, there is some confusion in these terms as many people use the terms 'logistics', 'physical distribution' and 'materials management' to mean the same general function.



Logistics controls the flow of materials through an organization on their journey from suppliers, through operations, and on to customers. But the final product of one organization is the raw material of another. For example, petrol is a final product of BP, but a raw material for Pickford's Removals. So, materials are actually moved through a series of organizations. This is called a **supply chain**.

2.1.2 Objectives of Logistics

The different functions of an organisation in some cases have conflicting objectives. Whereas Finance may opt for low stocks everywhere, Marketing and Production require high stocks of finished goods to satisfy customer demands quickly and high stocks of raw materials respectively.

With such conflicting objectives, compromise is clearly needed. Having one function (logistics) in charge of all material movement is a best way of overcoming this conflict to obtain a balance in objectives and get good results for the organisation as a whole.

- The main objective of an integrated logistics function is moving all materials into, through and out of the organisation while making the best use of available resources, and guaranteeing customer service.
- This is summarized in the aim of supplying, 'the right materials, to the right place, at the right time, from the right source, with the right quality, at the right price.'

These give specific objectives of logistics to include:-

- Give uninterrupted flow of materials into the organisation,
- Find and develop reliable suppliers,
- Make purchases at lowest long-term cost,
- Have efficient movement of work-in-progress,
- Give efficient movement of finished goods out to customers,
- Minimize costs of holding stocks,
- Maintain high quality, and
- Maintain good relations with suppliers and customers.

2.1.3 Functions of logistics

If you think of the integrated logistics function we have been describing, it includes a number of other functions. These include:

- **Procurement or purchasing;** which is responsible for buying the raw materials from suppliers.
- **Traffic and transport** which moves the raw materials from suppliers to the organization's receiving area.
- **Receiving** which unloads the trucks bringing in raw materials inspects the goods for any damage, and checks the goods delivered are the same as those ordered.
- **Warehousing or stores** which stores materials until they are needed, and takes care of them.

- **Inventory control** which deals with the replenishment of stocks and controls inventory levels.
- **Material handling** which moves the materials needed for operations during the process.
- **Shipping** which takes finished products, checks them and loads them onto, say, trucks for delivery to customers.
- **Distribution** which delivers finished products to customers
- **Location** which decides how many warehouses should be built and where they should be.
- **Communication** which keeps all records for the logistics system.

If you want to reduce the cost of logistics, you have to look at all of these functions. Trying to reduce each cost separately might actually increase the overall cost. This is because many of the costs need a balance. For example, purchasing could reduce the unit cost of a raw material by buying large quantities, but this increases the cost of inventories. Or traffic might reduce the cost of inward transport by using local suppliers, but this might increase the purchase price.

2.2 The contribution of procurement to supply chain management

- Provides expert analysis for forecasting, servicing, and delivering and supplies information throughout the supply chain
- Provides critical information to strategic management on price, availability and supplier issues.
- Enhances long-term relationships with key suppliers and resolves problem that may arise.
- Secures the maximum possible value in engineering costs through the implementation value engineering and value chain analysis.
- Enables effective negotiation of the best terms in respect to transformation and distribution.
- Advises on major sourcing policies such as *make* or *buy* decision, outsourcing, leasing etc.
- Ensures that procurement staff training provides an understanding of all the elements of the supply chain system.

2.3 Benefits of Supply Chain Management

- Reduction in internal organizational conflict.
- It encourages inter-departmental cooperation and makes team work much easier.

- Improvement in communication within the organization and the external stakeholders.
- Adoption of modern concepts in materials management such as Just-In-Time (JIT), Materials Requirements Planning (MRP I), Total Quality Management (TQM), etc. becomes easier.

2.4 Lean Supply and Supply Chain Relationships

Lean supply is a set of ideals which aim at providing maximum customer satisfaction or delight at minimum total cost to the entire supply chain.

It is an approach that focuses on satisfying fully the end customers' requirements at a minimum cost by eliminating waste wherever it exists in the supply chain.

Note: In lean supply, the customer is not a king but a partner.

2.4.1 Lean thinking

This is a way of looking at the supply chain with the view of cutting out waste wherever it exits in the supply chain. The supply chain should therefore be turned into a ***value chain***.

Waste: - it is the opposite of value and it refers to any human activity which absorbs resources but creates no value. For example;

a) Over production
b) Waiting
c) Un necessary transportation
d) Overstaying
e) Inspection, Etc.

Therefore, ***Value Chain = Supply Chain - Waste***.

2.4.2 Achieving Lean Supply

1. Specify value as defined by the end user or consumer m terms of quality, availability, packaging, etc.
2. Identify the supply chain and cut out the unnecessary steps. Review all the specific actions required in producing a specific product or service from raw materials stale up to the finished product ready for consumption.
3. Make the remaining value steps flow. With the elimination of non-value adding activities, you have a value chain. Focus on the product and its need rather than the organization or equipment so that all activities needed to produce that item occur in a continuous flow.

4. Let the customer pull the product from you as needed rather than you pushing the product to the customer.
5. Seek perfection i.e. cultivate a culture of continuous improvement and remember to benchmark with the best industry.
6. Ensure good communication between you and your supplier.

Chapter 3

The Procurement Process and Documentation

3.0 Learning objectives

At the end of this session candidates will be able to demonstrate an understanding of activities in the procurement process and roles of stakeholders by:

- *describing the activities of procurement process*
- *examining the elements that impact upon the effectiveness of the procurement process*
- *identifying the roles and responsibilities of different stakeholders in every activity of the procurement process, and*
- *identifying the content and flow of every document in the purchase cycle as well as analyzing the importance of every document in the purchase cycle.*

3.1 Introduction

The Procurement cycle is the cyclical process of key steps when procuring goods or services. This interactive tool has been developed the Chartered Institute of Purchasing and Supply (CIPS) to guide members through the procurement process with links to relevant knowledge to support you every step of the way through your procurement journey. CIPS provides a generic procurement process to involve the following steps;

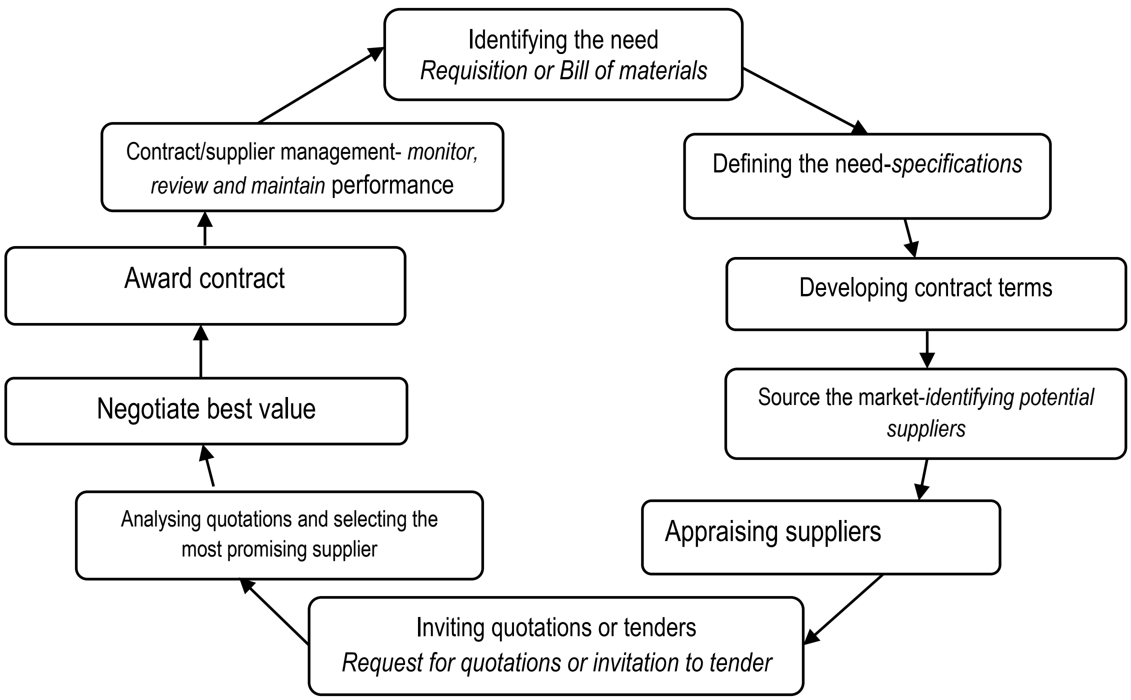
a) Identifying the need-Requisition or Bill of materials
b) Defining the need-specifications
c) Developing contract terms-preparation of tender
d) Source the market-identifying potential suppliers
e) Appraising suppliers
f) Inviting quotations or tenders-Request for quotations or invitation to tender
g) Analyzing quotations and selecting the most promising supplier
h) Negotiate best value
i) Award contract
j) Contract/supplier management-monitor, review and maintain performance

Thus, the procurement process should integrate the following steps;

Determining /Identifying Needs

This is the very first stage in the actual procurement process where departments/ services identifies their needs and send them to the procurement officer where they are unified to produce procurement plan. Here the basic need of the stakeholder(s) is explored, options considered, and the requirements briefly described as the basis for a plan and a specification. Procurement officers should not take the initial need for granted, but rather they should engage in a process that evaluates the needs and considers alternative cost-effective solutions.

Chart 3.a: The generic procurement process



Some 'needs' may already have been met by a previous and or by a current contract, the item sought may already be in stock from an alternative economic operator, or a potential purchase could be aggregated with other forthcoming purchases so as to present a more attractive supply opportunity to the supply market. Good practice by ensuring that there is a need that a procurement officer should not simply be a rubber stamp, Auditors will want to understand that there is a clear need.

Assessment of Commodity and market price (include make or buy assessment): Once the business needs are outlined and a high-level specification developed the next stage is to research the options available in the marketplace. By scoping out your spend and current positioning and dynamics of the marketplace you can start to identify potential suppliers and degree of competition in the marketplace. At this stage analysis can be conducted on whether to make or buy the product or outsource the service.

Procurement planning and budgeting

Procurement planning is a key function in public sector organizations. Its objective is to provide the organization with continuity of inputs (procurements) to enable it to achieve strategic objectives. It refers to the setting of procurement targets and activities by an organisation in a manner that spreads them out in an annual calendar in accordance with the availability of resources and needs.
This involves identifying what supplies, services or works are required or needed, quality and quantities needed, scheduling of delivery and also allocating funds (financial votes) to such procurements in accordance with the available and expected funds flows.

The procurement planning and budgeting process should rationally be aimed at;

- Avoiding emergency procurement
- Aggregating requirements both within the entity and between entities to realize value for money and reduce procurement cost.
- Making use of framework contracts wherever appropriate to provide an efficient, cost effective and flexible means to procure works, services or supplies that are required continuously or repeatedly over a period of time.
- Avoiding the splitting of procurements defeat the use inappropriate procurement methods like micro-procurements.
- Integrating, the procurement budget with the entity's expenditure programme.

Planning and budgeting for procurements is undertaken by User Departments, Boards or Councils and consolidation of such plans is undertaken by Procurement Units.

Procurement requisitioning

This involves a particular User Department requisitioning the procurement of particular supplies, services or works. The requisition should be filled with a clear *statement of requirements*; - detailed description of the procurement requirement. Such a statement of requirements in respect of;

a) Supplies is a *specification*,
b) Services is the *Terms of Reference* (TOR)
c) Works is the *Scope of Works* (SOW).

These may be accompanied by drawings, bills of quantities or their equivalent.

Confirmation of the availability of funds

On receiving the requisition, the Procurement Unit (PU) must ascertain the availability of funds before proceeding further with the procurement. Upon confirmation by the Accounting Officer as per the approved budget and sanctioning of the procurement, the PU then initiates such procurement.

Note: All procurement requirements should be approved by the Accounting Officer prior to commencement of any procurement process.

Review of statements of requirements and approval of Procurement Method

At this stage, specifications, terms of reference and the scope of works are reviewed by the Procurement Unit together with the User Department. This is undertaken to check, possibilities of over specification or under specification. It is also aimed at checking ambiguity and have clear specifications to providers or bidders.

The potential supply market is reviewed for its ability to meet the procurement requirement and, thereby decide on the appropriateness of the procurement method and evaluation criteria in the standard bidding document.

The procurement method indicated to be used for the procurement of the supplies, services or works in question, must be approved by the contracts committee. Therefore, upon review of the method, the Procurement Unit should forward the method to be used to the contracts/tender committee for approval.

Preparation of Bidding Documents

Bidding documents are then prepared by Bidding Documents are then prepared by the Procurement Unit. These documents also known as solicitation documents/tender documents contain;

- Instructions to Bidders (ITBs),
- Price Schedule,
- Evaluation methodology/criteria,
- Special Conditions of Contract,
- General Conditions of Contract, etc.

Approval of Bidding Documents

The Bidding Documents are then submitted by Procurement Unit to the Contracts Committee for approval.

Advertisement and Invitations for Bids

After approval of the Bidding Documents, then the tender is advertised inviting potential bidders to express their interest to tender or supply. Such advertisement should be in the language prescribed by the organizational policy and gazetted in a media of adequate coverage to ensure a fair reach of the potential supply market.

Bidders express interest by purchasing the Bidding Documents at a non-refundable fee, have them filled and returned not later than the closing time and date stipulated in the bid notice.

Receipt and opening of bids

Arrangements are made for the receipt of filled bidding documents. They should be returned sealed with original copies and photocopies of the filled documents. They should be received by the Procurement Unit of the entity within the period stated in the bidding documents.

Note: Any bidding documents arriving after the set time and date should not be received. And for those received, a receipt note acknowledging receipt be given to the bidder submitting them.

After closure of receipt, then sealed bidding documents should be opened in the presence of bidders or their representatives at the date indicated in the bid notice and standard bidding documents. Bidders are short listed basing qualifications.

Evaluation of bids

Bids are then evaluated by the evaluation committee in accordance with the evaluation criteria indicated in the bidding documents. This is done in three stages;

i. A preliminary examination to determine the eligibility of a bidder and administrative compliance of the bids received.
ii. A detailed evaluation to determine the commercial and technical responsiveness of the eligible and compliant bids.
iii. A financial comparison to compare costs of the eligible, compliant, responsive bids and determine the best evaluated bid.

The evaluation is done using methodologies prescribed under the procurement policy or regulatory framework of the organization. Methods used usually include;

- Quality Based Selection (QBS)
- Quality and Cost Based Selection (QCBS)
- Fixed Budget Selection (FBS)
- Least Cost Selection (LCS)
- Technical Compliance Selection (TCS), etc.

After the evaluation exercise, the Evaluation Committee drafts a report of its recommendations to the Contracts/Tender Committee of the best evaluated bidder.

Review of the Evaluation Report and Award of Contract

The Evaluation Report is then reviewed by the Contracts/Tender Committee which upon review of the recommendation may approve or reject the recommended bidder. If approved, the best evaluated bidder-one offering the Most Economically Advantageous Tender (MEAT) is awarded the contract to supply.

Note: It is at this stage that, before the award decision and signing is done, negotiation may be held with the bidder if need arises.

Administrative review, market price reassessment and signing the contract
After award of contract to the bidder is made, the contract document is forwarded by the Contracts Committee to the Accounting Officer of the procuring and disposing entity for signing. And on signing the contract, the Accounting Officer communicates the award decision by notice displayed on the entity's notice-board, and also undertakes an administrative review.

Contract Management and Monitoring
Managing the contract involves implementing delivery of supplies, services or works in accordance with the terms and conditions of contract and processing of payment for such delivery. This is the responsibility of the User Department for which procurement is made or a contract management team headed by a member of the User Department or from any other User Department of the entity.

Contract Monitoring is undertaken by the Procurement Unit which measures actuals with the planned and takes corrective action for the deviations identified. The main focus is on appraising supplier performance in the delivery of the required supplies, services or works. It is aimed determining whether to maintain the supplier on list of providers or recommend for his removal.

3.2 Elements impacting on the effectiveness of the procurement process

Procurement Organisation: As an organisation, procurement structures vary depending on the culture and structure of the organisation. The structure of the team whether this be centralised, decentralised or hybrid structure on a local and/or global level, should be aligned to deliver both the procurement and organisation strategy. This structure will enable the procurement process to run effectively.

External Environment: A business does not exist in isolation and can be influenced by other factors outside of their control; this is typically referred to as their 'external environment'. The external environment consists of competitors, the economic, social, monetary system and the political/legal system and affects all parts of the procurement cycle.

E-Commerce/systems: eCommerce systems including E-Sourcing and E-Procurement are widely used by organisations to buy and sell products and can utilise technologies such as mobile commerce, electronic funds transfer, supply chain management, Internet marketing, online transaction processing, electronic data interchange (EDI), inventory management systems and automated data collection systems.

Stakeholder engagement: In any activity an organisation undertakes, whether strategic, operational or tactical, the activity can only be successful with the input, commitment and support of its key stakeholders. Gaining and maintaining the support and commitment of stakeholders requires a continuous process of engaging the right stakeholders at the right time, understanding and managing their expectations.

Sustainability/CSR/Ethics Security: In addition to traditional economic criteria such as price and quality items such as social, economic and environmental factors should be considered to ensure a sustainable solution when procuring products and services.

Sustainable procurement helps organisations to eliminate waste, become more energy efficient and inevitably save money. Corporate Social Responsibility is a way of ensuring that the business monitors its compliance with the law and industry standards and how business processes can be managed to provide a positive impact on society.

Risk Assessment/Mitigation: During various stages of the procurement cycle you should understand the risks that can impact an organisation and implement strategies to mitigate and manage those risks effectively.

Continuous improvement: Continuous Improvement also known as 'Kaizen' means 'change for the better' and encompasses all people, products, services and processes in an organisation. Continuous Improvement consists of making continual small improvements rather than big changes at irregular intervals, requiring close monitoring and control and ideally inbuilt into the organization’s culture.

People and skills: People are a key asset and arguable the most important resource in an organisation, translating other resources into added value. Therefore, ensuring you have the right skill set within the team will help to achieve the organization’s objectives. There is a diverse skill set required as you progress through the purchase order cycle in order to manage relationships and influence stakeholders and suppliers, along with analytical skills, financial analysis, through to leadership and change management skills. Therefore, it is important to periodically review and support training opportunities where necessary to ensure people feel valued and the business retains the right skill set.

3.3 Procurement procedures and documents

Procurement staffs are in many cases dealing with considerable sums of money and are in effect the guardian of the organization’s treasury. For this reason, it is important that such coordinated and defined orderly procedures are adopted by the organization in order to ensure that possibilities of fraud are reduced or eliminated.

Procedures refer to a system of sequential steps or techniques describing how a task or job is done. They are formal arrangements through which policies linking strategy formulation at all level are implemented.

A Document refers to a presentation of data in digital or any other form for purposes of exchanging information and communication.

Procurement involves three main phases each involving specific documents as indicated below: -

3.3.1 The identification phase

This phase involves notification (by the user department) of the need to procure different goods and services. It could involve the use of either of the following documents;

i) Bills of materials: This is issued by the production control in the user department requiring items from the store. If the items are not available in the store, it is the duty of the store manager to issue a stores requisition note to the procurement office.

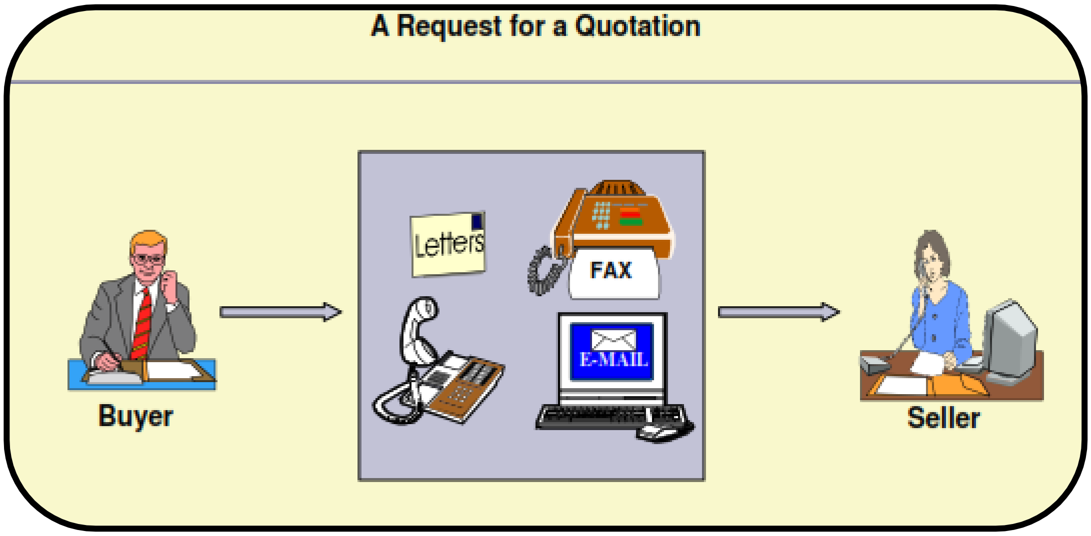
Note: - the movements of the documents
- Contents of the documents
- Importance of the document

ii) Requisition note: This is a document issued by the stores to stock control department. This note creates a record of who needs or which item is needed. It usually shows the stock level of that particular item whether zero or below minimum stock level. It also signals the procurement department to source and buy the item.

3.3.2 The ordering phase

The buyer after receipt of the requisitions or bills of materials, checks for accuracy in terms of conformity to specifications and also to identify whether it is a new purchase or a re-buy. If the item is a re-buy, then the procurement department issues a purchase order. If it is a new item to be bought then the following documents are commenced;

iii) Inquiry letter Or Request for Quotations: it is a request for information sent to suppliers. A request for a quotation is simply a letter, telephone call, fax, or e-mail message between buyers and sellers used as the initial step in a trade transaction. This is done to ascertain who is willing and able to supply and at what price and the terms of delivery.

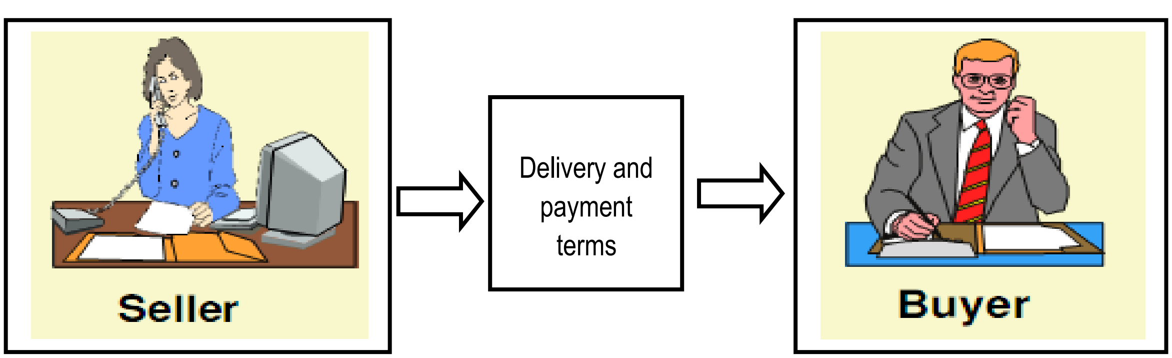


An example of a simple "request for a quotation" letter can be as below.

> Dear BMN,
>
> Please send me your quotation for 40 Massey Ferguson tractors, Model number 220HM. Please quote DDP, Luwero. Payment will be by cheque.
>
> Sincerely,
> Luwero, BuNet Trading Company

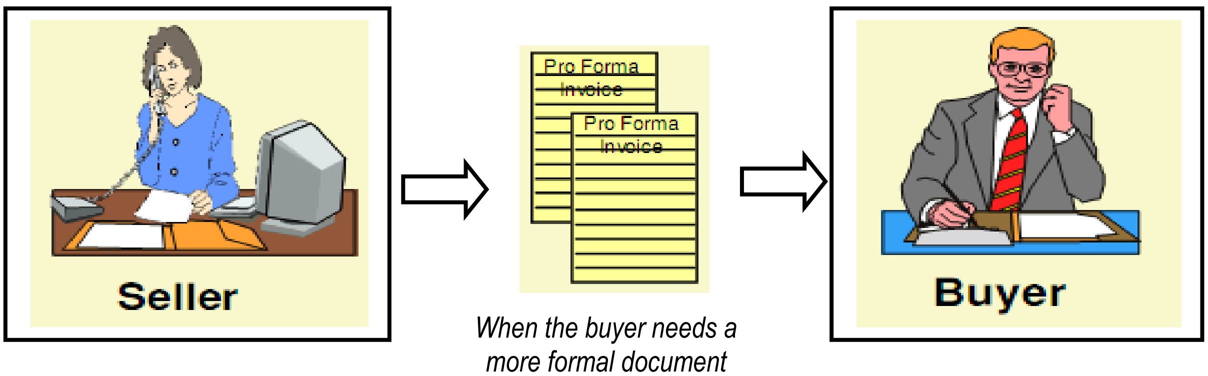
iv) Quotations: this is an expression of interest received from different suppliers in response to the inquiries. The interested suppliers make themselves known to the buying organization. Quotations show the price, quality, delivery and other business terms at which the supplier is willing to supply goods to the Organization. The quotation should be as specific as possible, to avoid misunderstandings. It is normally signed, and of course it is now possible to send E-mail messages with signature on them.

Quotation



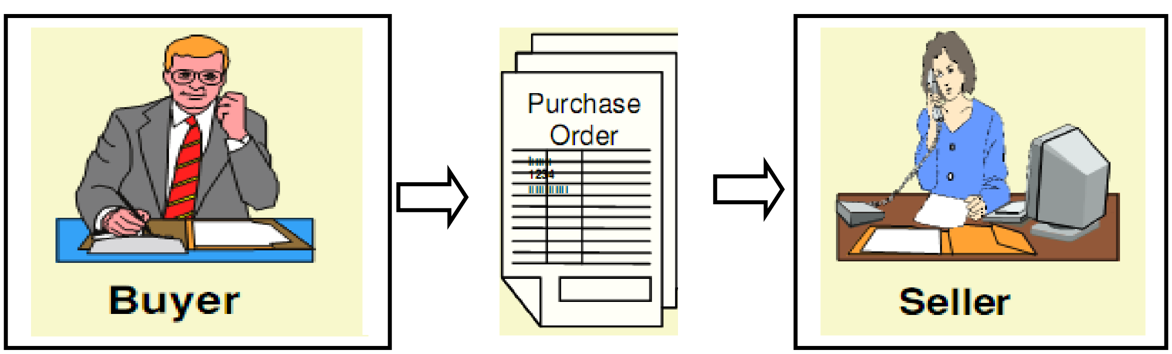
v) The Pro-forma invoice; this is a document that may be required as an alternative to or with a quotation. It is a more formal document than a quotation.
It looks like a regular commercial invoice, except that it says "PRO FORMA" at t he top. These words mean that the document in hand isn't the actual commercia l invoice but is almost exactly what the real invoice will look like.

Pro Forma Invoice



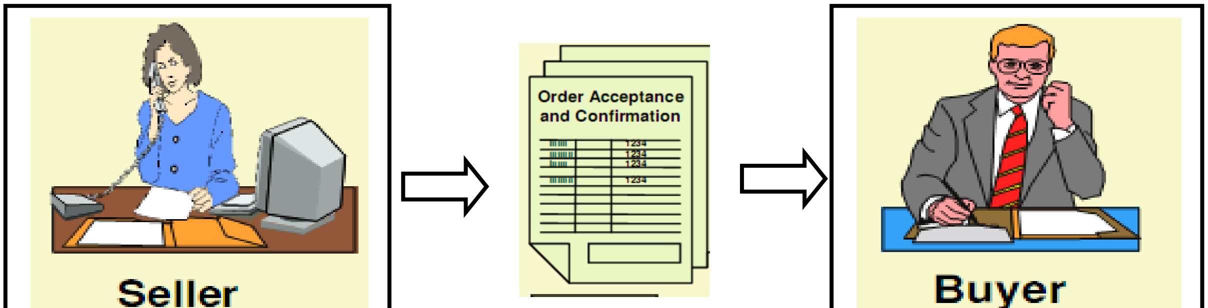
vi) Purchase order (Local Purchase Order): this is a document of acceptance issued to the supplier authorizing supply of items. It gives confidence to the supplier that he will be paid after supplying. It includes the quality of goods required, their quantity and price. It should be duly signed by the head of procurement department or general manager depending on the policies in place.

Purchase Order



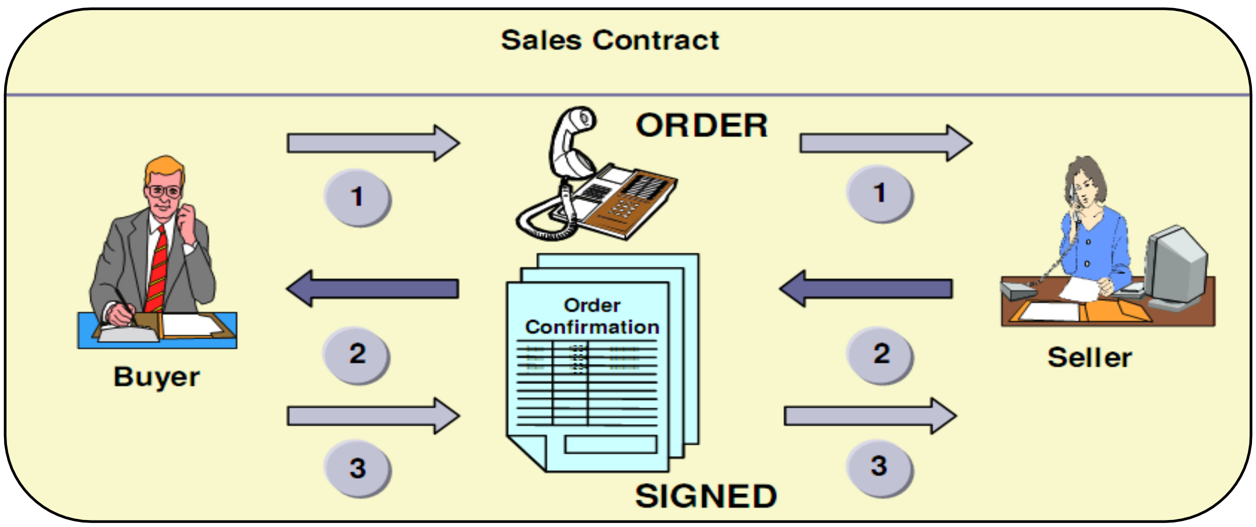
vi) Order acknowledgment note: this is normally sent by the supplier to the buying organization indicating that the purchase order has been accepted on the terms and conditions that were agreed upon.

Order Acknowledgement Note



Reply to a purchase order

When the order acknowledgement (Order Acceptance and Confirmation) note is signed by the buyer, then a ***Sales Contract*** is formed.



3.3.3 Post ordering phase

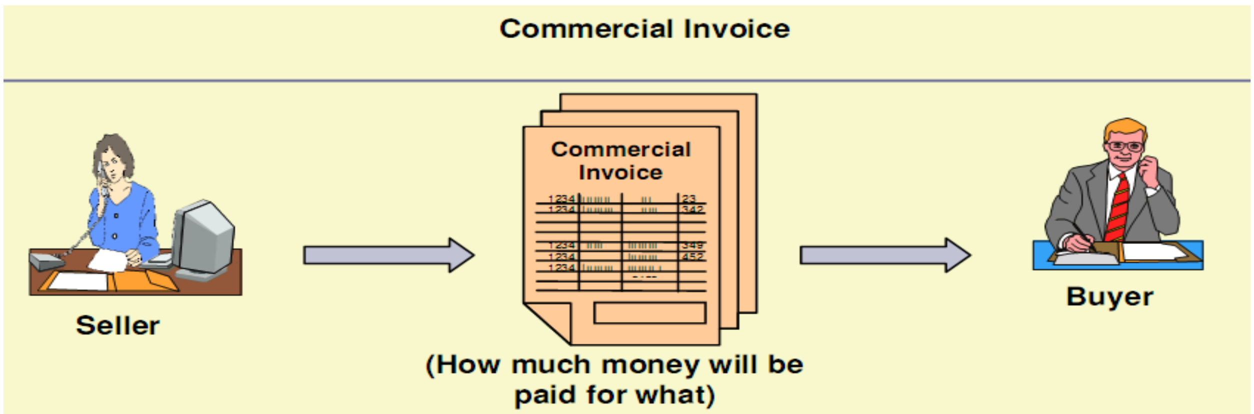
This phase involves the following documents: -

vii) An advice note: this is sent by the supplier notifying the buying organization that the goods have been dispatched or are ready for collection. This enables the buyer to make arrangements for receipt/receiving the goods.

vii) Delivery note: this is produced by the supplier on delivery of the consignment. It gives the detail of goods supplied. The receiving department does a physical examination to ensure that the document conforms to the physical delivery. The document is duly signed by the authorized receiving officer.

viii) Goods received note: This document gives a summary of the items received by the stores department and is always sent to the procurement department. The procurement department then informs the finance department that the supplier should be paid on receipt of the invoice of a particular delivery in question.

ix) Invoice: This is a document that claims payment for the goods supplied. It is received from the supplier and is compared with a purchase order and goods received note. It is then sent to the accounts department to prepare payments to the supplier.



Question: *Examine the importance of documentation in procurement.*

Chapter 4

Procurement values and principles

4.0 Learning objectives

At the end of this chapter candidates will be able to demonstrate an understanding of procurement values and principles by:

- *defining values and principles*
- *describing the CIPS procurement values and principles*
- *explaining the public procurement principles*
- *appreciating the importance of values and principles to procurement management*

4.1 Introduction

Values are principles or standards of behavior i.e. judgment of what is important in a given profession.

Principles are fundamental norms, rules, or values that represent what is desirable and positive for a person, group, organization, or community, and help it in determining the rightfulness or wrongfulness of its actions. A principle is thus a fundamental truth or proposition that serves as the foundation for a system of belief or behavior or for a chain of reasoning in a given discipline or profession. Like any other profession, procurement embeds values and principles that provide a guideline to the attainment of value for money.

4.2 CIPS Procurement values and principles

The Chartered Institute of Purchasing and Supply (CIPS) provides values and guiding principles of procurement to include the following;

Accountability: i.e. taking ownership and being responsible to stakeholders for our actions. This requires embracing the principles of;

- Applying sound business judgment
- Being knowledgeable of and abiding by all applicable laws and regulations
- Being accountable for achieving best value for the organisation's spend
- Maximizing competition to the greatest extent practicable
- Practicing due diligence
- Promoting effective, economic, and efficient acquisition
- Supporting economic, social, and sustainable communities

- Using procurement strategies to optimize value to stakeholders.

Ethics: i.e. acting in a manner true to these values. Principles that embed this value include;

- Acting and conduct business with honesty and integrity, avoiding even the appearance of impropriety
- Maintaining consistency in all processes and actions
- Meeting the ethical standards of the profession.

Impartiality: i.e. unbiased decision-making and action. This requires those involved in procurement operations to;

- Be open, fair, impartial, and non-discriminatory in all processes,
- Treat suppliers equitably, without discrimination, and without imposing unnecessary constraints on the competitive market,
- Use sound professional judgment within established legal frameworks to balance competing interests among stakeholders.

Professionalism: i.e. upholding high standards of job performance and ethical behavior. This requires the procurement function to;

- Be led by those with education, experience and qualifications in procurement
- Continually contribute value to the organization
- Continually develop as a profession through education, mentorship, innovation, and partnerships
- Develop, support, and promote the highest professional standards
- Seek continuous improvement through on-going training, education, and skill enhancement.

Service: i.e. obligation to assist stakeholders. This incorporates principles of;

- Being a crucial resource and strategic partner within the organization and community
- Developing and maintaining relationships with stakeholders
- Developing collaborative partnerships
- Maintaining a customer-service focus while meeting the needs, and protecting the interests, of the organization and the public.

Transparency: i.e. easily accessible and understandable policies and procedures. Principles to integrate here include;

- Exercising discretion in the release of confidential information
- Maintaining current and complete policies, procedures, and records
- Providing open access to competitive opportunities
- Providing timely access to procurement policies, procedures, and records.

4.3 Public procurement principles

Public procurement for example in Uganda, the Public Procurement and Disposal of Public Assets Act, 2003 as amended of Uganda like many other countries provides for the following principles to guide public procurement;

Non-discrimination: This principle requires that a bidder an interested supplier) should not be excluded from participating in public procurement and disposal on the basis of nationality, race, religion, gender or any other criterion not related qualification.

Fairness: This is the principle of equality of treatment which requires that identical situations be treated in the same way or that different situations not be treated in the same way. It does not depend on nationality (as with the principle of non-discrimination) but is based on the idea of fairness to individuals. Thus, treating two bidders from the same country differently could be unequal treatment but, since they are of the same nationality, there would be no discrimination (on grounds of nationality).

Transparency: Transparency refers to the principle that is central to a modern public procurement system, that gives to the public generally, and to the bidders' community in particular, information concerning and access to the law, regulation, policies and practice of procurement by government Procuring Entities.

Competition: From an economic perspective, "competition" operates as a discovery procedure by allowing different bidders to communicate the prices at which goods and services are available on the market. Those prices act as guideposts and reflect the demand and supply conditions at any given moment. They also reflect the differences in quality and in terms and conditions of sale of the different (non-homogenous) products available.

This is why the advertising provisions are so important, as they guarantee the widest possible competition, enabling bidders from all over the Community to communicate their prices to a given procuring entity, thus ensuring the greatest possible choice.

Procurement legislation seeks to prevent any distortions or restrictions of competition within the Community, and any attempts to prevent bidders from being able to tender will be prohibited. Such attempts can take many forms and can affect the products or services or the economic operator itself.

Economy: This is a principle that is often used to describe the technical efficiency of the procedure itself, i.e. whether the planning has been appropriate and carried out on time; whether the various responsibilities have been engaged; whether sufficient time has been given to all bidders to prepare suitable tenders; whether the procurement is made in a timely manner.

At a more "economic" level, the principle can also be used to identify whether the correct or best contracting strategies have been used to minimize waste and benefit from economies of scale.

At a policy level, the principle may be used to analyze the allocative efficiency of transactions and of the system as a whole to determine whether this can be optimized further.

Efficiency: Efficiency to speed up procurement functions is of high essence so as to avoid bogging down implementation of public programs at the expense of transparency. This means that through standardized procedures and consistent application of best selection practices minimize delays to the procurement process.

Ethics: Procurement activities in all organizations should be conducted in a manner that is ethical. Observing the codes of Ethics should be emphasized from time to time by management. In the Ugandan case, the Public Procurement and Disposal Public Assets Code of Ethics is provided for practitioners of procurement. And any other organization should also development a procurement code of ethics that will guide ethical conduct for those involved in procurement activities.

Preference and Reservation: Here, the procuring entity is required persuade providers to participate in the procuring process without regard to nationality especially within the public sector. Any reservation to this, the procuring should;

- Obtain prior written approval of the competent authority for instance the PPDA Authority in case of public sector procurement in Uganda.
- Include this exception to nationality and the grounds relied on in the bidding documents and the policies or regulatory framework in place.
- Also, a record of that procurement process should include such exception and grounds.

Open Competitive bidding: that is open competitive bidding should be the preferred method of procurement.

Best evaluated bid: The contract should be awarded to the bidder with the best evaluated bid on the basis of the methodology or criteria detailed in the bidding documents.

Public accessibility: This principle requires that copies of the procurement policies, rules, guidelines Standard Bidding Documents, procurement audits, records and dealings of the entity as well as other procurement documents should be made accessible to the public especially in the case public sector entities.

Publication of opportunities and information: The Authority should organize and maintain a system for the publication of data on public procurement opportunities, awards and any other information of public interest that may be determined by the Authority.

For instance, any procuring entity is required to advertise all bid opportunities through invitations to express interest or bid and communicate the subsequent award on its notice board.

Confidentiality: - A procuring entity is under the obligation not to disclose any information that would;

- Amount in breach of law;
- Impede law enforcement;
- Prejudice legitimate commercial interests of the parties;
- Inhibit fair competition, or
- In any way not be in the public interest, until the successful bidder is notified of the award.

The *exception to this* is when required to do so by an order of court.

Accountability: Accountability is defined as: "the quality or state of being accountable, especially an obligation or willingness to accept responsibility or to account for one's actions".

In accordance with this definition, it is said that public officials have the obligation and must be willing to accept responsibility for their actions. Accountability has a literal meaning related to counting and accounting for items of monetary value, but as a concept its expanded meaning covers ethics and corporate social responsibility.

- Procurement officers and procuring entities need to demonstrate:
- Good governance and a structure that encourages good governance
- Enforcement of internal and external legal regulations
- An absence of corrupt practices
- Accountability for their actions

In this context procuring entities are spending public money, generally derived from taxation imposed on citizens. It is therefore fundamental that Procuring Entities are made for the money spent on their behalf. Procuring Entities must therefore have structures and processes that allow them to 'account' for actual expenditure.

Chapter 5

Supplier Sourcing

5.0 Learning objectives

At the end of this session candidates will be able to demonstrate an understanding of sourcing by:

- *describing the sourcing process and policies*
- *explaining the criteria or attributes that provide the basis of supplier appraisal*
- *identifying the sources of information about potential suppliers*
- *appreciating the role of sourcing from international supply markets, and*
- *realizing the need to evaluate the factors that pose risk in the international supply markets while deciding to source from international supply markets.*

5.1 Introduction

Sourcing refers to activities involving searching market for goods and services. It also involves continuing relationship with preferred or potential sources. It involves decisions on how to allocate available business resources and what terms to do business on as well as finding new sources for existing products.

5.2 The sourcing process

1. *Establish need of the organization*; this is the first stage in the sourcing process where specifications, contractual terms, important requirements of users are established.
2. *Invite potential suppliers;* this can be through a pre-qualification for supply of various goods and services and invitation for bids/tenders or an expression of interest.
3. *Screen suppliers and develop a short list;* potential suppliers who are likely to be unable to satisfy your needs are dropped at this stage. The screening should be done on aspects of size, location, minimum order quantities, possession of ISO 9000 certification etc.
4. *Send inquiry to request for information from short-listed potential suppliers.* The inquiry may include a questionnaire for the supplier to complete and return the buyer for analysis. The inquiring should have an introduction, the type of product, experience, the number of organizations dealt with, credit facilities etc.
5. *Evaluate responses; -* potential suppliers are rated according to pre-determined

criteria that reflect the needs of the organization. The major areas of appraisal are; quality, financial, commercial, environmental and ethical issues.

6. *Select the supplier;* the supplier selected is placed on the approved list or a supplier database.
7. *Negotiate with the supplier;* this is done the value Justifies it and there are areas where further clarification or if the offer can be improved upon.
8. *Place the purchase order.*
9. *Rate supplier performance*; this entails getting feedback from users on supplier performance. This is called vendor rating (performance after delivery or after use).

5.3 Factors considered in the evaluation or appraisal of suppliers

There will be a range of factors to be appraised which are directly related to the particular requirement, but the following should act as a checklist of aspects to be assessed for the majority of contracts; the significance of each and thus the time devoted to the assessment will again vary according to the particular requirement:

- **Finance**: including turnover, profit, assets, ROC, borrowings, debts, credit status takeover/merger possibilities, market positioning. The appraisal should employ the service of credit agencies such as Dunn and Bradstreet to provide supplier evaluation reports.
- **production capacity** including available productive capacity, scope for expansion, capacity utilization percentage with and without your organization's requirements
- **production facilities** related to the particular requirements including range, type, age and sophistication of plant and machinery, maintenance levels, housekeeping
- **human resources**, including staff numbers and employment, skills and qualifications, training policies, management/worker relationships, worker representation, industrial dispute record, attitudes and motivation, staff turnover
- **quality**, including the implementation of quality systems, for example ISO 9001:2000, ISO 14000, policies on TQM, inspection and testing procedures, statistical controls, quality control procedures for sub-contractors, guarantees
- **performance**, including information on past and current projects, features and innovations introduced, references
- **Corporate Social Responsibility (CSR)** issues, including determining the policies on environment, human rights, equality and diversity, sustainability, ethics and ethical trading, biodiversity, corporate governance and impact on society
- **Information technology** including the extent and the use made of current IT to support and report on business activities.

The **10Cs** model advances attributes of a good supplier to include;

- **Commitment:** A good supplier should be committed to the market (buyer) and this is important when choosing a supplier for a long-term contract.
- **Capability:** The potential supplier should be able to provide solution to the need i.e. providing consistent quality. This is especially important when using suppliers for the first time.
- **Cost:** A good supplier should give good prices which are competitive and sustainable. This is important when the buying organization sells in a market where the margins are tight.
- **Control:** The supplier should have good quality control and quality assurance procedures in place. This is necessary if there is a potential of failure costs due to quality being less than 100%.
- **Clean/cleanliness:** A good supplier should be aware of his environmental impact and should be in position to reduce any negative impacts on the environment. This is so important it the buying organization is a well-known brand in the public eye.
- **Competence:** A good supplier should employ skilled and competent staff and should be able to invest in staff training and development.
- **Capital/cash resources:** The supplier should be financially stable especially when significant investment is required on the supplier's side.
- **Capacity:** A good supplier should be able to handle the volumes required especially if the buying organization expects its customer demand to increase quickly.
- **Culture:** The business and ethical values of a supplier should be in line with those of the buying organization.
- **Consistency/continuity:** A good supplier should work or operate on recognized standards especially when customers of the buying organization wish all inputs to be traced. For example, ISO 9000 certification.

5.3.1 Corporate Social Responsibility (CSR) and Procurement

While Enron is an example of a major collapse in corporate governance, many CSR issues and risks actually emanate from the supply chain: child labour issues, sweatshop accusations and poor management practices. Therefore, in order to comply with CSR more generally, the external supply chain needs to be addressed in evaluating suppliers and conduct of procurement operations. That's where Socially Responsible Procurement (SRP) comes in.

The Institute for Supply Management defines socially responsible procurement as a framework of measurable corporate policies and procedures and resulting behavior designed to benefit the workplace and, by extension, the individual, the organization, and the community. Pursuing this objective requires focused efforts along the six dimensions of socially responsible procurement:

- Community involvement
- Diversity and inclusion
- Environmental protection
- Ethics and financial stewardship
- Human rights respect
- Health and safety

Procurement professionals must set priorities and make tradeoffs between these dimensions in order to properly allocate what are typically limited resources. The procurement workgroup must consider the relevance of that dimension to overall company strategy, and whether actions taken by the company can truly make a difference in the marketplace.

5.3.2 The Elements of SRP

The following elements of CSR are some of the most relevant to the various stakeholders involved in the supply chain, namely: employees, customers, suppliers, the community, the environment, staff, customers and shareholders. They therefore make up most of the elements of SRP:

Environmental Responsibility: As knowledge relating to environmental damage increases, the pressure to change the ways in which organisations behave has increased – particularly amongst the manufacturing, mining and resources sectors. Companies need to monitor the environmental impact of suppliers, and develop an environmental Procurement Policy that aims to reduce the environmental impact of their own and their suppliers' activities, goods and services (otherwise known as 'green buying').

Human Rights: Human rights in the supply chain includes a range of complex issues, such as: slavery, bonded labour, child labour, freedom of association, working conditions and wages, exploitation and non-discrimination.

Equal Opportunity: Equal Opportunity addresses acts of discrimination on the basis of race, sex, religion, sexual orientation, disability and age.

Diversity: As a concept 'supplier diversity' is often mistakenly taken to mean any initiative to broaden an organization's supply base, for example by increasing the number of suppliers with whom the organisation does business. However, supplier diversity actually refers to initiatives that aim to increase the number of diversely controlled (e.g. ethnic-minority owned or women-owned) businesses that supply goods and services to both public and private sector organisations. It's about creating a level playing field, by offering under-represented businesses the same opportunities to compete for the supply of quality goods and services, as other qualified suppliers. Positive discrimination even.

> *"By increasing the diversity of our workforce, sales organisations and supplier communities we improve our access to people with talent and become more aware of our customers' needs, which enables us to create valued products and services."*

Corporate Governance: Supply chain governance is an integral aspect of the overall corporate governance of an organisation. It requires strong and transparent reporting processes across supply networks and supplier accountability for supplier performance.

Sustainability: Sustainability is about living and working in ways that meet and integrate existing environmental, economic and social needs without compromising the well-being of future generations. Obviously, this is particularly significant for the supply chain, which can make a significant contribution to sustainable development, resource minimization and risk minimization. "Put back what you've taken out" is becoming a SRP philosophy. This is increasingly the case in the Ugandan resource sector, as an example.

Impact on Society: The approach an organisation takes to labour and supplier relations can determine whether or not they are seen as a 'good corporate citizen' or a 'good employer'.

Ethics & Ethical Trading: Businesses are increasingly doing business in a 'borderless' world, which makes it even more essential to develop core principles of conduct, which can then be applied to employees and suppliers worldwide – morally if not legally.

Biodiversity: Biodiversity relates to protecting diversity concerning habitat, genetics and species and, as such, has an obvious impact on SRP – particularly offshore suppliers in developing nations.

Community Involvement: Companies that engage and assist their communities become valuable members of those communities and more respected by their stakeholder.

5.4 Sources of information about potential suppliers

a. Trade directories
b. Databases
c. Company websites
d. Sales persons
e. Trade journals

f. Informal exchange of information between buyers
g. Organizations promoting trade for example UMA
h. Customers both external an internal
i. Press for example newspapers, TV/Radio
j. Trade shows of fairs or exhibitions
k. Archives i.e. documents that are kept over time
l. Catalogues

5.5 Sourcing Internationally

There are a number of factors that differentiate purchasing abroad from local sourcing. The relative importance of each will differ from market to market and between commodities. However, the presence of any or all of these factors adds complication and risk to the purchasing process.

5.5.1 Why source locally?

- Speak the same language
- Belong to a similar culture
- Do business in the same legal system
- Work to the same standards
- No currency exchange problems
- Shorter lines of communication
- Quicker delivery periods which are less subject to delays

5.5.2 Why procure from abroad?

a) ***Quality*** is more often than not involved in the decision to purchase from abroad – but quality in this context can mean several things i.e. the buyers of raw materials for process industries may find what is apparently same commodity available from several countries; but the quality can mean several things i.e. the buyers of raw materials for process industries may find what is apparently same commodity available from several countries, but the quality available from each can vary greatly e.g. the inherent purity of a raw material in question.

To other buyers the quality factor in procuring abroad can be associated with the reliability and consistency of manufactured goods produced under different conditions and methods in each source.

b) There may be ***strategic reasons*** for foreign procurements, for instance to improve supply security by having a second source in another country.

c) Sometimes ***domestic capacity may not be enough to meet demand***, so the gap has to be filled from abroad.

d) ***Price***: price is most frequently quoted as the major reason for purchasing abroad. The explanation for this is peculiar to each situation but can usually be explained by identifying one or more of the following: -

- Larger quantities
- Lower wages
- Better productivity
- Better plant
- Lower R/M cost perhaps associated with proximity to source
- Government subsidy
- Lower transportation
- Economics of large-scale production

However, price comparisons are misleading if taken at face value. A more appropriate criterion for decision making in procuring abroad is the total through cost in the procurement process.

e) The buyer many prefer to buy from a foreign source which offers *features **not available on domestically** produced goods of similar type*. Technological innovations occur all round the world.

f) ***Customer preference***: – the buyer must understand the advantages offered by different markets in relation to their demands. Customer preference may also be based upon perceived quality and value or on the reliability of foreign goods in comparison to those of local origin.

g) ***Brand:*** – preferences influence purchasing decision. In situations where a particular brand is desired by customers or specified by product designers, the buyer has few options other than purchase abroad if that is where the particular brand originates.

h) The buyer may be compelled to go abroad ***to get what is required***. Many raw materials are not produced at all in the UK; for instance, cocoa, coffee, cobalt.

i) ***Reciprocal dealings:*** – many countries use reciprocal trading practices to help balance their foreign currency transaction.

5.5.3 Factors to be considered when sourcing abroad

Making an overseas procurement decision in pursuit of benefits, there are several risks in the international supply market that should be evaluated. Such factors include;

1. ***Language:*** – this is perhaps the most obvious difference to be found/involved. It is unsafe to assume that all business can be successfully conducted in the native language of the purchaser. Even though both parties may be employing English or some other shared language in conducting their business; it is possible that one party is less familiar with the language and differing meanings may be attached towards or contract items. Consensus ad idem is vital to a valid contract.

2. ***Currency:*** – exchange rates are not static. They are dynamic indicators reflecting the ever-changing relationships between competing economies. They represent an area of significant risk and uncertainty as they keep on fluctuating most of the time. The buyer in these cases must quantify the risk and take appropriate action to safeguard his/her position.

3. ***Payment:*** – transfer of funds internationally poses its own difficulties as a third party; normally a bank will normally be involved to facilitate this process, a service that will cost money.

4. ***Politics:*** – politics may be ignored by an enterprise, but to ignore the political situation of an overseas country when thinking of buying from abroad is perilous e.g. Zimbabwe & Iraq.

5. ***Legal requirements:*** – legal systems differ greatly between the importers and exporters country and in the event of a dispute, it may be difficult to determine which law is applicable to settle the dispute for instance there are many parts of the world where trade is conducted under collective laws examples are found in EU and OPEC countries.

6. ***Cultural differences:*** - culture is not static it is dynamic business and sociological culture between trading partners differs greatly which the prospective procurement should be aware of.

   Though sometimes overlooked, culture plays an important part in determining the success or failure of procuring abroad.

7. ***Inco terms***: – when procuring overseas it is necessary to be aware of the obligations of both parties in respect of terms of delivery, transportation, insurance and shipment of the goods under their contract of sale and supply of

goods. Misunderstandings normally arise and appropriate steps are desirable to prevent problems of this kind from occurring.

8. ***Customs:*** – import and export procedures between countries which are members of the EAC have been considerably simplified. There is need for careful administration of these procedures for products from outside the EAC to avoid unnecessary expenses. It is necessary to reduce the length of time goods are in customs. Every day's delay can add to costs.

9. ***Ethical standards*** (ethics do's and don'ts): – these differ widely throughout the world. The prospective purchaser should be aware of the differences and act accordingly in his/her own company's best interest and within the laws which govern.

10. ***Economic performance:*** – this is another key factor that differentiates procuring abroad from local sourcing. It is hard to understand and forecast performance trends of the buyers own economy or its economic indicators; to attempt such an understanding of one or several overseas economies adds a significant dimension to the tasks of a procurement department.

This list is not exhaustive and others like *lead time* and *differing time zones* can be considered depending on how you argue them out. One way to overcome this is to hold stocks in the country of import.

Questions:
a) Describe the single, dual, and multiple sourcing policies.
b) Examine the importance of engaging the right supplier?

Chapter 6

Outsourcing

6.0 Learning objectives

At the end of this chapter candidates will be able to demonstrate an understanding of the outsourcing strategy by:

- *differentiating between in-sourcing and outsourcing*
- *explaining the benefits or reasons for the outsourcing strategy*
- *describing the outsourcing process, and*
- *analyzing the costs associated with the outsourcing strategy.*

6.1 Introduction

Outsourcing is the retention of responsibility for the delivery of services by an organization, but the devolution of the day-to-day performance of those services to an external organization, under a contract with agreed standards.

In-sourcing is the process of changing from an outsourced service to delivery of the service using the internal resources of the purchasing organization. An example could be the decision to run and manage the vehicle fleet using internal resources at the end of an outsourcing contract.

6.2 Benefits of the proposition to outsource

1. The supplier can *save the procuring organisation money, over and above the best the organisation can do*. Organizations have outsourced because suppliers have offered cost savings and the area of improving cost within the existing business model has been forgotten. Improving the current situation should be the first task, followed by a challenge to the supplier to improve on that.
   Cost benefits accruing from suppliers here should include:

   a) Economies of scale from their greater purchasing power and preferred supplier arrangements in the area.
   b) More efficient and productive use of people and other resources from their greater experience and greater volume.
2. The *area is not the procuring organization's core business*. Determining the core business and focusing on that, whilst using the specialism of other organizations to perform non-core activities is key to business success. An organization may

therefore say, 'We run trains and not computers. Let's outsource the IT function to a specialist.' Once the non-core activities are outsourced, management time will be free to focus on core activities.

3. *Improving return on net assets* (RONA). RONA is a measure of how a business utilizes its assets to make money by comparing sales with assets. If the assets are sold to an outsourcing supplier the organization:
    a) has less assets but the same sales turnover – as a percentage the turnover will therefore be higher.
    b) has to make less provision to replace the assets through depreciation
    c) will have a single inflow of cash.
4. The high pace of technical change may mean that the procuring organization will prefer to use a specialist supplier to manage this as a service for them. It will mean that the specialists within the supplier will be able to better develop the resources to meet the changing needs of the business and in doing so, reduce the buyer's exposure.
5. The need for a *better service*. Here the supplier may be more experienced at providing this service than the existing resources, may have the necessary accreditations and may be able to use their greater volume and diversity to cope better with peaks and troughs. The supplier may simply have the expertise when internally we are amateurs.
6. The supplier may be able to provide a 'one stop shop' consistently across all of the sites of the organization.
7. It may not be possible for our organization to obtain the skills necessary to run that area of our business effectively.

6.3 The Outsourcing Process

Many organizations have rushed into outsourcing and many of them have regretted it. Sometimes those who advocate processes which take time and cost money before making a decision are ridiculed as being over-cautious or trying to avoid taking a given route. In the case of outsourcing, the time invested in the early stages of the process will pay dividends during the life of the outsourcing contract.

A process for outsourcing must include the following steps:

1. Strategic analysis
2. Selection of target areas
3. Specification of the requirement
4. Supplier selection
5. Implementation and review

6. Ongoing relationship management.

1. Strategic analysis

This first step is the process identification of core activities and consequently non-core activities. This gets to the heart of the organization and must involve key stakeholders and the board or management team, and even the owners of the organization.

2. Selection of target areas

Once the core areas are identified and ring-fenced, areas of the business which form a target for outsourcing must be identified. Again, this must involve key stakeholders and the board or management team, and participants in this discussion need to understand the long-term nature of outsourcing and the consequences of decisions made. For each target area this process will involve:

- A supply positioning analysis, with particular emphasis on the risk
- An assessment of the extent to which problems in the target area can be corrected before outsourcing.
- Understanding whether a better return on investment can be obtained from retaining the area in-house or from outsourcers
- A clear understanding of the objectives of the outsourcing project, how they will be measured and who will be responsible for measuring them.
- A clear plan of the project including stakeholder involvement and sign-off.
- A clear statement of how and where this area interfaces with core processes.
- Considering other options like internal service level agreements, management buy-out or a joint venture.
- Considering the financial, tax and legal implications of all options against the status quo.
- Communication to members of the organization impacted by the process.

3. Specification of the requirement

The specification of the requirement must be based upon a full understanding of the current situation. Organizations have made mistakes by writing specifications which they *believe* reflect what happens in the area to be outsourced but not what actually does happen. This has led to them either paying for services not required or being invoiced for extras or contract variations by suppliers who have been asked to undertake tasks not in the original specification. The specification must:

- Be clear and unambiguous
- Include measurable performance criteria of the level of key performance indicators
- Recognize any remaining problems and highlight them

- Describe the relationship sought with the supplier
- Reflect issues like confidentiality and security
- Identifying licensing issues and contract assignments necessary as part of the outsourcing contract where appropriate.
- Consider the terms and conditions of contract.

The specification must recognize that a supplier rather than a department will be performing the service and processes for change and development must be included. Finally, there is the question conflict of interest for the person drawing the specification. Where for example a vehicle fleet manager is to be transferred to the supplier with the team delivering the service, and the same person is asked to draw up the service specification, it would be possible to imagine circumstances when the specification may not be as demanding upon the supplier as it could reasonably be expected to be. Independent advice is needed here.

4. **Supplier selection**

Supplier selection must be rigorous and include a supplier appraisal, a tender process or alternatively a negotiation based upon the specification, due diligence concerning the supplier, and result in a business case which demonstrates clear benefit to the purchasing organization before the outsourcing project goes ahead. Factors which need to be considered are:

- A supplier preferencing and market management matrix analysis
- Whether the market will be interested in our requirement? (Normally the answer here is 'yes', but this cannot be taken for granted)
- Sharing any outstanding problem areas with potential suppliers
- Assessing the cultural fit between the two organizations
- Sharing sufficient information with the supplier to enable them to make their best offer to us – this may include the current costs of the area concerned and the variability of the requirement.
- A site survey by the supplier and discussion with users and current deliverers of the service.
- Supplier relationships with their suppliers
- Selection criteria not based simply on price –here the private sector could learn from the public sector's use of MEAT (Most Economically Advantageous Tender).
- Discussion with the supplier over their normal performance measure.
- Appropriate terms and conditions, including the means of termination.

Remember that the outsourcing relationship will be a long-term one. In this context the searching and detailed examination is vital.

5. Implementation and review

Implementation of the contract may take a number of months and both parties must approach the process as one moving from the competitive process of selection to a cooperative process of working together. Communication internally is vital.

Particularly to people impacted by the change, and joint working parties need to be established with the supplier to discuss:

- Contract management processes, including meetings, reporting and escalation processes.
- Handover planning
- Changes in working practices
- Changes to procedures
- Status of projects that will be live across the boundary of the outsourcing cut over.
- Linkages with other areas of the business and other suppliers.
- Processes for new employees of the supplier and also our employees who become employees of the supplier.

It is vital that communication channels remain open between the people managing the contract for the procuring organization and the supplier and employees on both sides who will be delivering the contact. At the end of the implementation phase it is appropriate for both parties to review the process they have been through and identify learning points for the future.

6. Ongoing relationship management

It is important to recognize we are now managing a supplier rather than a department. Typical non-core activities outsourced by organizations are: catering, security, IT, site maintenance, internal post and mail services, travel, stationery, vehicles and freight. Other organizations have outsourced legal, HR, finance and purchasing.

6.4 Costs/Risks of outsourcing

- *Cost;* -literally the outsourced operation could cost more than that previous operation or more than its budget or target.
- *Failure to supply;* – the service fundamental to the contract is not delivered.
- *Transition or mobilization costs;* – costs here can include changes to buildings or facilities to accommodate the new arrangements. Similar costs will be incurred if the function is insourced or there is a change of supplier.
- *Changes to processes*; – these may be part of transition costs, but it has been known for suppliers to insist on changes to processes during the life of contract.

- *Loss of control;* – this must include control of the day-to-day operations, but it may include a loss of the control of the future direction of that function. However, this may not matter and the direction and foresight of the supplier in his area may in fact be one reason why we selected them.
- *Contract management costs;* – the cost of people managing the contract. In many organizations this may simply be part and parcel of the work of one of the people in the purchasing team.
- *Loss of skills*; – the procuring organization may lose the skills to perform the functions outsourced. However, this again may part of the plan.
- A *lessened capacity to innovate*; – here the innovation may pass to the supplier's and the purchasing organization become too dependent on them. If this is the case the question has to be asked, 'should this area have been outsourced?'
- *Hidden costs;* – costs that will not be apparent at the start of the contract and may even not be apparent during the contract unless there is an extensive audit. These costs can include the following long list:
  - Ambiguous requirements, which cost money to clarify or put right.
  - Buyer's staff duplicating supplier duties
  - Buyer's staff by passing the agreed processes
  - Buyer's staff undertaking supplier duties 'to help out'
  - Changes to business operations necessary to suit supplier ways of working
  - Differentiation of requirements previously standard to become specials
  - Loose definition of the contract requirement
  - Failure to identify full extent of existing service
  - Settling on fixed costs in a descending cost area
  - Locking into ageing technology with supplier.
  - Over-specified requirements.
  - Payment in advance when this is not absolutely necessary.
  - Production of unused output, again probably because of an inaccurate specification.
  - Paying again for items already bought, for example software licenses.

It is worth noting how many of the hidden costs arise from a poor specification of the requirement.

Chapter 7

Procurement Audit

7.0 Learning objectives

At the end of this session candidates will be able to demonstrate an understanding of Audit in procurement activities by:

- *describing key audit concepts and procedures*
- *explaining the internal controls in the procurement process*
- *describing the main audit issues and practices in procurement*
- *explaining the principles and guidelines to audit of procurement*
- *appreciating the role of audit in procurement, and*
- *appreciating the role of different types of audit in procurement.*

7.1 Introduction to Audit

Auditing

Auditing is broadly defined as a systematic process of objectively obtaining and evaluating evidence in respect of certain assertions about economic actions and events, to ascertain the degree of correspondence between those assertions and established criteria and reporting the results to interested parties.

Auditing usually covers a particular period of time. Auditing may be narrowly defined as a written report on the examination of financial statements for a particular period of time.

Independent auditing

The International Federation of Accountants (IFAC), recognizing the responsibilities of the accountancy profession and considering its own role to be that of providing guidance, encouraging continuity of efforts and promoting harmonization, has deemed it necessary to establish an international "Code of Ethics for Professional Accountants" to be the basis on which the ethical requirements (code of ethics, detailed rules, guidelines, standards of conduct, etc.) for professional accountants in each country should be based.

The Auditors' Code describes 'independent audit' as providing reasonable assurance that published audited financial reports are free from material misstatement and are in accordance with legislation and relevant accounting standards.

7.2 Internal Controls

Good internal controls are fundamental to achieving key initiatives and goals of organisations. Utilizing good controls can help eliminate bottlenecks, redundancies, and unnecessary steps. Controls can prevent loss of resources, including capital assets, inventory, proprietary information, and cash. They can help ensure compliance with applicable laws and regulations. Periodic audits against the control guidelines can ensure that a process in control stays in control.

These internal controls are designed to provide reasonable, but not absolute, assurance regarding the safeguarding of resources, reliability of operating and financial information, and compliance with laws and regulations. The concept of reasonable assurance recognizes that the cost of a control should not exceed the benefit to be derived. It also recognizes the need for uncompromising integrity, good business judgment, and a culture of good control practices.

In management's selection of procedures and techniques of control, the degree of control employed is a matter of reasonable judgment. When it may be impractical or impossible to institute any of the controls listed, as could be the case of a small or remote operation/department, management should choose among the following alternatives:

- Improve existing controls through increased supervision and audits;
- Institute alternative or compensating controls; and/or
- Accept the risks inherent with the control weakness.

The internal control process should be supported by a commitment from all levels of the organisation. The process itself should include operational analysis, development of control procedures and techniques, communication, and monitoring. Operational analysis requires evaluation of risks and a determination of the appropriate control objectives. Also, the operating environment (such as level of automation, budget and resources) should be taken into consideration as well as a cost-benefit analysis to ensure the cost of a control does not exceed its benefit.

Based on the operational analysis, specific control techniques or procedures can be selected. These may include approvals, authorizations, reconciliations, duty segregation, reviews and/or documentation.

Throughout the process, communication should flow freely in the form of training, awareness and feedback. Once in place, the control activities should be monitored and evaluated. This can be accomplished through some combination of self-audits, internal audits, and external audits. The feedback provided can be used to further improve the internal control system.

Frequently, any business cycle encompasses a specific transaction from its initiation through to completion. For example, the procurement disbursement cycle of an organisation might encompass requesting a product, creating and approving a purchase order, receiving product and invoice from the vendor and issuing payment to the vendor.

The control guidelines within each cycle should be written in a manner to satisfy the basic objectives of organisational systems of internal control and to meet external requirements, including Generally Accepted Accounting Principles (GAAP) and applicable laws and regulations. Fundamental control criteria, however, are:

a) That transactions are conducted in accordance with management's general or specific AUTHORIZATIONS;
b) That transactions are properly ACCOUNTED for and accurately and promptly RECORDED; and
c) That the assets and records of the university are adequately SAFEGUARDED.

The control matrix shown (next page) provides a general guideline for the processing of all transactions consistent with the control criteria noted above.

7.2.1 Internal Controls for Procurement

Internal controls are the mechanisms by which procurement processes support the strategic goals of accountability, transparency, traceability, and data integrity.

Having appropriately designed controls in place for procurement not only protects against the misuse of taxpayer or organisational money, but also enhances employee awareness and attitudes toward control ling the cost of essential purchases. The larger the organization and the more decentralized the procurement function is, the greater the importance of control procedures over purchasing.

Each organisation must design a system of procurement controls that are appropriate for the size, locations, and structure of its operations. Internal controls over procurement should be designed to ensure that unauthorized purchases are prevented; cost considerations are evaluated; nonessential purchases do not occur; and statutory requirements are followed to ensure fair and open competition, and cost- effectiveness in the procurement process.

This section discusses internal controls designed to ensure the efficiency and cost-effectiveness of the procurement process.

Procurement Procedures

<u>Approving authority</u>: Clear lines of authority for approving procurements (before they occur) should be established. Depending on the size of the organisation, approvals may consist of verbal approvals or, in larger organisations, requisitions or purchase orders (either electronic or manual) may be used to formally document the request and approval process.

Reason for Control

Purchase approvals, whether oral or written, help ensure that each procurement is necessary for the organisation's operations and that cost considerations have been evaluated. Written approvals are superior, but cost considerations may necessitate oral approvals in smaller units of organisations.

Verification of Budget Appropriations: Prior to authorizing a major purchase and periodically for routine purchases, the availability of budget appropriations should be verified. In an electronic system, application controls should be built into the software to prevent the approval of a requisition or the issuance of a purchase order if sufficient appropriations are not available. In other systems, the budget officer should be consulted to determine the availability of appropriations.

Reason for Control

Checking the availability of appropriations will ensure that authorized procurements do not exceed budget authorizations.

Separation of requisitioning and receiving from approving authority: Where practical, the approval to purchase goods or services should be authorized by personnel other than the employee requesting the purchase; the approval to purchase should also be segregated from the receiving of goods and services.

Reason for Control

By segregating the approval to purchase from the request to purchase and the receiving of assets or services purchased, the opportunity to make personal purchases from public or organisational funds (and for these transactions to remain undetected) is reduced.

Properly Designed Forms and Record-Keeping Procedures

Design of procurement forms or documents: All procurement forms (such as requisitions and purchase orders) should be designed to include specific details about the items or services to be procured including quantity, costs, model numbers, terms of sale, availability of appropriations, and approvals to procure.

Reason for Control

Properly designed forms allow comparisons to be made between items requested and items purchased in terms of descriptions, quantities, and prices. Forms are also used to record the approval to purchase and thereby limit unauthorized procurements from occurring. Properly designed forms provide an audit trail on the procurement process from start to finish.

Numbering or serializing documents/forms: All purchasing forms should be sequentially numbered.

Reason for Control

Sequential numbering allows for the tracking of issued requisitions and purchase orders and for the cancellation of unused purchase orders.

Multiple copies of procurement documents: Procurement forms should have multiple copies so that other departments such as receiving and accounts payable can be notified of the authorization to procure goods and services.

Reason for Control

Multiple copies facilitate communication (especially in large organisations) about the ordering and expected arrival dates of items or services procured.

Separating approving authority from creation of vendor lists: Access to the module for creating new vendor selections and lists should be segregated from employees who authorize purchases or approve claims for payment.

Reason for Control

In a computerized purchasing environment, segregating the duties of creating new vendor accounts from the duties of authorizing procurements and approving claims for payment lessens the opportunity for establishing fictitious vendors and making payments to them.

Capturing new vendor data: Complete addresses, Social Security numbers, tax ID numbers, etc. should be obtained for all vendors and entered into the vendor master file.

Reason for Control

For the purposes of discouraging the creation of fictitious vendors, Social Security or tax ID

Numbers and other data should be required before new vendors are added to the master file.

Encumbrance accounting: Once goods or services have been approved for purchase, appropriations can be reserved for the estimated amount of the approved purchase or service by establishing an encumbrance. Encumbrance accounting is most efficient when the requisition or purchase order process is computerized and an encumbrance is established automatically when a purchase order is issued. For smaller local governments without sophisticated computerized purchasing systems, encumbrances for high cost purchases and services should be recorded via journal entry.

Reason for Control

Encumbrance accounting provides budgetary control over purchases and services. When an encumbrance system is in place, it will help prevent budgetary line items from becoming over expended.

Review of outstanding encumbrances: Before the close of the fiscal year, the finance department should review all outstanding encumbrances and determine if amounts designated should be continued, adjusted, or cancelled.

Reason for Control

Sometimes goods or services are ordered and never received, but the original encumbrance isn't liquidated. In other instances, encumbrances are established "in bulk" at the beginning of the year but are not completely utilized. To ensure proper financial reporting, outdated and nonspecific encumbrances should be liquidated before the end of the fiscal year.

Receiving Procedures

Verification of slips against goods received: When goods or services are delivered, receiving or packaging slips should be verified against the quantity, type, and condition of the goods received.

Amounts received should also be compared to amounts ordered, as described on the purchase requisition or purchase order. Verified receiving slips should be forwarded to the person responsible for preparing the claim voucher.

Reason for Control

Verification of the accuracy of receiving slips to both the actual goods received and to the requisition or purchase order will usually detect shipping errors and ensure that payment will only be made for quantities ordered and received in satisfactory condition.

Segregation receipt and verification from the requisitioning or authorizing responsibility: The responsibility for the receipt and verification of items ordered should be segregated from the employee who requested or authorized the purchase.

Reason for Control

An employee with both of these responsibilities could order items that are not necessary and keep them for personal use without being detected.

Payment Procedures

Assembling a voucher or claim package: Each department that ordered goods or services should assemble a voucher or claim package containing: the verified receiving slip, the approved purchase order (if applicable), the original invoice and the certification or signed approval of the department head stating that the goods or services were received and they are a true and just charge. All voucher packages should be forwarded to the

claims auditing body or official, or other appropriate officer as provided by law or policy.

Reason for Control

The voucher package is the basis for the audit of claims. A properly prepared voucher package will help ensure that payments will only be authorized for goods and services actually received, that are of acceptable quality, and that further a lawful purpose of the local government. A complete voucher package also lessens the risk that unauthorized purchases and services will be paid for without detection. Payments to legitimate vendors may be delayed if a complete voucher package is not presented for the claims auditing body or official.

Delivery before claim: Even if not required by statute, goods should be received and/or services rendered before a voucher or claim is submitted.

Reason for Control

A requirement that goods and services are received before payment serves to ensure that purchases are legal and necessary for the organization's operations and were received or performed in a satisfactory manner. It also helps avoid to the potential for making a constitutional gift to a vendor who has already been paid, but ends up not providing the agreed upon goods or services.

Checks directly sent to vendors: Vendor checks should not be returned to the department or the official who requested or made the purchase. Checks should be sent directly to vendors.

Reason for Control

Direct mailing of vendor checks prevents an employee from intercepting a check written to a phony vendor or for delaying payments to vendors to solicit gifts or other gratuities.

Statutory Controls

Competitive bidding requirements: With certain exceptions, procurement of goods must be done in accordance with competitive bidding requirements as provided for under the policy or law.

Reason for Control

One of the goals of competitive bidding requirements is to foster honest competition so that quality commodities and services are obtained at the lowest possible price. Competitive bidding also guards against favoritism, extravagance and fraud, while allowing interested vendors a fair and equal opportunity to compete.

Exceptions to competitive bidding: The law generally requires that the procurement policy provide that alternative proposals or quotations be obtained by use of written

requests for proposals (RFPs), written or verbal quotations, or other methods, for procurements that are not subject to bidding requirements.

Reason for Control

Procurement policies and procedures generally ensure that competition is sought in a reasonable and cost-effective manner for procurements below the bidding thresholds and for other contracts exempt from bidding.

Analytical Review Procedures

Periodic review of Vendor lists: Management or their designee should periodically review a listing of vendors and cumulative amounts purchased from individual vendors.

Reason for Control

Reviewing vendor listings provides management with a "big picture" of the scope and nature of all purchases made. The review may identify opportunities for cost savings and can be used to identify aggregate purchases that may be subject to competitive bidding. Unusual or unknown vendors may also be detected during this type of review.

7.3 Fundamental principles of independent auditing

The Auditors' Code, published by APB, prescribes nine fundamental principles of independent auditing, as follows:

a) ***Accountability***: Auditors act in the interests of primary stakeholders, whilst having regard to the wider public interest. The identity of primary stakeholders is determined by reference to the statute or agreement requiring an audit: in the case of companies, the primary stakeholders are the general body of investors.

b) ***Integrity***: Auditors should act with integrity, discharging their responsibilities with honesty, fairness and truthfulness. Integrity helps to insulate auditors from matters of conflict of interests and elevate their objectivity. Confidential information obtained in the course of the audit is disclosed only when required in the public interest, or by operation of law.

c) ***Objectivity and independence***: Auditors should be seen to be objective in all their dealings with their clients. They express opinions independent of the entity and its directors.

d) ***Competence:*** This is the ability to carry out professional duty with great knowledge and skills. Auditors should exhibit competence, derived from the acquired qualifications, training and practical experience. Auditing demands understanding of financial reporting and business issues, together with expertise in accumulating and assessing the evidence necessary to form an opinion.

e) ***Rigor:*** Auditors approach their work with thoroughness and attitude of professional skepticism. This was emphasized in the famous pronouncement of Lord Denning, which states that "*an auditor is not a blood hound, but should approach his job with* *professional skepticism believing that someone, somewhere, has made a mistake and that a check needs to be carried out to ensure that no such mistake was made and this forms the whole essence of auditing."* Auditors assess critically the information and explanations obtained in the course of their work and such additional evidence as they consider necessary for the purpose of their audits.

f) ***Judgement:*** Auditors apply professional judgement, taking account of materiality in the context of the matters on which they are reporting.
g) ***Clear communication:*** Auditors' reports contain clear expressions of opinion which are set out in writing for proper understanding.
h) ***Association:*** Auditors allow their reports to be included in documents containing other information only if they consider that the additional information is not in conflict with the matters covered by their reports and that they have no cause to believe it to be misleading.
i) ***Providing value:*** Auditors add to the reliability and quality of financial reporting. They provide to directors and officers constructive observations arising from the audit process, thereby contributing to the effective operation of the business entity.

7.4 Audit Evidence

"Audit evidence" means the information obtained by the auditor in arriving at the conclusions on which the audit opinion is based. Audit evidence encompasses the quantity and quality (or reliability) of evidence to be obtained by auditors. It is important for auditors to obtain sufficient, appropriate and reliable audit evidence to enable them draw reasonable conclusions on which to base their audit opinion. Audit evidence may be obtained from:

a) An appropriate mix of tests of control and substantive procedures; and
b) Substantive procedures and enquiries made to ascertain the adequacy of the accounting system as a basis for the preparation of the financial statements.

An auditor should understand the following matters in relation to audit evidence:

1. The nature of audit evidence;
2. The sufficiency of audit evidence;
3. The appropriateness of audit evidence;
4. The evaluation of audit evidence; and
5. Reliability of audit evidence.

Chapter 8

Procurement Negotiations

8.0 Learning objectives

At the end of this session candidates will be able to demonstrate an understanding of negotiation activities in procurement by:

- *describing the negotiation concept*
- *examining the objectives and importance of negotiations to procurement management*
- *identifying circumstances that lead to negotiations*
- *explaining approaches, rules and styles of negotiation,*
- *describing the process of negotiation, and*
- *evaluating the qualities of a negotiator.*

8.1 Introduction

Negotiation has been described as the finest opportunity for the buyer to improve his or her company's profits and obtain recognition. Negotiation is defined as;

a) *'the process whereby two or more parties decide on what each will give and take in an exchange between them due to a disequilibrium in the terms of trade.'*
b) *'the process by which we search for terms to obtain what we want from somebody who wants something from us.'*
c) *'a compromise to settle an argument or issue to benefit two or more parties as much as possible.'*

Negotiation is not only used for business purposes but also in our daily lives as well. Communication is always the link that will be used to negotiate the issue or argument whether it is face to face, on the telephone or in writing.

Negotiation is not only between two people but can involve several members from two parties.

8.2 Importance of negotiations in procurement

Negotiation in a business context can be used for selling, purchasing/procurement; staff (contracts for workers), borrowing (e.g. loans) and transactions along which anything else that you fill are applicable for your business. Negotiation is not only used for business purposes but also in our daily lives as well, communication being the link that is used to negotiate the issue or argument.

It might be face to face, on the telephone or in writing. Negotiation is not only between two people but can involve several members from two parties. Specifically, to procurement, negotiations serve the following importance;

1. Helping to obtain the best value for money in respect of services or works and goods.
2. Outstanding and long-term relationships are established through negotiation especially where a partnership approach to negotiation is adopted e.g. in JIT approach.
3. Critical supplies, outsourcing etc.
4. Negotiation helps obtain fair and competitive prices.
5. Negotiation helps achieve customer satisfaction through negotiating quality that shall meet better customer services levels.
6. Conflict resolution if there is nonperformance by the provider i.e. negotiation for new terms or amendments in a contract can reduce conflicts and stress in relations that would crop up.
7. Negotiation aids proper contract management. This is achieved during a negotiation when the role of the employer, the contractors and sub-contractors are defined and agreed upon.
8. Helps obtain on-time performance of the contracts.
9. General terms and conditions of supply are agreed upon and determined through negotiation.

8.3 Approaches to Negotiation

a) ***Adversarial negotiation*** also referred to as *distributive* or *win-lose* negotiation, is an approach in which the focus is on positions staked out by the participants in which the assumption is that in the event time, one party wins the other party loses. As a result, the other party is regarded as an *adversary.*

b) ***Partnership negotiation*** - also referred to as *integrative* or *win-win* negotiation is an approach in which the focus is on the merits of the issues identified by the participants in which the assumption is that through collective problem solving one or both parties can gain without the other having to lose.

Since the other party is regarded as a partner rather than an adversary, the participants may be more willing to share concerns, ideas and expectations.

8.3.1 The Characteristics of Adversarial and Partnership Negotiations

Adversarial or win-lose negotiation	Partnership or win-win negotiation
1. The emphasis is on computing goals to be attained at the adversary's expense.	- The emphasis is on ascertaining the goals held in common with the other party.
2. Strategy is based on secrecy, retention of information and low trust in the perceived adversary.	- Strategy is based on openness, sharing of information and high trust in the perceived partner.
3. The approach is basically hostile and aggressive.	- The approach is basically friendly and non- aggressive.
4. The key attitude is that if we win, you lose.	- The key attitude is how the respective goals of each party can be achieved so that both win.
5. Parties use threats and ultimatum with the aim of keeping the adversary on the defensive.	- The parties refrain from threats which are seen as counterproductive to the rationale.

8.3.2 Negotiation styles

Negotiation according to Kennedy et al (1980) in their book '*Managing Negotiations*' is the process by which search for terms to obtain what we want from someone who wants something from us. In any negotiation, the advance that knowledge about the styles of negotiation is very important as it's linked to the power relationship in any negotiation and this assists in clarifying the positions of parties and the overall approach that should be taken. Whether the approach is adversarial or collaborative, determining an appropriate style for each negotiation is important. Kilman and Thomas identified ***five*** styles of negotiation as follows: -

Competition: In this style the concern for others is low. Its characterized by the desire to win at all costs often described as a *win-lose* approach. In this approach one party seeks to have all their requirements recognized without giving any reciprocal recognition to the valid needs of the other party.

Accommodation: This is characterized by the desire to please others at the expense of your own interest. This approach is usually called *lose-win* or soft negotiation.

Accommodation is very appropriate when the issues are important to the other party and there is an opportunity to build credits to later use on more important issues.

Avoidance: This is where the real issues at the heart of the negotiation are ignored. Avoidance is an appropriate style when; The issues are trivial and more important issues are pressing, there is no chance of getting what you want if you use other styles like accommodation, when there is need for both parties to have time to cool down and regain perspective, when you need more time together information, someone else can handle the issue more effectively than you do, and when the issue is a symptom of another big issue.

Potential negative effects of using an avoidance style are; decisions may be made by default, unresolved issues are never addressed and may surface later in the relationship, creative solutions and important opportunities are prevented, and exclusive use leads to damage of personal credibility and may be difficult to recover when a different style is required.

Compromise: this is a negotiation style where the parties meet at a mid-point. Both parties achieve a moderate but incomplete satisfaction with their agreement in a type of *sub-optimal win-win*. Compromise is an appropriate style when; goals can be accommodated, when there is time pressure, when issues are not worth the effort of being accommodated in full, a temporary settlement to a complex issue is needed, and when backing is needed because collaboration/competition is not working.

Potential negative consequences; none is fully satisfied with the agreement and this leads to a short agreement which requires a lot of selling and policing, perception of a sale-out on important issues, and principles and long-term objectives may be lost by focusing exclusively on the practicalities.

Collaboration: This style is characterized by the desire to satisfy all interests of either parties in a *win-win* situation. It is appropriate when; joint goals can be agreed, finding a long lasting or creative solution is required, when both sets of interests are too important to be compromised, reaching a consensus/ common agreement is required, developing and maintaining a relationship with the supplier is wanted, and when there is need to learn to set assumptions or better understand the views of others.

The potential negative consequences are; it's very time consuming to reach agreement, too much time can be spent on insignificant issued, unfounded assumptions about trust can lead to advantage of another party taking your position, and ineffective decisions result because too many people input into the process.

8.4 The Negotiator

For one to carryout successful negotiations, negotiators need to demonstrate the following qualities;

1. He should be wise i.e. should have learnt from the experience of others and be able to utilize the experience he has gained during his time as a practicing negotiator.
2. A good negotiator should be fully equipped with all the technicalities of a negotiation. For instance, before going into a particular negotiation he should establish his BATNA-*Best Alternative to a Negotiated Agreement* should have a *bottom line* and should establish a *Zone of Possible Acceptance* (ZOPA) etc.
3. Should have knowledge of the materials, services/works for the procurement under question.
4. Should be patient and persistent.
5. Having clear thinking and broad ideas; In other words, he should be in position to make decisions that are suitable for reaching at an optimum decision at a particular negotiating point.
6. Should have persuasive quality and should be logical.
7. A good negotiator should believe in optimism and never let an opportunity to slip out of his/her hands.
8. He should be in position to go along with people with ease and enthusiasm.

8.5 The negotiation process

- **Preparation/Planning for Negotiation (Pre-negotiation Phase)**

'Cases are won in chambers" is the guiding principle in preparation for negotiation i.e. legal victories are often the outcome of the preceding research and planning or strategy on the part of counsel. Buyers can learn much by studying the strategies and tactics of legal, diplomatic and industrial relations and applying them to the procurement field. The matters to be determined at the preparation stage are as follows: -

a) **Who is to negotiate?**

i. Teams vs individual

- *Individual approach* - when negotiation is to be between two individuals, both should have sufficient status to settle unconditionally, without any reference back to higher authority.

- *Team approach* - for important negotiation especially where complex, technical, legal, financial, etc. issues are involved or for procurement of capital items, a team approach should be used. This is because an individual buyer is rarely qualified to act as a sole negotiator.

ii. Expendable Person (match like with like among the parties)

iii. Authority and power to commit organization

iv. What makes them good negotiators

v. Patience in discussing issues of the negotiation

b) **The venue**

The buyer should normally expect the vendor to come to him unless there are good reasons to the contrary e.g. the buyer is seeking concessions or it is desirable to respect the vendor's facilities. There are advantages in negotiating on a home around. Not only are surroundings familiar but access to rules and expert advice is facilitated. The buyer is also under no obligation in respect of hospitality provided by the vendor.

c) **Gathering intelligence**

This normally involves;

i. Ascertaining the strengths and weaknesses of the respective negotiating positions.
ii. Assembling relevant data relating to costs, production, sales etc.
iii. Preparing data which it is intended to present at the negotiation in the form of graphs, charts, tables, etc.

d) Determining objectives

Buyers should be clear as to what the negotiations are expected to achieve e.g. if the matter under question is price, the vendor should come with a minimum price which he/she should not go below. Similarly, the buyer should set a maximum price above which he/she should not go. In other words, parties should establish their *bottom-line*, their Zone of Possible Acceptance (ZOPA) and Best Alternative to a Negotiated Agreement (BATNA).

e) Tactics and strategy

That is developing positions or attitudes to be taken or adopted the negotiation designed to achieve set goals.

f) The "dummy run"

It is advisable to subject all argument, tactics and overall strategies to a critical scrutiny.

Summarily, preparing for negotiations requires;

a) *Creating alternatives:*
   - *Consider alternatives on different issues e.g. price*
   - *Overlaps, the more overlaps the better*
   - *Consider their position and yours*
   - *Establish minimum acceptable position*
b) *Identify the contents of the deal*
   - *Identify tangible & intangible motives*
   - *Comparison of parties' strengths*
   - *Objectives of the negotiation*

- **The Introductory Phase of Negotiation**

Successful negotiators in the introductory phase tend to expend considerable effort in;

1. Establishing an atmosphere that is conducive to the agreement. They may include social interchange, giving an impression of wishing to work to a mutually advantageous goal.
2. Validating assumptions (acceptable assumptions).
3. Testing the other party's position, willingness to collaborate or propensity to oppose.
4. Clarifying issues and the weight given to them by the other party.
5. Trying to ascertain whether any new information will be introduced by the other party.

In the introductory phase of negotiation, the following prescriptive points should be given due consideration: -

i. Be on time; - being late necessitates an apology and signals a lack of organization.
ii. Make brief opening statements should be used and be seen to be listening to the other party.
iii. Do not make quick decisions.

- **Actual Negotiation Phase**

At the actual time of negotiation, you must put the following aspects into consideration: -

f) **Stages**: - even with a philosophy of partnership negotiation, the activities of the participants will change at each stage of the negotiation process. These activities alternate between competition and operation. It is therefore useful for a negotiator to recognize this pattern of interaction and also recognize the stage that has been reached in a particular negotiation.

g) Techniques

i. In framing an *agenda*, the more difficult issues should appear later. Thus enabling some agreement on less controversial matters to be reached early in the negotiation.
ii. *Questions* are a means both of eliciting information and keeping pressure on an opponent, Questions may also be used to control the pattern and progress of the negotiation.
iii. Negotiation is between people - it is therefore essential to be able to *weigh up the personalities of one's opponent* and the drives that motivate them e.g. achievement, fear etc.
iv. *Concessions*; Buyers should avoid a "pattern of concessions" (concessions are a means of securing movement when negotiations are dead locked) the outcome tends to be more favorable when the concessions made are small rather than large. An experienced negotiator will often *"throw a sprat to catch a mackerel*".

h) Negotiating behavior

All negotiations involve interpersonal skills. The negotiating styles applicable vary according to the specific situation, training in negotiation should therefore include training in behavior analysis which should lead to an understanding of the responses likely to be involved by particular behavior e.g. shouting usually causes the other person to shout back.

i) Body language

It is important to note that over the centuries, man has become more articulate; he has developed an ability to hide how he really feels in situations. As a skilled negotiator therefore, you must watch the body language. No matter what people say, how they feel, can often be picked up from their body positions and gestures during the negotiations. The following are some of the postures and what they may indicate;

Posture	Possible meaning
- Leaning forward when making a point.	- Interested was to emphasize a point.
- Avoid eye contact.	- May be embarrassed, not telling the truth.
- Arms folded; body turned away from you.	- Defensive, no compromise not interested.
- Looking away, at watch or at window.	- Wants to leave or avoid any further discussion.
- Hands supporting head and leaning back in chair.	- Confidence.
- Stroking nose regularly with a finger avoiding eye contact	- May be lying

- Good eye contact, fingers stroking face.	- Interested in what you are saying.

Summarily during actual negotiations, know when to:

- *Hold concessions*
- *Know when to give in*
- *Avoid arguments/deadlocks*
- *Present facts……keep rational*
- *Suggest an agenda to guide meeting*
- *Establish Rapport between the parties*

- **Post negotiations phase**

Once you have come to the final agreement, it is important to have it down in writing along with both parties' signatures. Before the agreement is signed or formally endorsed, do not say anything about the terms agreed because your next sentence could break the agreement.

Sell the agreement to the constituents of both parties i.e. what has been agreed, why it is the best possible agreement, what benefits will accrue, etc.

Implement the agreement e.g. place contracts, set up joint implementation teams.

Establish procedures for monitoring the implementation of the agreement and dealing with any problems that may arise.

8.6 Summary / Conclusion

1. The most important part of negotiation is planning. Preparing well, will give you an advantage when negotiating.
2. Only use, the knowledge and experience you need to achieve your objective.
3. Have confidence and be seen that you can keep control at all times.
4. Aim highly but do not under estimate the opposition.
5. If you are selling something, be persuasive and offer some incentive to keep customers interested.
6. Do not close an agreement until you are happy. This could however be difficult if you have been put in a tight corner. But this would perhaps be an effect of poor preparation.

Questions:

a) *You have recently been appointed a buyer for a leading food manufacturer. You have been asked by the purchasing manager to make a presentation on "Effective*

Negotiation" for an upcoming seminar. Draft presentation notes that you will distribute to the participants.

b) *What are the barriers to effective procurement negotiation?*

c) *What is the role of procurement in negotiation?*

Chapter 9

Capital and Revenue Procurements

9.0 Learning objectives

At the end of this session candidates will be able to demonstrate an understanding of capital and revenue procurements by:

- *defining capital and revenue procurements,*
- *identifying categories of capital items,*
- *distinguishing between capital and revenue procurements,*
- *identifying factors to consider in procuring capital items, and*
- *analysing the application of the lifecycle costing technique to capital procurements.*

9.1 Introduction

Capital goods or purchases are long term requirements often with a high value used for production of goods or services. Buying capital goods such as buildings, plant and machinery and computers, differences in several ways from the purchase of non-capital goods. Unlike production goods or office supplies, capital goods are not bought for current needs to be used up in a short time but are bought for long term requirements to be used for the production of goods and services.

Capital goods are items which are not obtained for re-sale either directly or after processing but for retention within the business.

Revenue procurements on the other hand are those which are re-sold to the customer and hence bring some revenue to the organization.

9.2 Categories of capital goods

a) *Buildings;* – this refers to permanent construction on a site to house or enclose equipment and personnel employed in industrial, institutional or commercial activities.

b) *Installation equipment*; – this refers to essential plant or machinery or other major equipment used directly to produce the goods and services of the producing organization.

c) *Accessory equipment;* – this is a durable major equipment used to facilitate the production of goods and services or to enhance the operation of goods and services.

d) *Operating equipment;* - this refers to semi - durable minor equipment which is movable, used in but not generally essential to the production of goods and services. For example; brooms, special foot ware, etc.

e) *Tools and Instruments;* - these arc semi - durable or durable potable minor equipment and instrument required for producing, measuring, calculating, etc. associated with the production of goods and services e.g. word processors, surgical instruments, timing devices, etc.

f) *Furnishing and fitting equipment;* - these are all goods and materials employed to fit buildings for their organizational purposes but not equipment used specifically in production. For example; carpets, furniture, benches, etc.

9.3 Distinctions between capital and revenue procurements

There are a number of factors that distinguish procurement of capital goods from procurement of revenue goods: -

- The basic procurement price of a capital asset is only an element and sometimes not an important element in total cost of acquisition. Other costs are also relevant and may arise anytime over the life of an asset.
- The procurement of capital items tends to be non-recurring. It is unlikely to have had a similar procurement in the recent past.
- The monetary value of the procurements may be high suggesting a need for specialized techniques of evaluation and control. This also raises a question relating to financing of the procurement.
- The benefits to be obtained from the procurement are often intangible and difficult to evaluate. For example, a machine may be replaced by a superior model in order to secure quality improvement.
- Negotiations are usually more extended and complex than in other acquisition.
- Specifications for capital items are usually more difficult to draft because of technical complexity of the items to be procured.
- A team approach is usually needed in which the contribution of other departments and not just that of procurement must be effectively coordinated and managed.
- Buying a capital asset usually means buying a service too.
- Some capital goods can be shared by partners.
- In capital goods' acquisition, there is consideration for buying used items.

9.4 Factors to consider when buying capital equipment

Purpose of the equipment

Flexibility i.e. the equipment should be capable of being used for purposes other than those for which it was primarily acquired.

Standardization; - the equipment should be compatible with any already installed equipment so as to reduce the cost of holding stock.

Life; - this refers to the period the equipment will have before it is written off due to depreciation or obsolescence.

Reliability; - the equipment should be reliable so as to avoid breakdown which leads to loss of good will through extended deliveries and possibilities of high investment in stock.

Durability; – the equipment should be used for a long time for its intended use.

Cost of operation; – for example; cost of fuel, power maintenance, etc. it is important to ascertain whether specialized or additional labour will be required.

Cost of installation; – does the price include the cost of installation, commissioning and training of operators.

Cost of maintenance i.e. can the equipment be maintained by own staff or special arrangements have to be made.

9.5 Lifecycle costing

Lifecycle costing has been defined by the Chartered Institute of Management Accountants (CIMA) as;

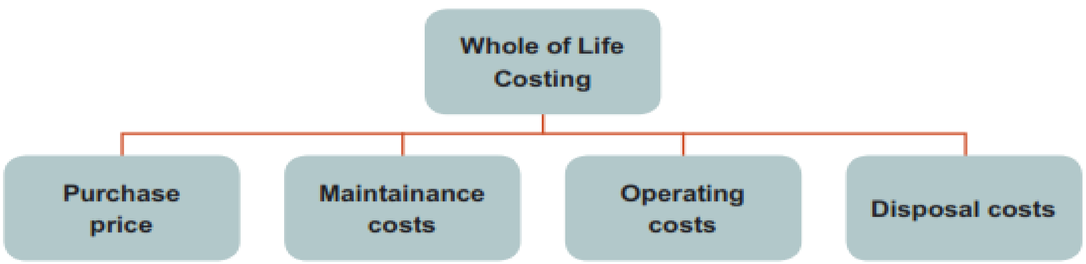
> *'the practice of obtaining over their lifetime the best use of the physical assets at the lowest cost to the entity (Terotechnology). This is achieved through a combination of management, financial, engineering and other disciplines.'*

The term *Terotechnology*, coined in 1970, is derived from the Greek verb '*tereo*' and means literally *'the art and science of caring for things*'. Lifecycle costs are therefore those associated with acquiring, using, caring for and disposing of physical assets, including feasibility studies, research, development, design, production, maintenance, replacement and disposal, as well as the associated support, training and operating costs incurred over the period in which the asset is owned.

Whole-of-life costing (also known as life-cycle costing or total cost of ownership) is the most relevant in a procurement context. This is the cost to the organisation of acquiring the product (including design and planning where applicable), installing or commissioning it, training others to use it, operating it, repairing it, maintaining it, and disposing of it at the end of its life *(see figure 9.a)*.

For some types of products, the lowest cost option up front may not be the cheapest over the life of the asset. This is typically the case for products that use power, water, fuel or other consumables, or have complexities associated with disposal (such as containing hazardous materials).

Figure 9.a: Life-cycle costing model



Acquisition costs	***Operating costs***
• Purchase cost	• Labour
• Delivery charge	• Materials
• Insurance and taxes	• Consumables
• Installation and commissioning	• Energy supply and consumption
• Training and support	• Contract and supplier management
• Internal costs associated with changing from the incumbent supplier (which should be identified prior to tenders being received)	• Transaction costs
	• Environmental costs
	• Cost of change (e.g. a decision to use alternative materials)

Maintenance costs	***End-of-life costs***
• Specialist labour	• Safe disposal
• Specialist tooling	• Resale
• Spare and replacement parts	• Ongoing liabilities
• Reduced output with age	• Decommissioning
• Frequency of maintenance and recommended downtime	• Removal for sale or scrap
• Servicing and inspection regimes	• Reinstatement of land or buildings for alternative use
• Costs associated with equipment downtime	

Life-cycle analysis is a more complicated method to measure the environmental impacts of a product over its life ('cradle to grave'). It is a highly technical and specialist area, governed by the ISO 14040 set of standards, and covers:

- extraction of raw materials
- product manufacturing
- packaging and distribution
- product usage/consumption
- end-of-life disposal.

Life-cycle analysis does not take account of social and economic considerations associated with a particular activity or product. In a procurement context, life-cycle analysis has fairly limited application, although the term is often used interchangeably with total cost of ownership and whole-of-life cost.

Life-cycle thinking (rather than life-cycle analysis) is a useful concept for procurement professionals to be aware of, which means having an understanding of where in the life cycle a product's main impacts occur. This can inform development of specifications which address these impacts.

9.5.1 The importance of lifecycle costing

Unless lifecycle implications are taken into consideration, there is a danger that initial cost on delivery will be used as the sole criterion when selecting a physical asset. This simplistic approach can, however, have detrimental implications for the total lifecycle cost of the item.

Lifecycle costing is of particular importance for products liable to rapid technological or style changes. From the standpoint of producers, rapid technological change may mean that revenue from sales may be insufficient to make the original investment in design and development worthwhile. From the buyer's viewpoint, the asset may, to a greater or lesser extent, be obsolete before the amount invested in its procurement has been recouped.

Procurement executives concerned with the acquisition of capital items are therefore advised to:

- Ensure that specifications include reference to factors that have a bearing on the cost of ownership of an asset, such as maintenance and the availability of spares.

- Create a communication bridge with the supplier regarding developments in the particular field

- Treat initial costs as only one of many factors that will contribute to their total life cycle costs
- Ensure all factors that may have implications for the total lifecycle costs are given due consideration before recommending the procurement of a particular asset.

9.5.2 Application of lifecycle costing

Apart from the procurement of capital equipment, lifecycle costing can be applied to:

- *Acquisition control;* estimating the future costs of large- scale acquisitions
- *Optioneering;* comparing the returns on a number of expenditure options
- *Pricing;* ensuring that, in addition to direct and general overhead costs (not including depreciation), an interest charge is included that reflects the overall costs of capital required to satisfy all capital providers so that the annual equivalent cost of fixed assets will recover both depreciation and a profit margin that satisfies all providers.
- *Project analysis;* measurement of the cost of a project against its targets
- *Product design;* provision of data that will enable designers to modify or improve designs that will improve consumer satisfaction and give a product greater cost advantage over those of competitors
- *Replacement decisions*; as the cost of using and repairing physical assets increases with age, lifecycle costing can indicate when it is more beneficial to dispose of an asset and procure a replacement than it is to meet increasing maintenance costs.
- *Supplier support;* provision by suppliers of comparative lifecycle estimates for their products.

9.5.3 Lifecycle costing methodology

The life costing methodology involves the following four basic steps;

1. Identify all relevant costs. As in the *figure on the next page*, these are initially broken down into acquisition and operation, maintenance and disposal costs, and then broken down further under each heading.
2. Calculate the costs over the anticipated life of the asset of all elements identified above. Such costs may be:
   - Known rates, such as operator pay, maintenance charges

- Estimated rates based on historical figures or other empirical data
- Guesstimates based on historical figures or other empirical data
- Guesstimates based on informed opinion.

3. Use discounting to adjust future costs to apply to the present- that is, the time when the procurement decision is made. This reduces all options to a common base, thereby ensuring fair comparison.
4. Draw conclusion from the cost figures obtained by the above procedure.

Question: What is the buyer's role in acquiring capital items?

Chapter 10

Procurement Planning

10.0 Learning objectives

At the end of this session candidates will be able to demonstrate an understanding of procurement planning by:

- *describing the procurement planning process*
- *explaining the rationale for procurement planning*
- *appreciating the guidelines to preparing procurement plans*
- *recognizing the qualities of a good procurement plan*
- *assess the importance of procurement planning, and*
- *examining the samples of procurement plans.*

10.1 What is procurement planning?

Procurement planning is a key function in all organizations be it public or private. Its objective is to provide the procuring organisation with continuity of inputs to enable it to achieve strategic objectives. Harvey

Procurement planning is defined both as a process used by contracting authorities to plan contracting or purchasing activity for a specific period, as well as a plan for the purchase of a specific requirement. To achieve both definitions those carrying out procurement need to be closely involved with budget managers and user departments.

Specifically, Procurement planning refers;

> *'to the setting of procurement targets and activities by a procuring organisation in a manner that spreads them out in an annual calendar in accordance with the availability of resources and needs.'*

10.2 Why Procurement Planning?

Mackay said, "Failures don't plan to fail; they fail to plan." Planning is a vital part of the procurement activities. The amount of planning undertaken is one of the distinguishing characteristics between good procurement professionals and others.

The purpose of procurement planning is threefold:

a. first, to clarify and quantify (to the extent possible) the technical, cost, and schedule objectives of the procurement;
b. second, to define the plan for accomplishing the objectives; and third,

c. to determine a methodology for evaluating performance against defined objectives during the time that the contract is being carried out.

Whether or not a procurement plan is required will depend on the complexity of the requirement, the sensitivity of the requirement, and/or the estimated value of the requirement, e.g., capital projects.

Within the framework of the annual procurement plan, this is the stage in the procurement process when the objectives of making procurement are considered in relation to stakeholder needs and when a planned approach to the procurement is set out. This process is vital to the success of the procurement, although it may be executed in parallel with or immediately after the specification. Where a sample procurement plan is provided, auditors will want to see a clear procurement plan signed off by key stakeholders, as it represents a decision to proceed. Procurement level plan could also involve co-operation with other procuring entities.

A Procurement plan is a requirement under the public procurement legal framework and many organizations' policies. An annual procurement plan is also the first step in the procurement planning process. Ideally, the relationship that procurement officers have with user and budget departments should be so close that they are involved at an early stage of the budget cycle, where departments are identifying their needs in the respective budget year.

10.3 Procurement planning process

Procurement planning may undergo the following stages;

1. Identifying the needs (listing of needs);
2. Determining the priorities;
3. Determining the required budget;
4. Determining the different lots (packaging);
5. Determining the procurement methods;
6. Determining the deadlines for starting and the duration of every activity;
7. Determining a general procurement plan;
8. Determining a specific procurement plan.

The public procurement regulatory framework of Uganda i.e. the Public Procurement and Disposal of Public Assets regulatory framework provides an illustrated procurement planning process as in charts below.

1. Preparation of departmental procurement plans by user departments in line with approved work plan and budget of the Procuring and Disposing Entity (PDE) as provided under Regulation 3(2) PPDA PDEs regulations, 2014.

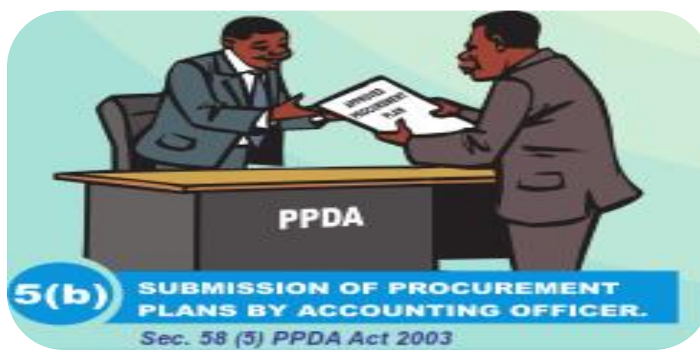
2. Consolidation of all user department procurement plans into a single procurement plan of the Procuring and Disposing Entity as provided under Regulation 3(1) PPDA 2014 amendments for PDEs. This is aimed at aggregation of procurements to gain economies of scale in procurement and make use of framework contracts.

3. Approval of procurement plans i.e. after consolidation of procurement plans by the procurement and disposal unit, the PDU then forwards them to the Contracts Committee for approval. This is as provided under Regulation 3(4) of the 2014 PPDA amendments for PDEs.

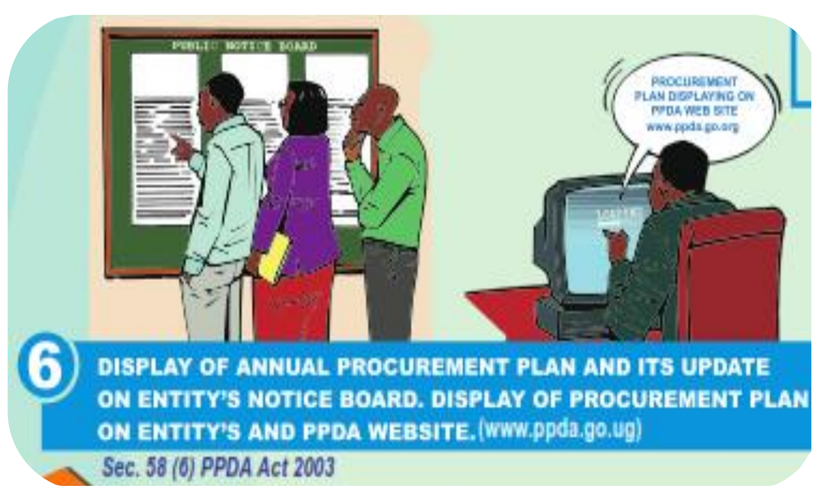
4. Procurement plans approved by the Contracts Committee are forwarded to Management /Board/Council for approval

5. Approved Procurement plans are submitted to the Ministry of Finance by the Accounting Officer as required under Section 58 of the PPDA Act, 2003. This facilitates tracking of funds release to the PDE by the Ministry.

Also copies of procurement plans are also submitted to the PPDA Authority by the Accounting Officer as required under Section 58(5) of the PPDA Act, 2003.



6. The annual Procurement plan and its update are displayed on the entity's notice board as well as its website and that of the PPDA Authority. (www.ppda.go.ug). This is done following the provisions under Section 58(6) of the PPDA Act, 2003.



10.4 Qualities of a good procurement plan

An ideal procurement plan should have the following key qualities;

a. *Simple but specific* i.e. reflecting particular procurement that is desired.
b. *Measurable* the procurement plan should be quantified in order to physically determine progress.
c. *Realistic/achievable*; a procurement plan must be realistic and achievable taking into account the resource constraint (financial, staffing and the conditions/environment in which it will be implemented. So a procurement plan must not be a mere wishful list of items but rather is should be linked to the budget.
d. *Time bound;* this requires a procurement plan to specify a time frame in order to improve manageably.
e. *Relevant;* a procurement plan must be relevant to the local needs and therefore a good procurement plan must be conceived through popular participation with all the stakeholders and experts taking part in the planning process.

10.5 Advantages of Procurement Planning

a. Links are forged between the user unit, the finance unit, and the procurement unit from the earliest notion of there being requirement/need;
b. Economies of scale are gained by uniting the requirements of different areas;
c. There are no surprises when requirements manifest themselves in later months;
d. Everyone can plan and schedule resources for the coming year more effectively;
e. The procurement plan is linked to the national plans and strategic plan of the procuring organisation.

10.6 Consequences of not undertaking procurement planning

By not undertaking such a planning process:

a. Stakeholders, the finance department and the procurement team would work in isolation, unaware of each other's' needs.
b. Requirements received by the procurement team would be surprises, for which no pre-planning would have been possible.
c. Procurement officers would miss information on the potential requirements because they would not know they existed.
d. Economies of scale would be lost because the requirements of different areas would be processed separately.

e. Requirements would not be timed to the year-end of potential economic operators and so better deals could not be achieved.
f. Resource scheduling would be difficult. Periodic indicative notices would not be published as easily.
g. Co-operation with other contracting authorities would be more difficult as visibility of future needs would be limited.
h. There would be no procurement plan linked to the strategic plan of the contracting authority.

10.7 Samples of Procurement plans both general and specific

A general procurement plan

N°	Title of tender	Estimated cost	Source of funds	Tendering method	Prequalification (yes/no)	Prior study (Yes/No) Estimated duration	Local Preference (Yes/No)	No objection to tender document (Yes/No)		Publication period	No objection to evaluation report (Yes/No)		Contract Management : Supervision and control mission (Yes/No)
									FINANCING			FINANCING	

A Specific procurement plan

N°	Title of tender	Estimated cost	Source of funds	Tendering method	Required resources	Preparation of tender document (study)				No objection on the tender document				Advertisement		Bid opening		Bid evaluation		Expertise required	No objection				Notification and contract signing		Recruitment of the supervising mission	Contract management			
						S		E				Financing											Financing					S		E	
						TD	ED	TD	ED	TD	ED	TD	ED	TD	ED	TD	ED	TD	ED		TD	ED	TD	ED	TD	ED		TD	ED	TD	ED

KEY:
S: Start
E: End
TD: Tentative date
ED: Effective date (to be filled in at appropriate time)

Chapter 11

Procurement Ethics

11.0 Learning objectives

At the end of this session candidates will be able to demonstrate an understanding of ethics in procurement activities by:

- *describing the main ethical and unethical practices in procurement*
- *explaining the guidelines to ethical procurement and supply*
- *identifying the unethical practices in the procurement process*
- *appreciating the role of ethics in procurement*
- *appreciating the role of codes of ethics and integrity safeguards, and*
- *describing the business-to-business ethical issues that ought to be embraced in procurement.*

11.1 Introduction to Ethics

The majority of organisations use supply chains in order to support their business activities, using third parties to provide goods, works and services. It makes sense to outsource to specialists the aspects of the business that are not core competencies however failing to understand how these goods, works and services are delivered can lead to damaged reputations and even worse legal consequences. There have been several high-profile cases in recent times both in public and private sector agencies to highlight this.

The exercise of ethical procurement and supply is fundamental to dealing with such challenges in organisations.

11.2 Key definitions

"Ethics" is concerned with the moral principles and values which govern our beliefs, actions and decisions.

"Procurement ethics" is concerned with the moral principles and values that govern beliefs, actions and decision made by the parties involved in procurement. The term values in this definition is concerned with questions relating to what is right, good and just. It forms the basis on which ethical decisions are made.

"***Ethical procurement***" (often referred to as responsible procurement) refers to procurement processes which;

- *respect fundamental international standards against criminal conduct (like bribery, corruption and fraud) and human rights abuse (like modern slavery) and respond immediately to such matters where they are identfiied and*
- *result in progressive improvements to the lives of people who contribute to supply chains and are impacted by supply chain decisions*

"***Corrupt practice***" means the offering, giving, receiving, or soliciting, directly or indirectly, of anything of value to influence the action of a public official in the procurement process or in contract execution;

"***Fraudulent practice***" means a misrepresentation or omission of facts in order to influence a procurement process or the execution of a contract;

"***Collusive practices***" means a scheme or arrangement between two or more bidders, with or without the knowledge of the Borrower, designed to establish bid prices at artificial, non-competitive levels;

"***Coercive practices***" means harming or threatening to harm, directly or indirectly, persons, or their property to influence their participation in a procurement process, or affect the execution of a contract.

10.3 Key guidelines to ethical procurement and supply

Business managers today owe to embrace the key guidelines to ethical procurement and supply in order to realize value for money. Such guidelines should cover aspects like;

- The importance of ethical procurement and supply
- Standards and legal responsibilities
- Organisational responsibilities
- Personal responsibilities
- Areas of risk for unethical procurement and supply
- Adopting ethical procurement codes of practice.

11.3.1 The importance of ethical procurement and supply

There are three main reasons why ethical procurement and supply is essential;

1. Protects the rights of workers
2. Protects the rights of customers/consumers
3. Safeguards employees by protecting the reputation of the organisation.

Over 29 million people are subjected to forms of modern slavery, which can be seen through human trafficking, forced labour and slavery. Vulnerable people are abused by scrupulous businesses to provide goods, works and services despite this behaviour being illegal in every country in the world.

Customers and consumers should be safe in the knowledge that when they buy goods and services, the people or organisations involved within the supply chain are honest, trustworthy and have high moral standards. Only through robust due diligence procedures and a comprehensive understanding of how the goods, works or services are produced, will the end user be protected from poor or dishonest business practices.
The damage to an organization's reputation if direct or indirect unethical behavior is revealed can be devastating to a business. Pressure groups like Transparency International regularly name and shame organisations or sectors who abuse best practices, people or resources. This has an impact on potential investors, funders, donors but more importantly on current and potential employees. Short term gains can create long term problems therefore anyone responsible for procuring goods, works or services has an obligation to safeguard the interests of all stakeholders and adopt ethical best practice standards.

11.3.2 Standards and legal responsibilities

Legislation exists to penalise those behaving inappropriately along with international and industry standards, which define good practice, as explained below.

International Labour Standards: these provides for

a. Freedom of association and the effective recognition of the right to collective bargaining
b. Elimination of all forms of forced or compulsory labour
c. Effective abolition of child labour
d. Elimination of discrimination in respect of employment and occupation.

Local laws in supplier countries: Local agents will carry out due diligence on suppliers to ensure compliance with all local laws.
Buyer country laws with extraterritorial reach: States or countries legislate outside of their own jurisdiction. For example, California has legislated to require monitoring, reporting and transparency around supply chains outside of the home organization's jurisdiction.
International Guidelines: this covers

a. United Nations (UN) Guiding Principles on Business and Human Rights
b. Organisation for Economic Co-operation and Development (OECD) Guidelines for Multi National Enterprises

The standards are established and apply not only to direct impacts of business activity but also to indirect relationships.
Private Standards: Standards are set by industries, companies and sectors. Professional bodies also provide accreditation models, e.g. Chocolate, coffee, diamonds, electronics, gold, cotton and fisheries.

World Economic Forum: Partnering Against Corruption Initiative (PACI) is a global, multi-industry, multistakeholder anti-corruption initiative. It was set up to raise business standards and to contribute to a competitive, transparent, accountable and ethical business society.

UN Global Compact: Strategic policy initiative for business committed to aligning operations and strategies with ten universally accepted principles in the areas of human rights, labour environment and anti-corruption.

Extractive Industry Transparency Initiative (EITI): A global coalition of governments, companies and civil society groups working together to improve openness and accountable management of revenues from natural resources. Encourages transparency of revenue flows and production data to avoid corrupt practices.

Transparency International: Over 100 national chapters globally work together with a number of partners in government, business and civil society to mitigate against bribery.

11.3.3 Organisational responsibilities

In order to protect employees, the organisation and their agents, codes of practice and policies should be in place to mitigate risk and reinforce appropriate behaviours. The formats most widely adopted are;

- Procurement guidelines
- Due diligence procedures
- Code of Conduct for employees, its agents, suppliers and outsourced companies. This should be
- signed off by the governing body (e.g. Board of Directors) and supported by a number of policies approved by the CEO.
- Statutory declaration to be signed by suppliers certifying they understand the organisation's approach to modern slavery.
- HR policy, which incorporates details about whistle blowing. Best practice suggests a Whistle Blowers Hotline is in place, along with details about the circumstances where whistle blowing is required, the method of reporting and the protection offered to whistle blowers.
- Business ethics policy, which should contain anti-bribery policies and procedures. These should be signed by staff and suppliers on an annual basis. It is highlighted within anti-bribery and anti-corruption laws, that it is an offence if there is seen to be a "failure by a commercial organisation to prevent bribery", therefore this activity will help to mitigate this risk.
- Anti-bribery and anti-corruption training for procurement staff and suppliers.
- Ensuring that the organisation's representatives demonstrate integrity. This should be seen in the following four areas:

1. ***The process***: This must be fair and reliable. Procurement decisions must be driven by the best deal for the organisation and shouldn't be influenced by other factors, e.g. personal relationships.
2. ***The market***: Markets must be competitive and free from interference, i.e. anti-competitive behavior. In many countries, legislation exists to curb anti-competitive practices.
3. ***The organisation***: Purchasing and supply organisations are equally responsible for demonstrating a commitment to deal with integrity. Organisational cultures should reflect this value and senior executive teams must ensure through appropriate policies and governance, that the highest levels of integrity are achieved.
4. ***The people***: People are involved in creating commercial contracts and relationships. Human nature means that people will behave in different ways and some are more easily influenced than others. Organisations must ensure that staff understand the importance of integrity in procurement related activities.

11.3.4 Personal Responsibilities

The individuals responsible for procuring goods and services on behalf of an organisation need to be compliant with the business ethics policy, company procurement guidelines and due diligence procedures. Integrity can be safeguarded in the following ways: (See Chart 1.1)

11.3.5 Areas of risk for unethical procurement and supply

The risks when procuring goods, works and services are apparent at each stage of the procurement and supply process. The following examples highlight where unethical practices can occur.

Pre-Contract Award

- *Manipulation of identified requirements*; the requirement identified by the end user may be manipulated to facilitate bribery and corruption within works, services or goods contracts to the benefit of a single supplier.
- *Biasing designs and specifications*; Design and specifications may be deliberately biased to dishonestly influence the award of a contract towards a particular supplier.
- *Allowing inferior vendors proceed the selection process*; Due diligence within the bidding process can be influenced to allow inferior vendors through the selection process where they may commit fraud later.

- *Manipulating bid evaluation*; Evaluation and scoring of bids may be manipulated to influence the selection and award of a contract.
- *Deliberate single source justification*; someone from the organisation deliberately writes a single source justification to avoid competitive selection. This may be to avoid the tender process or to influence the award to a pre-determined supplier.
- *Award manipulation*; the award of a contract may be manipulated or influenced regardless of the selection process.

Chart 1.1: Integrity safeguards

Post-Contract Award

- *Quality control*; corrupt acquisition or acceptance of inferior or substitute products.
- *Quantities received*; corrupt receipt of lesser amounts specified within the contract or falsely representing the need for additional goods, works or services than required.

- *Payments and processes*; creation or illicit authorization of false invoices or corrupt authorization of payments for incomplete or non-existent works, services or goods.
- *Authorization of additional works*; corrupt manipulation of contracts to award further works.

11.3.6 Adopting ethical procurement codes of practice

For an ethical procurement and supply chain to be in place, proactive engagement is required throughout the entire supply chain. Ethical practices must be encouraged as the repercussions for failing to address this issue can be catastrophic. The following considerations are necessary to achieve compliance.

1. Develop standards and policies

Purchasers must have clear standards and policies on ethical issues, which must be evident throughout the entire supply chain.

2. Supplier selection

Ethical criteria should be used for selection, which is consistent with the purchaser's stated standards and policies. The Official Journal of the European Union (OJEU) process requires this information to be included within the invitation to tender (ITT) specification.

3. Measurement

Clear performance standards regarding ethical practices should be included within the specification, allowing suppliers to understand their responsibilities and obligations prior to bidding.

4. Ethical monitoring

Regular review meetings should be conducted by the purchaser with the supplier and any other parties within the supply chain. Unannounced 'spot checks' are a useful measurement tool to avoid cover ups.

5. Proactive contract management

Look for early warning signs of potential problems. This might involve site visits and other checks for non-compliance.

6. Robust contractual clauses

Clear standards of behaviour should be detailed within the contract with explanations of remedial action or penalties should the standards not be acceptable. Confidentiality or non-disclosure clauses can also be included although separate confidentiality and non-disclosure agreements can be set up. Sub-contractors or third-party agents should also be bound by the terms of the contract.

British Institute of Facilities Management (2014): Ethical Procurement and Supply: *Guidance Notes for Facilities Managers;* BIFM September 2014.

11.4 Business-to-business ethics

There are complex problems to be resolved when addressing ethical and social responsibility issues and many of these issues are extremely sensitive. Recommended best practice includes developing and understanding suppliers' operations and offering guidance and support when improvement is necessary or appropriate.

Buyers should seek appropriate guidance, be open about concerns, and engage positively with suppliers and internal customers or peers, however difficult that may be. The resource implications of addressing these issues must be balanced against the potential risk to the reputation of the organisation and, in the public sector, the organisation's requirement to comply with the EC procurement rules (where the permitted primary criteria are solely economic).

Buyers have a responsibility for the supply chains from which goods and services come into their organisation or directly to their customers. CIPS believes this should include ethical as well as commercial and technical guidance and support.

The CIPS Personal Ethical Code is the starting point for developing a code of practice for business-to-business ethics. The issues include the following:

- ***Transparency, confidentiality and fairness:*** All suppliers should be treated fairly and even-handedly at all stages of the procurement process.

  This means being open with all those involved, so that everyone, especially suppliers, understands the elements of the process, that is, the procedures, timescales, expectations, requirements, criteria for selection and so on. Supplier confidentiality should be safeguarded, and unsuccessful suppliers should be debriefed with as much transparency about the procurement process as can be provided, for example, on the weaker aspects of their tender.
- **Use of power***: Buyers should discourage the arbitrary or unfair use of purchasing power or influence.*

  Power is a key element in supply relationships. The exertion of undue influence or the abuses of power, as well as being unprofessional, may contravene relevant legislation and are unlikely to achieve long-term best value for money.

  It is important to ensure compliance with all applicable legislation, such as restraint of trade and anti-trust legislation, the Competition Act 1998, in particular Chapter II, Abuse of Dominant Position, and the Treaty of Amsterdam, Articles 81 and 82, which address anticompetitive practices and abuse of dominant position.
- **Corruption**: *Buyers must not tolerate corruption in any form.*

  Buyers aware of any corrupt activity have a duty to the profession and to their employing organisations to alert their senior management. Bribery is a criminal offence in the UK (and in most other countries) and the law is being strengthened to include offshore bribery. CIPS fully supports the Organisation for Economic Cooperation and Development (OECD) convention on combating bribery of foreign public officials in international business transactions.

- **Declaring an interest:** *All personal interests should be declared.*
  Buyers should encourage colleagues to declare any material personal interest which may affect, or be seen to affect their impartiality or judgement, in respect of their duties. Examples include owning a significant shareholding in a supplier or close family members being employed by a key supplier.
- **Business gifts and hospitality**: *There's no such thing as a free lunch*
  The offer and receipt of business gifts and entertainment are sensitive areas for buyers, despite being recognized as standard business practice. Organisations should have a clear policy on accepting business gifts and buyers should encourage colleagues to comply with any such policy.
- **Payments from suppliers**: *Suppliers should not have to pay to be included on an approved or preferred supplier list.*
  Suppliers should be selected on the basis of meeting appropriate and fair criteria and should only be invited to contribute towards the costs of joint projects or initiatives where there are clear and tangible business benefits to the supplier.
- **Payment terms**: *Late payments undermine an organisation's credibility*
  Buyers should ensure that their suppliers understand and agree to the buying organisation's payment terms. Buying organisations should try to ensure that valid invoices are paid in accordance with the agreed terms. Buyers should work with colleagues to ensure that their employer's business processes enable payments to be made promptly.
- **Barter and reciprocal trading:** *Where appropriate, barter is acceptable business practice, but reciprocal trading may not be.*
  Barter is trade by exchange of goods or services for other goods or services. There is no exchange of money and, as barter is not usually a condition of contract between two parties, coercion is not an issue, provided both parties have a current business need for the goods/services of the other party.
  However, reciprocal trading which is conditional on suppliers also being customers of an organisation, is unacceptable business practice. Reciprocal trading is acceptable only when there is no coercion, both parties are in agreement and there is mutual benefit and transparency.
- **Supplier relationships and competition**: *Relationships with suppliers, regardless of duration, should be managed professionally.*
  Buyers should manage suppliers, and supply networks comprising multiple tiers of suppliers, in a professional manner. Both short- and long-term contracts have their place, but from time to time longer-term contracts especially should be

subject to open and transparent competition. Where there is only one supplier capable of meeting the requirements, established internal business controls should be respected in the quest for the best value for money solution.

Chapter 12

E-Procurement

12.0 Learning objectives

At the end of this session candidates will be able to demonstrate an understanding of Electronic Procurement by:

- *defining the e-procurement concept and its trend*
- *describing the e-procurement cycle*
- *explaining the drivers and enablers of e-procurement*
- *appreciating the strategic contribution of e-procurement to procurement management*
- *examining the potential of e-procurement to help leverage supply chain operations, and*
- *realizing the changes brought to procurement and supply by e-procurement.*

12.1 Introduction to e-procurement

E-procurement sometimes also known as *supplier exchange* is the Business-to-Business (B-2-B) or Business-to-Consumer (B-2-C) purchase and sale of supplies and services through the internet as well as other information and networking systems such as **EDI**, (Electronic Data Interchange) and Enterprise Resource Planning (ERP).

The Chartered Institute of Purchasing and Supply (CIPS) defines e-procurement as:

> *'the combined use of electronic information and communications technology (ICT) in order to enhance the links between customer and supplier, and with other value chain partners, and thereby to improve external and internal P&SM processes. E-Procurement is a key component of e-business and e-commerce'.*

The beginnings of e-Procurement were in the early 1980s with the development of electronic data interchange (EDI). This allowed customers and suppliers, most often in the fast-moving consumer goods business (FMCG), to send and receive orders and invoices via secure store and call forward networks. These EDI systems allowed businesses to exchange and synchronize master data files on products, prices, specifications and information about each other's locations and trading practices

In the 1990's internet software started to become available, and software companies began to develop buyer managed electronic catalogues for use by vendors. Sometimes these proved to be too unwieldy due to failures in communication between customers and suppliers (salesman and buyers), and software companies started to customise, maintain and host some catalogues, effectively becoming “the intermediaries between the buyer hub and the vendor spokes” and vice-versa. As the catalogues became outsourced, software companies started to offer the same catalogues to a number of buyers.

Another development in e-Procurement that arose at a similar time was the proliferation of e-marketplaces which covered some of the electronic trading needs of certain industries, such as automotive and aircraft. These act as a virtual market place for suppliers, distributors, agents and customers.
Typically, E-Procurement websites allow qualified and registered users to look for buyers or sellers of goods and services. Depending on the approach, buyers or sellers may specify costs or invite bids. Transactions can be initiated and completed on-line (see Figure 11.a). Ongoing purchases may qualify customers for volume discounts or special orders.

E-procurement software may make it possible to automate some buying and selling. Companies participating to be able to control parts inventories more effectively, reduce purchasing agent overheads and improve manufacturing cycles, e-procurement is expected to be integrated with the trend towards computerized supply chain management. E-procurement is done with a software application that includes features of supplier management and complex auctions.

Figure 11.a: The e-procurement cycle

E-Procurement enables:

- The automatic processing and auctioning of orders and of related trading documents and data, thereby enhancing the speed and certainty of doing business at a lower total cost
- Improved workflow of the internal procurement process - this enables end-user self-service and decentralization with centralized control through company-specific catalogues
- New functionality - such as e-Requests For Quotations (RFQs) and on-line bidding in e-auctions (both conventional and Dutch)
- Use of potentially more efficient and cheaper connectivity methods - such as the Internet and XML (a computer language for coding content and delivery) however, these may result in a lack of security
- Connectivity to external sources of information - e.g. databases, catalogues and portals such as e-Hubs and e-marketplaces
- Connectivity to external supply chains - for example, extranets and allowing shared real time information (such as suppliers accessing real time sales)
- Sourcing - for example, using intelligent search engines and data mining
- Connectivity to internal systems and sources of information – these include inventory management, maintenance management and Materials Resource Planning (MRP), Enterprise Resource Planning
- (MRP & MRPII) systems amongst others
- Payment systems - e.g. links to banks, credit card companies and purchasing cards
- Improvements in supply chain mechanisms and consortia etc. leading to mutual benefit

12.2 The key drivers and enablers of e-Procurement

Noting that e-procurement is the electronic integration and management of all procurement activities including purchase requests, authorization, orderly, delivery and payment between the supplier and the purchaser then this system should be driven by the factors such as: the *right price*, right *place*, *right time*, right *quantity*, right *quality*, right *source* and right *service*.

To successfully conduct electronic procurement across borders, e-procurement systems rely on some key enablers and these are;

a) **e-Signature (**Digital Signature): Data in electronic form which are attached to or logically associated with other electronic data and which serve as a method of authentication with regard to this data.
b) **e-Identity:** Dynamic collection of all attributes (characteristics) in an electronic format related to a specific entity (Citizen, enterprise or object) which serve to ascertain a specific identity.
c) **e-Attestations** (Virtual Company Dossier): A set of certificates and attestations in electronic format to be provided by the suppliers to prove compliances with the selection and exclusion criteria of the procurement process.
d) **e-Catalogues:** Electronic supplier catalogues, prospectuses, used to prepare and submit offers or parts of them.
e) **e-Archiving:** Use of electronic means for long-term preservation of documents in digitized format ensuring that they can be easily retrieved without conversions.

12.3 E-procurement changes and Benefits

The resulting benefits to buyers will be:

- Reduced transaction costs and cycle times
- Possibility of developing Vendor Managed Inventory
- Improvements in Just in Time deliveries
- More accurate deliveries due to reduced input order errors by suppliers
- Shared performance measurement data which encourages improved supplier performance
- Potential for less expediting by the buyer as the supplier acknowledges orders by exception which automatically updates the buyer's system
- Reduced stock due to shared sales/forecast information
- Possibility of using self-billing

Benefits to suppliers will include;

- Engaging in the e-Business process also brings potential benefits to suppliers. These include:
- Time and cost savings in re-inputting orders
- Reduction in errors, e.g. from re-inputting orders, deliveries, returns, invoices and payments
- Reduced transaction costs and cycle times
- Holding less stock as a result of more efficient communications with customers i.e. real time sales data
- Information for use in planning and forecasting

- Improved supplier performance by sharing supplier measurement information
- Faster payment
- Improved management information

E-Procurement has changed the dynamics of the Procurement and Supply Management (P&SM) profession by, for example, placing a greater emphasis on knowledge management. It is suggested that e-Procurement will change the culture of P&SM in an organisation and may lead to a greater emphasis on cost and prices.
E-Procurement can release time to be spent on more value-adding aspects of purchasing, such as the development of end users' purchasing competencies and the development of suppliers. CIPS believes it is an opportunity to deploy competencies to the greatest effect.

CIPS also advises professional procurement practice to consider how e-Procurement can enhance transactional purchasing by providing end users with quick and easy to use electronic systems, such as electronic catalogues for selecting and purchasing their requirement from preferred suppliers. This should reduce transactional costs by improving speed and efficiency and provide greater commitment to contracts by the reduction of 'maverick purchasing', i.e. purchases made outside of an organisation's contractual arrangements.
CIPS believes that e-Procurement has the potential to facilitate communication between purchasers, their customers, suppliers and employees. It can particularly be used as a communication tool to encourage suppliers to become more efficient and more focused on meeting the organisation's needs.

Chapter 13

Sustainable Procurement Management

13.0 Learning objectives

At the end of this session candidates will be able to demonstrate an understanding of Sustainable Procurement Management by:

- *defining the sustainable procurement concept*
- *describing the spheres of sustainable procurement*
- *explaining the drivers and elements of sustainable procurement implementation*
- *appreciating the strategic contribution of sustainable procurement practice*

13.1 What is Sustainable Procurement?

Sustainable procurement is a purchasing and investment process that takes into account the economic, environmental and social impacts of the entity's spending. Sustainable procurement allows organizations to meet their needs for goods, services, construction works and utilities in a way that achieves value for money on a whole-life basis in terms of generating benefits not only to the organization, but also to society and the economy, while remaining within the carrying capacity of the environment".

Sustainable Procurement means improving the efficiency by which public money is spent while at the same time using market power to bring about major environmental and social benefits locally and globally. It is the process of purchasing goods, services and works that takes into account the social, economic and environmental impact that such purchasing has on people and communities whilst still achieving value.

Sustainable procurement as "a process whereby organizations meet their needs for goods, services, works and utilities in a way that achieves value for money on a whole life basis in terms of generating benefits not only to the organization, but also to society and the economy, whilst minimizing damage to the environment" (Department for Environment, Food and Rural Affairs, 2006).

Due to the high-profile nature of the issue of sustainability as an issue, sustainable procurement represents a significant opportunity for the Procurement and Supply Management Professional to raise the profile of procurement and to demonstrate leadership in a key strategic area to their organisations.

The Chartered Institute of Purchasing and Supply (CIPS) Sustainable Procurement as;

> *'a process whereby organisations meet their needs for goods, services, works and utilities in a way that achieves value for money on a whole life basis in terms of*

generating benefits not only to the organisation, but also to society and the economy, whilst minimizing damage to the environment'.

The definition then elaborates on the meaning of whole life basis by stating that sustainable procurement should consider the environmental, social and economic consequences of design; non-renewable material use; manufacture and production methods; logistics; service delivery; use; operation; maintenance; reuse; recycling options; disposal; and suppliers' capabilities to address these consequences throughout the supply chain".

Sustainable procurement is a powerful driver for delivering improved economic, environmental and social outcomes, and believes that sustainable procurement underpins the achievement of cost effective, leading practice procurement. It does this by generating value for money and gaining efficiencies within and between organisations.

Hence, it is observed that Sustainable Procurement Practice has three dimensions known as *pillars* or "*the triple bottom-line issues*". These are environment, social, and economic. There are sustainable issues under each pillar that should be integrated into the procurement processes as illustrated in figure 13.a.

Fig 13.a: ***The Three Spheres of Sustainable Procurement***

Environmental: Every product or service bought has environmental impacts throughout its life-cycle from the extraction of raw materials, the manufacturing of the product through to its use and disposal. The product must be environmentally harmonious, in the sense that its manufacture, use, or disposal will not negatively impact on the environment. For example, the use of energy should be moderate (-use of energy saving lighting systems), and the method of generation should take advantage of renewable energies, to maintain fossil fuel levels. Summary, it is seeking to minimize any negative environmental impacts of goods and services purchased, across their life cycle from raw material extraction to end of life.

Social: Purchasing actions have social implications, and public procurement can be used to drive social improvements- for example working conditions for publicly contracted construction workers, disabled access in public buildings, employment opportunities for marginalized groups, working against child labour or supporting Fair Trade. Another example of social sustainability: products that have been manufactured under good conditions and fairly traded. Summarily, it is managing and monitoring supply chains to ensure that fair contract prices and terms are applied and that ethical, human rights and employment standards, as expressed in the International Labour Organisation (ILO)'s Fundamental Conventions are met.

Economic: The term economic in this case does not just mean the initial purchase price but also means efficient procurement including usage costs such as electricity and water consumption, maintenance expenditures and disposal costs at the end of its life. Also, economic sustainability ensures that there is an economic benefit both to the community from which the product was manufactured and to that in which it was sold.
This economic principle relates not only to obtaining value for money from our contracts, across the whole life of the product or service, but also ensuring as far as is possible under relevant procurement law, that local businesses, particularly Small and Medium sized Enterprises (SME's) can benefit from procurement processes by being able to supply the organization where it is feasible for them to do so. An example of a whole-of-life costing assessment is shown in. Actual procurements and projects are often more complex than the one illustrated in here. The structure should be customized to suit the particular procurement being considered.

Table 13.1a: Example of a whole- of-life costing assessment (hot water system)

Hot water system	*Calculation*	*Cost over 10 years (ex GST)*
Acquisition		
Purchase cost (RRP)	1x $1,855	$1,855
Delivery (nil)	$0	$0
Disposal of packaging (kerbside recycling)	$0	$0
Installation	$500	$500
	Subtotal	**$2,355**
Use		
Energy use	0.114 MJ per litre 1.3 cents per MJ 200 litres per day 365 days per year 10-year life	$1,081.86
Maintenance and repair	@ $250 (service twice in 10 years as per manufacturer's recommendation)	$500
	Subtotal	**$1,581.86**
Disposal		
Removal from site	Included in installation	$0
Scrap metal value	$20 (subsidises installation)	($20)
	Subtotal	**($20)**
	Whole-of-life cost:	**$3,917.57**

13.2 Drivers of sustainable procurement

CIPS position is that; effective procurement is sustainable procurement that promotes positive outcomes for the economy environment and society. Organisations should promote sustainable procurement throughout the acquisition and disposal process and sustainability should be embedded in all procurement decision making. Beyond ***legislative requirements***, there are many drivers (as referenced in the BS8903: Principles and framework for Procuring Sustainable) that support sustainable procurement, such as:

a) **Financial:** Provides the delivery of operational cost savings through more efficient goods, works and services; challenging demand at source to ensure need; reducing end of life disposal costs; driving efficiency in the supply chain; and developing market capacity, innovation and competitiveness. Sustainable procurement should reduce waste which, in turn, reduces cost.

b) **Risk:** Significant sustainability impacts should be identified and addressed as part of any comprehensive risk management strategy. Identified risks may include, but are not limited to legal risks, financial liabilities, moral/ethical risks, security of supply risks, price volatility risks and risks to reputation. An organization's risk profile will continue to evolve based in part on the rapidly changing environments and the growing public awareness and appetite for sustainable solutions.

c) **Increased stakeholder expectations and awareness:** Generates greater pressure on organizations to consider the environmental, economic and social aspects of business and to implement sustainable initiatives. Organizations should recognize the need to foster stakeholder goodwill and proactively and effectively address expectations and concerns in regard to sustainable procurement.

d) **Organizational policy commitments and targets:** An expression of the culture, values, and vision by which an organization operates. This should be supported by procurement and reflected in procurement policy, strategy objectives, business practice and decision making.

13.3 Benefits of Sustainable Procurement

The benefits of adopting a sustainable procurement approach are numerous. The receiver of the benefits can be the purchaser, the market (or supplier) or the community. Some benefits can apply to all these groups.

Benefits to **the purchaser** can include:

- securing best value for money and achieving a more efficient use of public resources
- generating financial savings through greater energy efficiency; reduced waste disposal (including reduced packaging to waste); reduced water use; and reusing materials and products, thereby lowering the cost of a product over its life cycle
- achieving positive publicity associated with the purchase and use of products, services and suppliers with good environmental and social responsibility records
- providing government leadership to the community in demonstrating social and environmental responsibility through the purchase of sustainable products and services.

Benefits to **the market** can include:

- increasing the availability of sustainable products and services at more cost-effective prices

- expanding the market for sustainable products and services, with potential benefits for local businesses
- expanding market opportunities gained from stronger product and service differentiation
- reducing transport-related costs such as fuel, vehicle maintenance and road congestion
- supporting and encouraging innovation through demonstrating preference for more sustainable products and services
- encouraging industry to develop capacity to operate in a clean, green economy.

Benefits to **the community** can include:

- reducing adverse environmental and social impacts arising from procurement decisions
- reducing waste to landfill, saving water and reducing greenhouse gas emissions
- reducing air and water pollution
- reducing consumption of both natural and processed resources
- promoting health, safety and equality in the community
- influencing purchasing decisions to support issues such recognising equality and diversity;
- increasing employment and skills; and developing local communities and their physical infrastructure
- improving social inclusion and cohesion through creating employment and business opportunities for disadvantaged or marginalized groups.

Social benefits: Being sustainable is also considering the social factors of a good or service. Suppliers can be socially responsible by adopting ethical practices and being compliant with legislative obligations and other actions that benefit society including inclusiveness, equality, diversity, regeneration and integration. Social impacts that can be taken into consideration across sustainable procurement activities include:

- supporting suppliers to government who are socially responsible and adopt ethical practices
- considering human health impacts
- supporting the use of local and emerging small businesses
- supporting socially inclusive practices, such as employment and training focused on disadvantaged groups
- assessing the impact of occupational health and safety concerns (both here and abroad)
- ensuring compliance with relevant regulatory requirements.

13.4 Principles of sustainable procurement management

Value for money is the core principle underpinning procurement. This means that all relevant financial and non-financial costs and benefits should be taken into account over the entire life of the procurement. Sustainability should be considered as part of the value for money assessment.

Other principles of sustainable procurement include:

1. adopting strategies to avoid unnecessary consumption and manage demand
2. minimizing environmental impacts over the life of the goods and services by choosing products or services that have lower adverse impacts associated with any stage in their production, use or disposal
3. fostering innovation in sustainable products and services through the design and implementation of procurements
4. ensuring that fair and ethical sourcing practices are applied and that suppliers are complying with socially responsible practices, including legislative obligations to employees.

The Chartered Institute of Procurement and Supply (CIPS) positions principles of sustainable procurement to include;

1. Resource productivity,
2. Stakeholder involvement and collaboration,
3. Whole life costing,
4. Specific activity focus,
5. Integrating sustainability throughout; and
6. Training.

Resource productivity: Sustainable procurement should emphasize the need for increasing resource productivity. Organisations that take this approach may well make long-term savings due to the reduced quantities of materials they will need to purchase. It may be that such an approach needs an initial outlay, however, and a strong business case will have to be made to the relevant parties within the organisation. Procurement is central to delivering an organisation's corporate commitments on sustainability at an operational level because of the reliance on high levels of purchased goods and services, and so Procurement and Supply Management professionals should take the lead in developing sustainable business solutions.

Stakeholder involvement and collaboration: Procurement and Supply Management professionals can only deliver sustainable procurement with on-going engagement and collaboration with internal stakeholders, budget holders and key suppliers to reach the most effective solutions.

Whole life costing: In order to convince these interest groups, it is necessary to demonstrate a whole life costing approach to procurement, rather than selecting on purchase price alone. To do this it is necessary to consider initial costs (such as design, construction and installation, purchase or leasing, fees and charges) and future operating costs (such as rent, rates, inspection, energy and utilities use, maintenance, repair, disposal, security, replacements/renewals, dismantling and management). Potential losses of revenue should also be considered (when a machine is out of use due to maintenance, for example). Applying a whole-life cost approach provides greater value for money and reduce the need for resources, ensuring greater sustainability.

Specific activity focus: Resource productivity and other aspects of sustainable procurement can also be made more effective with little initial outlay by targeting specific parts of the procurement cycle. Procurement and Supply Management professionals need to focus on demand management (i.e. stimulating the demand, estimating its volume, and planning the production accordingly) and optimizing specifications (i.e. specifying resource efficient products such as products incorporating recycled content) in order to successfully provide the value-for-money benefits of sustainable procurement.

Integrating sustainability throughout: while particular areas of the procurement cycle should be highlighted, optimum business benefits from sustainable procurement are realized by integrating sustainability throughout the procurement decision making process. For example, risks to sustainability (i.e. risk of loss of supply chain, child labour, hazardous materials etc.) should be targeted at an early stage to ensure they can be mitigated as much as possible. Another example is of key performance indicators and targets associated with sustainability which can be written into the contract with the supplier and reviewed at regular intervals to ensure that the supplier is acting sustainably.

Training: In order for Procurement and Supply Management professionals to have sufficient knowledge of sustainability to be able to integrate practices into their procurement, they should be effectively trained. Due to the frequently developing practices in sustainability, Procurement and Supply Management professionals with existing knowledge should ensure that they update and maintain their education in this area, especially in terms of legislation that is relevant to sustainability in its widest sense.

13.5 Elements of Sustainable Procurement Practice

The implementation of sustainable procurement practice is a big challenge to many organisations. Having a successful implementation calls for the integration of elements such as;

a) People and Leadership
b) Documentation of the Drivers for Sustainable Procurement
c) Sustainable Procurement Policy, Strategy and Communications
d) Sustainable Procurement Processes
e) Engagement of Suppliers in Sustainable Procurement
f) Validate Achievement and Measurement Results in Sustainable Procurement

People and Leadership

Procurement should serve as the lead for developing, implementing and maintaining a sustainable procurement policy and program. To accomplish this, it will be necessary to ensure:

- Clear identification of the procurement staff's roles and responsibilities for the program,
- including a Sustainable Procurement Champion, with support and influence at the senior management level
- Appropriate training of the procurement staff in sustainable procurement best practices
- Procurement staff are provided with performance goals and objectives including aspects of sustainable procurement, for which they are held accountable through their personal development evaluations and assessments
- Organization reports are available externally that show the achievements in sustainable
- procurement (i.e. newsletters, annual reports and/or website communications)

Documentation of the Drivers for Sustainable Procurement

Once significant drivers for sustainable procurement activity have been assessed and identified (See: Background), it is advisable to document and describe the drivers in terms of potential benefits to the organization, key stakeholder, or beneficiary. Clear documentation will:

- Effectively develop a clear organizational business case for sustainable procurement
- Assist in the development of policy, strategy, action plans and initiatives, as well as provide a reference point against which actual outcomes can be compared

Sustainable Procurement Policy, Strategy and Communications

There should be clear and agreed upon sustainability objectives embedded within procurement and organization policy, strategies, procedures and process. These objectives should ensure that:

- The organization has identified, and regularly reviews, the sustainability objectives to be achieved through the procurement process
- A sustainable procurement policy is endorsed by the organizational management team, references any legislative policy on sustainability, and has been communicated to suppliers and throughout the organization
- The public procurement organization scrutinizes its sustainable procurement strategy internally and has subjected the strategy to review by one or more external stakeholder groups (i.e. the public, end users, budget/finance)
- The organization regularly reviews its sustainable procurement strategy covering risks and supplier engagement
- The organization's sustainable procurement strategy aligns with the agency's strategic plan

Sustainable Procurement Processes

Processes should be developed and adopted to ensure sustainability is considered in the procurement of products and services. These processes include, but are not limited to:

- Identification of a high-level expenditure analysis of the organization's spend profile (See: *Spend Analysis Practice*)
- Measurement and mitigation of the key sustainability impacts/risks of each procurement category
- Ensuring that key contracts have incorporated sustainability criteria; these are decided while the bid is being developed and carried through into specific objectives in the contract (i.e. specifying resource efficient products such as energy efficient appliances, and products that incorporate recycled content).
- Identification and reduction of supply chain sustainability risks (i.e. risk of supply loss, child labor, hazardous materials, etc.) at an early stage in the procurement process

Engagement of Suppliers in Sustainable Procurement

Engaging suppliers in sustainable procurement objectives will result in targets being set for suppliers that will improve their sustainability performance in relation to their provision of products and/or services to the organization. Targets should be achieved by:

- Ensuring that key performance indicators and targets associated with sustainability performance/impact have been shared and agreed upon with suppliers
- Identifying suppliers with negative sustainability performance/impacts through a review and analysis of established indicators (e.g. reduction of waste to landfill by x% per annum), and encouraging identified suppliers to work in partnership with the organization to improve sustainability performance/ impacts.

Validate Achievement and Measurement Results in Sustainable Procurement

Identify and implement performance management improvements that will have a positive impact on sustainable procurement procedures. The improvements can be substantiated by ensuring that:

- The organization has identified its key sustainability impacts and developed a process for managing these through procurement,
- The organization has identified a peer group or program for benchmarking its sustainable procurement performance against other organizations
- The organization has identified management actions to improve practices relating to sustainable procurement.

……. END …….