

# **Productivity Commission Inquiry into Government Procurement**

## **Department for Industry and Skills**

### **Introduction**

Over the next 10 years, South Australia's industrial future will be shaped by local, national and global trends, including the rise of:

- the 'fourth industrial revolution' where goods and services will be increasingly connected with unprecedented processing power
- higher levels automation of both goods and services, and
- digital connectivity and global engagement as more services become mobile.

The South Australian economy has also been transforming, with manufacturing having been the largest provider of Gross State Product in 2006-07, but now services like health care and social assistance have taken this position.

South Australia has also seen a reduction in the number of medium sized business (20-199 employees) and large businesses (200+ employees).

In the ten years to 2016-17, South Australia's goods and services exports have grown by 33% from \$11 billion to \$14.7 billion, with services again being a significant contributor to this growth.

The openness of the South Australian economy is crucial to businesses expanding, including into new markets. More than 2500 businesses export, with Asian markets being the largest source of trade expansion. China has overtaken the United States as the biggest export market.

### **The role of Government - new approaches to procurement are needed**

Governments globally are increasingly recognising the importance of their role in industry development as a regulator, a purchaser of goods and services, a collector and holder of data, a service and information provider, as well as a facilitator and advocate.

To drive industry development, procurement platforms need to be more open to innovative tendering and variant bids – such as is often seen with major projects that include effective levers to tie in local industry development and social procurement. Such procurements are markedly different from the more transactional procurements designed to drive efficiencies.

In South Australia, the need has never been more important to ensure greater value for money and efficiencies, without impeding the quality of public service provision. Improved public procurement practices could result in substantial savings to taxpayers, while at the same time stimulating industry development. Government has the capacity to demand the production of innovative products and services to deliver more efficient and effective products and services.

The potential for innovation lies in better quality preparation well ahead of a planned procurement. True value for money and cost savings can be gained by routinely seeking out new solutions to public sector needs. By using clear and robust output specifications, purchasers can give firms the space to propose innovative solutions. By Government acting as intelligent customers and being more open to new approaches, it can stimulate the market for innovative products and services and encourage the growth of innovative and dynamic businesses.

### **Innovation and commercialisation in South Australia - issues for further consideration by the Commission**

Fostering other Government objectives such as innovation and sustainable development through procurement has gained momentum across Europe in recent years. While enterprises and individuals are the primary sources of innovation, it is widely recognised that public policy can enhance the framework conditions for effective innovation. The EU Reports "Public Procurement for Research and Innovation" (Sept 2005), "Creating an Innovative Europe" (Jan 2006) call on governments to "use public procurement to drive demand for innovative goods, while at the same time improving the level of public services". These reports and stakeholder consultations conclude that the crucial issue is not whether procurement for innovation gain is feasible but how to make it happen.

In the United States, the Small Business Innovation Research (SBIR) program is a highly competitive program that encourages domestic small businesses to engage in Federal Research/Research and Development (R/R&D) that has the potential for commercialisation. Through a competitive awards-based program, SBIR enables small businesses to explore their technological potential and provides the incentive to profit from its commercialisation. By including qualified small businesses in the nation's R&D arena, high-tech innovation is stimulated and the US gains entrepreneurial spirit as it meets its specific research and development needs (SBIR website).

In 2000, the United Kingdom launched the Small Business Research Initiative (SBRI) to encourage the allocation of R&D expenditures to small firms. Originally a voluntary guideline, since the 2005 Budget the SBRI has mandated that every British Government department contract a minimum of 2.5 per cent of external R&D from small businesses. In 2006, the government also launched the supply2gov website which targets small businesses by advertising lower-value public sector procurement opportunities (NESTA 2007). The UK's 2017 Industrial Strategy renews the government's commitment to SBRI, including a refocus to increase impact for innovative businesses, building capability in the public sector, and introducing a new £20 million stream, 'GovTech Catalyst', that supports tech firms to provide the government with innovative solutions for more efficient public services.

The UK's SBRI bears little more than superficial resemblance to its successful US counterpart. In particular, although the two share similar targets of 2.5 per cent of external R&D being sourced from small businesses, in the US this figure is viewed only as a starting point (NESTA 2007).

South Australia could adopt a similar approach to the US model and introduce a flexible, phased structure and strong programme management processes to

enable broader cultural change within government. Furthermore, it must recognise that a mandatory minimum target should represent only the beginning of greater engagement with small innovative firms.

The ability to test and trial an innovative product or service needs to be improved in South Australian procurement. This is not well covered in South Australia compared to other similar jurisdictions. The New South Wales Procurement Innovation Stream and Queensland ICT SME Participation scheme policy need further investigation by the Productivity Commission but appear appropriate. Both policies allow for direct negotiation on test and trial basis, for an order up to \$500,000 (QLD) or \$1,000,000 (NSW).

An approach to generating the commercialisation of genuinely innovative products and services from South Australian procurement activity, requires that agencies concentrate some of their procurement activity on such opportunities. That is, locating new products and services. Whether agencies are capable of this, is a matter for further consideration. Deloitte Access Economics describes this as follows: *“Raising the standards of procurement activity to lift the economic contribution of procurement activity in South Australia must be seen as a joint project with increasing the SA Government’s procurement efficiency and effectiveness. ... To assist these goals, it is recommended that the State Government consider the implementation of complementing procurement strategies; this could potentially include procurement centres of excellence where a strong body of knowledge and experience can be developed, focusing on thematic industries.”*<sup>1</sup>

An authorisation environment which is accommodative of innovative approaches and objectives in procurement is also required. Changes to allow for testing and trialing novel or innovative approaches is required, especially in the lower value end of procurement, where tests and trials are most likely to occur.

The department also endorses the findings of the Harper Review that outcome-based procurement can assist to drive innovation and encourage new and innovative methods for achieving a government’s desired result.

A role for SME procurement is supported in principle. However, the UK Crown Commercial Service model, makes coordination of SME focused procurement simpler. It could be adopted together with a broader centralisation of procurement advice. The Deloitte findings are also relevant here regarding the levels of procurement capability across government.

### **Red tape in procurement**

The changes in procurement rules, governance and documentation made by the State Procurement Board in 2016 were a significant step forward. This included the increase in the simple procurement threshold and the setting of default limitations of liability and lowering of insurance requirements.

In 2017 the Department of State Development in conjunction with the Simpler Regulation Unit (SRU) in the Department of Treasury and Finance (DTF), held

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<sup>1</sup> Deloitte Access Economics 2014, “Economic contribution analysis of State Government procurement”, report for Office of the Industry Advocate.

meetings with 53 industry associations to gain an understanding of the services that industry associations offered to members, the opportunities and challenges members face in running their businesses, and how the South Australian Government can work with industry associations to support their members. 252 issues were captured from associations including examples of red tape and compliance that impacted on their ability to supply to government. Some of these issues have since been addressed. Topics included contract conditions including unlimited liability requirements, complex clauses not understood by businesses, duplication of information provision in the tender process, lack of government and industry communication on key issues, time that it takes to get a response from government, access to skills required for future work, procurement done in large contracts that are not manageable for smaller South Australian businesses, high level of paperwork required to comply with work health and safety laws.

For potential further, red tape reductions, notably, Business SA has provided a well-reasoned argument for more pre-qualification, such that, tender information doesn't need constant repeating because the business has already met key benchmarks.