



Draft Report

Inquiry into Government Procurement Stage 2

30 August 2019

© Government of South Australia. Published 2019. All rights reserved.

No part of this publication may be reproduced by any process except in accordance with the provisions of the *Copyright Act 1968* (Cth), without prior written permission from the South Australian Productivity Commission.

Disclaimer

The views expressed herein are those of the South Australian Productivity Commission and do not purport to represent the position of the Government of South Australia. The content of this draft report is provided for information purposes only. Neither the South Australian Productivity Commission nor the Government of South Australia accepts any liability to any person for the information (or the use of such information) which is provided in this draft report or incorporated into it by reference. The information in this draft report is provided on the basis that all persons having access to this draft report undertake responsibility for assessing the relevance and accuracy of its content.

South Australian Productivity Commission
GPO Box 2343
Adelaide South Australia 5001
AUSTRALIA

Telephone: 08 8226 7828
Email: sapc@sa.gov.au
Website: www.sapc.sa.gov.au

An appropriate citation for this publication is:

South Australian Productivity Commission 2019, *Inquiry into Government Procurement Stage 2*, Draft report, August 2019

About the South Australian Productivity Commission

The Commission provides the South Australian Government with independent advice on facilitating productivity growth, unlocking new economic opportunities, supporting job creation and removing existing regulatory barriers.

The Department of the Premier and Cabinet (DPC) Circular PC046 sets out the objectives and functions of the Commission; how inquiries are referred to the Commission, undertaken and reported on; and how the Commission and public sector agencies work together.

The Commission was established to assist the government:

- i. to improve the rate of economic growth and the productivity of the South Australian economy in order to achieve higher living standards for South Australians;
- ii. to improve the accessibility, efficiency and quality of services delivered or funded by government;
- iii. to improve South Australia's competitiveness for private sector investment;
- iv. to reduce the cost of regulation;
- v. to facilitate structural economic changes while minimising the social and economic hardship that may result from those changes;
- vi. to take into account the interests of industries, employees, consumers and the community;
- vii. to increase employment;
- viii. to promote regional development; and
- ix. to develop South Australia in a way that is ecologically sustainable.

The Commission is supported by the Office of the South Australian Productivity Commission (OSAPC) which is an attached office of the Department of the Premier and Cabinet. The Chair of the Commission also serves as the Chief Executive of the OSAPC.

For more information on the Commission, including DPC Circular PC046, visit the website at www.sapc.sa.gov.au.

Disclosure

The Commissioners have declared to the South Australian Government all personal interests that could have a bearing on current and future work. The Commissioners confirm their belief that they have no personal conflicts in regard to this inquiry.

Terms of Reference

SOUTH AUSTRALIAN PRODUCTIVITY COMMISSION INQUIRY INTO GOVERNMENT PROCUREMENT – CAPITAL PROJECTS AND PRESCRIBED PUBLIC AUTHORITIES

I, Steven Marshall, Premier, hereby request that the South Australian Productivity Commission (the Commission) expand the scope of its current inquiry into the efficiency and effectiveness of South Australian Government procurement processes and practices to include capital project procurement and all public authorities including those currently exempt from the *State Procurement Act 2004*.

The Commission's deliberations on the additions to the scope are to be presented to the Government in a separate report.

Background

The South Australian Government's 'Strong Plan for Real Change', documents its election commitment to implement reforms enabling South Australian businesses to better participate in government procurement.

The State's public authorities manage and perform their procurement functions via a mix of centralised and decentralised arrangements depending on their organisational structure and functions. Whilst subject to some exclusions, they are required to comply with the State Procurement Board's (SPB) Procurement Policy Framework and the Department for Industry and Skills' Industry Participation Policy (IPP), local interpretation and application of these governing frameworks, may lead to inconsistent implementation of policy and operational guidelines.

The general government sector capital investment program reflects continued significant investment by the government in delivery of its services. Purchases of non-financial assets are expected to be \$2.0 billion in 2018–19. The forward estimates contain a major infrastructure investment program of \$8.3 billion in the general government sector over four years. As a result of feedback received from the business sector during the current Commission inquiry into procurement, the government has decided that the scope of the inquiry be expanded to include capital projects, as it represents a significant portion of government procurement expenditure and there are opportunities to improve procurement processes.

The state's prescribed public authorities collectively are responsible for a significant amount of procurement in the course of delivering functions on behalf of the South Australian Government, including capital procurement that is not included in the figures above. Procurement by prescribed public authorities, as listed in Schedule 1 of the State Procurement Regulations 2005, is also now in the scope of this inquiry.

Terms of Reference

This inquiry is an expansion of the scope of the current inquiry into goods and services procurement.

As a result, the Commission should address the following terms of reference in a second stage of the procurement inquiry that covers capital procurement and all procurement by prescribed public authorities:

1. Consider the time and costs associated with procurement, that is:
 - a. The time taken to complete the supplier selection stage of the procurement process;
 - b. The cost to business of participating in the procurement process; and
 - c. How the time and costs of the procurement process in South Australia compare to other jurisdictions.
2. Assess the level of compliance by public authorities and other declared bodies with government procurement policies, guidelines, principles, standards and directions.
3. Consider the appropriateness of procurement governance and reporting arrangements. This includes procurement under a Public Private Partnership arrangement.
4. Evaluate the effectiveness of the IPP, in particular, the IPP's impact on:
 - a. Competition between firms, including those from interstate and overseas;
 - b. Prices and value for money of goods and services procured over time; and
 - c. Broader economic effects such as the growth of local industry and employment.
5. Examine the risk management framework used by public authorities to evaluate supplier bids and specifically whether it is appropriate to the value of the procurement.
6. Consider examples of contemporary procurement policies and practices from interstate, overseas and the private sector and their effectiveness in:
 - a. Generating local output and employment;
 - b. Building industry capacity; and
 - c. Promoting innovation.
7. Provide recommendations on action the government should take to improve the effectiveness and efficiency of State Government policies and practices for the government's procurement activities.

Scope

The Inquiry now includes government procurement for capital projects in addition to the procurement of goods and services.

All public authorities subject to the State Procurement Act 2004 continue to be in scope. Applicable prescribed public authorities, as listed in Schedule 1 of the State Procurement Regulations 2005 (attached), are also now in scope.

The Commission should have regard to relevant state and federal legislation, South Australia's national and international obligations about procurement and the South Australian Government's election commitments.

Process

The Commission should consult with a cross section of businesses operating in South Australia, the Small Business Commissioner, Industry Advocate, State Procurement Board, key

business associations and industry representation (including unions), as part of the public engagement process. Engagement should also occur with the Public Works Committee of Parliament.

The Commission is to provide a separate report to the government on the first stage of this inquiry dealing with goods and services procurement, with a draft report due by 15 March 2019 and a final report by 17 May 2019.

The Commission is to provide a second report on capital procurement and procurement by prescribed public authorities, with a draft report to be provided during August 2019 and final report by 31 October 2019.



Hon Steven Marshall MP
PREMIER OF SOUTH AUSTRALIA

31/1/2019

Attachment:

- Schedule 1 - State Procurement Regulations 2005

Schedule 1—Prescribed public authorities

Adelaide Venue Management Corporation
Architectural Practice Board of South Australia
Construction Industry Training Board
Health Services Charitable Gifts Board
Legal Profession Conduct Commissioner
Local Government Finance Authority of South Australia
Motor Accident Commission
Return to Work Corporation of South Australia
South Australian Forestry Corporation
South Australian Housing Trust
South Australian Water Corporation
Superannuation Funds Management Corporation of South Australia
Urban Renewal Authority

Preface

The release of this draft report gives interested participants the opportunity to comment on the Commission's analysis in relation to its inquiry into South Australian Government procurement.

In preparing this draft report, the Commission invited public submissions and consulted widely with a range of individuals, businesses, organisations and government agencies.

The Commission invites further written submissions on the draft report by 20 September 2019. These submissions may address any of the issues covered by the terms of reference. Following the release of the draft report, the Commission will hold further consultations as necessary including after 20 September 2019.

At the conclusion of consultation on the draft report, the Commission will prepare a final report to be presented to the Government of South Australia by 31 October 2019.

With respect to the publication of the final report, the Department of the Premier and Cabinet (DPC) Circular PC046 states that:

- 'the Commission must ensure the final report is available on its website ... within 90 days of delivering the report to the [Premier]' and
- 'the [Premier] will endeavour to respond ... within 90 days of receiving the report'.

We would like to thank all those who provided input to this inquiry, which includes a wide range of businesses, not-for-profit organisations and their associations, as well as acknowledge the assistance and cooperation from the State Procurement Board, government departments, the Industry Advocate and the Small Business Commissioner.

In addition, we would like to acknowledge and thank the OSAPC staff for their work in researching and preparing this draft report.

The Commission looks forward to receiving feedback on the draft report.

Dr Matthew Butlin
CHAIR AND CHIEF EXECUTIVE
25 March 2019

Adrian Tembel
COMMISSIONER

Contents

About the South Australian Productivity Commission	3
Terms of Reference.....	4
Preface	8
Contents	9
Key messages.....	15
Executive summary	16
1. The scope of the inquiry	16
2. Unlocking value: the overview.....	17
3. South Australian Government procurement spending	18
4. The issues	19
5. A better system architecture	19
6. Prescribed authorities.....	21
7. Construction.....	22
8. SA Industry Participation Policy (SAIPP) for construction and prescribed authorities....	26
9. Other procurement issues.....	27
10. Conclusion.....	28
Draft recommendations	29
Draft recommendation 2.1.....	29
Draft recommendation 3.1 (supplementary to Stage 1 recommendation 2.9)	29
Draft recommendation 3.2.....	29
Draft recommendation 3.3.....	29
Draft recommendation 4.1.....	30
Draft recommendation 4.2.....	30
Draft recommendation 4.3.....	30
Information request	31
Information request 5.1	31
Definitions.....	32
Acronyms	36
1. Introduction.....	40
1.1 Context	40
1.2 Terms of reference.....	41
1.3 The Commission’s approach	44

1.4 The current South Australian procurement system	45
1.5 Stakeholder feedback	46
1.5.1 External stakeholder feedback	46
1.5.2 Prescribed public authorities	47
1.5.3 Public authorities	47
1.5.3.1 Non-DPTI public authorities.....	47
1.5.3.2 DPTI	48
1.6 Structure of the draft report.....	49
2. Prescribed public authorities.....	50
2.1 What is a prescribed public authority?.....	50
2.1.1 The legal and policy framework.....	50
2.1.2 Historical basis for prescription	52
2.2 Who are they and what do they do?	53
2.2.1 Characteristics of prescribed public authorities	53
2.3 Prescribed public authorities: purpose, governance and procurement activity	54
2.3.1 Commerciality	54
2.3.1.1 The Commission’s view	56
2.3.2 Risk	56
2.3.2.1 The Commission’s view	57
2.3.3 Governance and audit.....	58
2.3.3.1 The Commission’s view	59
2.3.4 Capability	60
2.3.4.1 Policy	60
2.3.4.2 People	61
2.3.4.3 Systems and technology	62
2.3.5 Procurement activity.....	63
2.3.5.1 Type.....	63
2.3.5.2 Size of spend	65
2.3.5.3 Continuous improvement.....	68
2.4 Prescribed public authorities: preferences and priorities.....	69
2.4.1 Organisational responsiveness	69
2.4.2 Alignment with SPB policy and process	69
2.4.3 Use of whole-of-government contracts.....	70
2.4.4 Limited procurement requirements	70

2.4.5 Existing oversight is appropriate.....	70
2.5 Review of prescribed public authorities, 2018	71
2.6 The value of prescribed status.....	72
2.7 Proposed reform	73
2.7.1 Step 1: PPAs form part of state procurement reporting arrangements.....	73
2.7.2 Step 2: State-wide system reforms – PPA contribution.....	74
2.7.3 Step 3: Transitioning	74
2.7.4 Stage 4: A single system.....	75
3. Construction	76
3.1 Background	76
3.1.1 What is ‘construction’ for the purposes of this procurement inquiry?	76
3.1.2 Value and volume of contracts and spend	77
3.1.2.1 Construction procurement spend.....	77
3.1.2.2 Contract value and volume	77
3.1.2.3 Commission data.....	78
3.1.2.4 Results.....	78
3.1.3 Governance arrangements: how is the spend managed?	79
3.1.3.1 Regulatory environment for construction procurement.....	79
3.2 Construction issues	87
3.2.1 Value for money.....	87
3.2.1.1 Stage 1 findings and conclusions on value for money.....	89
3.2.1.2 Strategic planning for value	90
3.2.1.3 Factors of value for money in construction	95
3.2.1.4 Evaluating for value for money outcomes.....	104
3.2.1.5 Measuring the achievement of value	107
3.2.1.6 Commission’s working conclusions and recommendations	109
3.2.2 Risk management.....	109
3.2.2.1 Background	109
3.2.2.2 Approach taken.....	110
3.2.2.3 Stakeholder feedback	115
3.2.2.4 Findings.....	115
3.2.2.5 Working conclusions and draft recommendations.....	117
3.2.3 Contract management	118
3.2.3.1 Introduction	118

3.2.3.2 Approach taken.....	118
3.2.3.3 Stakeholder feedback	119
3.2.3.4 Findings.....	122
3.2.3.5 Working conclusions and recommendation.....	125
3.2.4 Capability	125
3.2.4.1 Introduction	125
3.2.4.2 What the Commission heard	129
3.2.4.3 Commission’s view.....	130
3.2.4.4 Current procurement construction capability frameworks.....	133
3.2.4.5 Developing a construction procurement capability strategy	138
3.2.5 Engagement with suppliers.....	141
3.2.5.1 Market engagement	141
3.2.5.2 What the Commission heard	142
3.2.5.3 Observations from the data on market approach	146
3.2.6 Streamlining the procurement process	150
3.2.6.1 Introduction	150
3.2.6.2 Agencies’ role in the construction process.....	150
3.2.6.3 Roles in the construction project implementation process.....	154
3.2.6.4 Stakeholder feedback	155
3.2.6.5 Findings	156
3.2.6.6 Conclusions and draft recommendation	163
3.3 End piece	167
4. Other procurement issues	171
4.1 Metrics, reporting and performance	171
4.1.1 Agency information.....	171
4.1.2 Findings	172
4.1.2.1 Procurement activity measures	172
4.1.2.2 Capability measures.....	174
4.1.2.3 Continuous improvement.....	174
4.1.2.4 Outcome measures.....	175
4.1.3 Working conclusions and draft recommendations.....	176
4.1.3.1 Reporting	176
4.1.3.2 Measurement.....	177
4.2 Innovation.....	187

4.2.1 Introduction	187
4.2.1.1 South Australian procurement system design for promoting innovation	188
4.2.2 Findings	191
4.2.2.1 Innovation in procurement and intellectual property policy design	191
4.2.2.2 The use of public policy instruments to support innovation by suppliers.....	193
4.2.3 The Commission’s view	195
4.2.3.1 South Australia’s innovation policy	195
4.2.3.2 Intellectual property guidance material	198
5. SA Industry Participation Policy for construction and prescribed public authorities.....	199
5.1 Overview and application of the SAIPP to construction projects.....	199
5.2 Evidence of the impact of the SAIPP	202
5.2.1 From submissions received by the Commission	202
5.2.1.1 Impact on the selection of suppliers.....	205
5.2.1.2 Impact on local participation and competition	205
5.2.2 From the random sample of 106 tenders.....	209
5.2.2.1 Method	210
5.2.2.2 Results.....	211
5.3 Issues raised regarding the SAIPP	214
5.3.1 Scoring.....	214
5.3.2 Weighting and thresholds.....	215
5.3.2.1 Impact of tender evaluation formulas on the actual weighting of ECT/IP Plans scores.....	216
5.3.3 Compliance	216
5.3.3.1 Participants’ views	216
5.3.3.2 SAPC’s views.....	216
5.3.4 Administrative cost	217
5.3.5 Delays.....	217
5.4. How to include broader impact (regional considerations, innovation, productivity, competition).....	217
5.4.1 Participants’ views	217
5.4.1.1 More focus on disadvantaged groups	217
5.4.1.2 More focus on training of local suppliers	217
5.4.1.3 More focus on consultancy services.....	217
5.4.1.4 More focus on graduates.....	218
5.4.1.5 Higher impact in large tender	218
5.5. Summary and conclusions.....	218

6. A better system architecture	220
6.1 The current architecture	220
6.2 Principles for better system architecture.....	224
6.2.1.1 Optimising value	224
6.2.1.2 Simplicity.....	226
6.2.1.3 Appropriately devolved accountability.....	226
6.2.1.4 Clear authority	227
6.2.1.5 Capability	227
6.3 Three discussion options.....	227
6.3.1 Option A: Optimising within current arrangements	228
6.3.2 Option B: A strengthened SPB underpinned by a whole-of-government SP Act	228
6.3.3 Option C: Create Procurement SA and repeal the SP Act.....	229
6.4 Incorporating construction and goods and services	231
6.5 Implementation and other issues.....	232
Appendices.....	233
Appendix 1: List of submissions for the Government Procurement Inquiry Stage 1 issues paper.....	233
Appendix 2: List of submissions for the Government Procurement Inquiry Stage 1 draft report.....	235
Appendix 3: List of submissions for the Government Procurement Inquiry Stage 2 issues paper.....	236

Key messages

This draft report addresses Stage 2 of the Commission's inquiry into the effectiveness and efficiency of State government policies and practices for government procurement.

South Australia currently has three separate procurement streams: for goods and services; for construction; and public authorities that are exempted by regulations under the *State Procurement Act 2004*. While these streams are reasonably managed – in some cases very well managed – given their systems, data and capability limitations, the State can do better.

The Commission considers overall the procurement system leaks value at all stages such as:

- managing the procurement spend strategically;
- developing the right definition of the procurement requirement;
- utilising the right approach to market; and
- managing contracts.

It is impractical to control everything from the centre of government. To ensure the goods, services and construction procured are delivered in full and at the right price and value, the procurement system must strike a balance between being directed, analysed and energised centrally, and having the accountability, authority and professional capacity in the agencies.

Currently the system is fragmented, unproductively prescriptive, cannot assess overall performance and does not focus on developing capability in the SA Government procurement professionals. The leakage of value is significant: the typical 5 per cent annual improvement could deliver this state \$500 million per annum.

In the Commission's view, there is an opportunity to drive long-term value in SA government procurement, built on:

- growing and maintaining a highly capable procurement profession as a foundation for ultimately replacing the current regime of rules-based compliance with greater application of discretion and professional judgement;
- strengthening capability in line agencies while abolishing barriers to whole of government procurement activities; and
- transforming the central government's capacity to unlock direct and indirect value for the State through high level strategic techniques, methods and actions.

The Commission outlines three options for further discussion. It favours fundamental change: abolishing the current fragmented arrangements; replacing the State Procurement Board with Procurement SA covering all procurement, led by a qualified CE; who would report to a Minister with scope to implement targeted or whole of government procurement policies and initiatives; and driving the shift from the current rules-based, compliance-heavy procurement culture to a more professional judgement based model. The Commission also proposes phasing in the change to focus on priority areas and manage implementation risks.

The Draft Report also addresses prescribed public authorities, construction procurement and South Australia's Industry Participation Policy. The final report is due 31 October 2019.

Executive summary

1. The scope of the inquiry

In October 2018, the SA Government tasked the Productivity Commission (the Commission) to:

- evaluate the effectiveness and efficiency of State Government policies and practices for the procurement of goods and services; and
- identify options to improve procurement practices and their impacts on local industry, noting concerns expressed by small and medium enterprises (SMEs) about the cost of and time expended in tendering for procurement opportunities.

Initially, the inquiry focused on agencies and matters that fell within the scope of the *State Procurement Act 2004*, which specifically excluded construction expenditure and prescribed public authorities (e.g. SA Water and Renewal SA). On 15 February 2019, the government expanded the scope of the inquiry to cover these exclusions.

Accordingly, the overall inquiry was divided into two stages. Stage 1 addressed the inquiry's original terms of reference. The final report for Stage 1 was delivered to the Premier on 17 May 2019. The Government's response has been released (<https://dpc.sa.gov.au/resources-and-publications/government-procurement-inquiry>): 28 of the Commission's 30 recommendations were accepted in full; and the others were accepted in part. In summary, the recommendations aimed at unlocking short-term value in government procurement while starting some key long-term reforms. The recommendations called for:

- a strategic plan to raise the capability of the South Australian Government's procurement professionals;
- reforming the reporting requirements for government authorities to central procurement to provide the metrics for understanding and analysing whole-of-government procurement;
- streamlining procurement, including adopting the principle that generally procurement decisions should only be authorised once;
- actions to improve contract management, increase knowledge of the marketplace and provide clearer guidance in key areas such as achieving value.

In addition to the extended scope, Stage 2 considers some matters that were deferred to Stage 2 because they required a whole-of-government view of procurement. These matters were largely governance and institutional arrangements. The final report for Stage 2 is due on 31 October 2019.

This draft report sets out the Commission's preliminary views, some of which are in an early point of development for various reasons that are explained in the document. The Commission looks forward to further consultations with stakeholders and interested parties on the Commission's work to date, including its analyses, conclusions, information requests and draft recommendations.

This is very much a draft. The Commission found that some of the process of collecting key information and evidence from those areas not governed by the *State Procurement Act 2004* took significantly longer than expected despite significant efforts by agencies, particularly from DPTI (which plays a central role in construction). These difficulties strongly suggest there are serious issues in recording and accessing information in DPTI and other agencies. As a result, progress to this point is uneven, remaining preliminary on some issues. This will be addressed in the coming weeks.

Notwithstanding the delays in receiving some information, the Commission appreciates all the assistance received from all participants (both private and public sector). In particular, during this stage, both DPTI and SA Water allocated key personnel to work with the Commission on a part-time basis to assist with the research.

2. Unlocking value: the overview

The inquiry process to date (including the SA Government's acceptance of the recommendations from Stage 1) has persuaded the Commission there is a real opportunity to unlock significant long-term value in SA Government procurement activities. In essence, the opportunity is built on:

- a sustained commitment to developing a highly capable procurement profession within the SA Government based on professional standards, training and development and improvement that is the foundation for moving from the current model of rules-based compliance to one where the exercise of professional judgement plays a much larger role;
- strengthening the capability in line agencies to undertake the procurement required by their agency;
- breaking down barriers, including silos within and between agencies, to leveraging whole-of-government procurement activities;
- very significantly increasing the central capacity to unlock direct and indirect value for the state from its procurement spending through: high-level strategic techniques, methods and actions, together with building – with energy, focus and as a strategic priority – professional capability in the state's procurement professionals.
- more specifically, the Commission is inclined at this point to recommend abolishing the currently fragmented approach including removing the State Procurement Board and establishing a new body, Procurement SA, led by an appropriately qualified CE. The Commission is further inclined to propose that the Procurement SA CE report directly to a designated minister with:
 - the scope and authority to implement targeted or whole-of-government procurement policies and initiatives;
 - the role of catalysing the transformation of the current rules-based, compliance-heavy procurement culture to a more professional judgement discretion model with a strong secondary purpose of value creation; and
 - the authority to recommend intervention by the minister.

While the Commission is unable to quantify the net benefits to the state of the proposed changes, it considers there are good reasons for believing they are likely to be substantial. Moreover, the reforms can be staged in a way that would both optimise net benefits and costs and better manage the implementation risks.

The draft report is structured around five elements:

- a better system architecture to drive value from whole-of-government procurement (this is discussed in Chapter 6 but the Commission considers it the central point of the report);
- procurement in **prescribed public authorities**, including underpinning legislation, architecture of roles and accountabilities, policies, and delegations;
- procurement for **construction expenditure**, including underpinning legislation, architecture of roles and accountabilities, policies, and delegations;
- Other whole-of-government procurement issues; and
- the performance of the South Australian **Industry Participation Policy** (SAIPP) in the procurement system;

3. South Australian Government procurement spending

South Australian Government procurement spending has a substantial impact on the South Australian economy, amounting to more than \$11 billion annually or around 10 per cent of the gross state product (June 2018). These purchases are extremely important to the South Australian economy, underpinning the provision of critical public services and having a significant impact on employment, business activity and investment.

The Commission has considered several of its draft recommendations through the prism of changes that strengthen competitiveness of local businesses, including SMEs, and avoid increasing industry protection.

The Commission's evidence base includes:

- 67 (total for both inquiries) written submissions in response to the issues papers and the Stage 1 draft report, all of which are published on the Commission's website;
- engagement with individuals from industry associations, businesses, not-for-profit organisations and government agencies;
- recent surveys by Business SA, the Office of the Industry Advocate and the SA Tenders website;
- a sample gathered by the Commission of the outcomes of 103 randomly selected recent procurements from public authorities in Stage 1 and a random sample of 106 recent procurements for the expenditure covered in the Stage 2;
- responses from agencies to the Commission's information requests;
- a compilation of trends, developments and reforms in Australian and selected overseas jurisdictions.

Analysis of this evidence base and discussions with stakeholders identified the key issues and concerns that the Commission considers should be addressed.

4. The issues

The issues identified in Stage 1 and 2 of the inquiry were similar. The shared issues were:

- lack of transparency by agencies;
- lack of engagement by agencies;
- risk aversion by decision makers;
- red tape costs;
- lack of or limited capability;
- barriers to innovation in the procurement system;
- the meaning in practice of value for money; and
- contract management shortcomings.

Government agencies also advised the issues identified by businesses in addition to their own concerns and improvement opportunities. Their advice set some business concerns in a wider context, particularly about some processes and practices required by SA's procurement system.

In the Commission's view, these matters point to opportunities to improve the overall value captured by the state from procurement expenditure. The draft recommendations and information requests in the Stage 2 draft report will focus on options to optimise the overall architecture of the state's procurement system.

5. A better system architecture

The Commission acknowledges some areas of very good procurement practice within government that are marked by a strategic use of the procurement function, sufficient resources of qualified professionals, effective monitoring of contracts, organisation around market segments and a clear expectation of the financial savings to be achieved (in addition to meeting non-economic objectives).

That said, and having now considered construction procurement and prescribed public authorities, the Commission considers the existing whole-of-government architecture – the combination of system design and organisation roles – to be inadequate. The Commission's concerns include that the state's procurement function is fragmented into several streams that have limited relationship with each other, lacks a consistent set of principles, pays insufficient attention to human capability, and has a framework of strict thresholds that have not been recently reviewed or challenged.

Moreover, at a whole-of-government level, the current architecture does not allow a focus on whole-of-system benefits, suffers from poor availability of data and has limited capability to manage procurement strategically.

In summary, the current system unnecessarily leaks value, notwithstanding pockets of generally good practice.

Consequently, the Commission sees a real opportunity to unlock long-term value by improving the system architecture to focus and energise efforts across the state's procurement areas to maximise the value of procurement spending and implement evidence and data-based strategic improvements to the state's procurement system.

A key need, in the Commission's view, is a stronger central procurement body to drive whole-of-government procurement based on five foundational elements:

- sufficient seniority, accountability and authority for the function to shape and implement reforms;
- whole-of-government performance monitoring and data analytics;
- the capability to undertake strategic analysis, and exercise professional judgement in identifying and pursuing whole-of-government improvement initiatives that break down silos and reinforce a state-first interest in all procurement activities;
- the capacity to assist agencies for whom procurement may not be a mainstream part of their role; and
- capability development for the government's procurement professional cadre.

This would build on the current accountability framework for chief executives in respect of procurement in government agencies, which would need some strengthening.

A move in this direction is consistent with other states which have focused on improving data collection, developing analytic tools for analysing procurement data, and developing capability frameworks for procurement functions and personnel. The primary aim is to extract the maximum value for the total procurement spend.

The Commission notes there are several important considerations in identifying options for a more fit-for-purpose central procurement body. It proposes five principles at this point:

- optimising value;
- simplicity;
- appropriately devolved accountability;
- clear authority; and
- capability.

Three options for a stronger system architecture

The Commission sets out for discussion three options to increase the value generated by the state's procurement spend. They are:

- **Option A: optimising existing architecture** without changing the legislation and the role of the State Procurement Board.

- **Option B: a strengthened State Procurement Board underpinned by an amended *State Procurement Act*** with legislative underpinning for a centralised, comprehensive role for the SPB. The changes would incorporate the five foundations set out in Section 6.1.
- **Option C: Procurement SA**, a new body to replace the SPB, with a strong mandate for a centralised, comprehensive role. The changes would incorporate the five foundations set out in Section 6.1.

There are several elements in each option that will require additional investment to capture the potential value associated with better management of the procurement spend. All three options require a yet unquantified investment in people and technology.

At this point, the Commission sees the greatest advantage in Option C; however, the options are put forward for discussion so that the Commission can provide the best advice to the government in its final report. It intends to develop them further (or identify superior alternatives) in the coming weeks.

As part of the report, we have considered the procurement arrangements for the different elements of the additional scope of the Stage 2 report. The issues discussed in each chapter are summarised in the following sections. The Commission has also reviewed the impact of the SAIPP on construction and prescribed authorities.

6. Prescribed authorities

The *State Procurement Act 2004* (SP Act) defines a prescribed public authority (PPA) as 'a person or body that has been declared by the regulations to be a prescribed public authority for the purposes of this Act'.¹ The *State Procurement Regulations 2005* (SP Regs) set out the bodies declared to be PPAs in Schedule 1.²

By being prescribed, PPAs are not bound by the SPB's procurement regime and most have developed their own procurement frameworks. That said, PPAs must comply with other legislation and government policies that require disclosure, reporting or referral in relation to aspects of their procurement activity. For example, most PPAs are 'public authorities' and subject to Treasurer's Instructions (TIs).

PPAs are also generally subject to Premier and Cabinet Circulars, which 'are used to establish whole of government policies and often include an instruction or requirement to take specific action in the implementation of those policies (including *PC013 – Industry Participation Policy*). Once a circular has been approved by Cabinet it must be followed by all government departments.' The biggest exception to this general requirement is that PPAs are explicitly exempt from *PC028 – Construction Procurement Policy*. The reason for this exemption is not known.

The current prescription status of prescribed public authorities is based historically on ministers' and chief executives' views – the Commission has received very little information

¹ *State Procurement Act 2004*, section 4.

² *State Procurement Regulations 2005*, regulation 4, Bodies declared to be prescribed public authorities (Section 4 of Act).

pertaining to the original reasons. It is worth noting that there are a variety of other commercial public entities that are currently not prescribed.

All PPAs share the view that to be subject to the SP Act would create administrative burdens and result in lost commercial opportunities, potentially causing some PPAs to compromise their statutory and business obligations and outcomes. The Commission accepts that complex and specialised procurement activity is undertaken by some PPAs, for which they need timely and flexible procurement arrangements. This is not a barrier to a whole-of-government framework, provided it has appropriate categories of specialisation that can be managed where excellence already exists.

PPAs generally observe the objects of the SP Act in their procurement frameworks and practices and some use SPB documentation or variations of it to formulate their policies.

Aside from the potential administrative burden of complying with SPB policies and procedures, the Commission sees no compelling reason to exempt PPAs from the broader procurement framework. Further, the Commission is inclined to the view that there are benefits to including PPAs in a more flexible whole-of-government framework.

7. Construction

Not all the information sought by the Commission was received in a timeframe that allowed for the type of analysis necessary to reach a conclusion on some issues. This was most problematic in DPTI's case given the central role that agency plays in construction procurement. Nonetheless, consultation with other public authorities and external stakeholders identified some possible options to improve the effectiveness of DPTI's own procurement and the services that it provides to other agencies.

It is also evident that DPTI understands the importance of a strong procurement process and is attempting to improve its processes. The Commission expects that with the information in hand now and further consultation with DPTI and other public authorities will allow it to develop recommendations on the issues identified in this chapter.

Background

The definition of 'construction procurement' for this SAPC inquiry is associated with a 'prescribed construction project' as provided in the *State Procurement Regulations 2005*. The exclusion of prescribed construction projects from the *State Procurement Act 2004* means construction procurement valued over \$150 000 (excluding GST) does not come under the SP Act or the State Procurement Board procurement policy framework.

Regulation specific to construction procurement

There are three arrangements or frameworks that govern the procurement of South Australian Government construction projects:

- The State Procurement Board's procurement policy framework applies to the government procurement of construction valued at \$150 000 (excluding GST) or less. Prescribed authorities are excluded from the framework.
- DPTI's Construction Procurement Policy: Project Implementation Process applies to all prescribed construction projects. DPTI is responsible for the management of

construction projects in the civil and building (commercial) construction sectors. Prescribed public authorities are exempt from this policy.

- Prescribed public authorities have their own policies and guidance for procurement activity which may include procurement relating to construction projects.

In addition, all public authorities are required to comply with PC015 Procedures for Submissions to Cabinet Seeking the Review of Public Works by the Public Works Committee (PWC). Section 16A of the *Parliamentary Committees Act 1991* requires that public works must be referred to the PWC if the total amount of money provided by Parliament or a state instrumentality to be applied to construction of the work exceeds \$4 million. No public monies can be expended until the PWC has presented its final report.

The following issues relating to construction procurement were identified by stakeholders.

Value for money

In its response to the Commission's final report, the SA Government supported the recommendations on value for money and provided the following commitments:

- revise and develop an improved SPB Value for Money in Procurement Guideline to better assist government agencies in applying and determining value for money;
- better practices identified by the Commission in other jurisdictions will be considered in drafting the new guideline;
- the revised guidance will be incorporated into current SPB training courses. A series of specific information sessions will also be held; and
- businesses, business associations and not-for-profit organisations will be informed of the revised value for money guidance in the following ways:
 - The materials will be published on the SA Tenders and Contracts website.
 - Businesses will be provided with the revised guidance as part of each tender (where appropriate).
 - The Office of the Industry Advocate will communicate the guidance material to businesses as part of regular industry engagement forums.

The Commission considers that more transparency would benefit the construction procurement by public authorities by increasing the efficiency of the process (more fit for purpose bids and less time wasted both for suppliers and for client agencies).

Throughout the consultation process a consistent message was that a lot of value can be lost from an underdone acquisition plan. The Commission recommends that more time and resources are allocated to complete this stage.

The final report for Stage 1 observed the procurement function is increasingly being used as a tool to contribute to other government objectives. Those objectives or priorities have not, traditionally, been considered as part of a procurement 'value for money' assessment.

The Commission sees merit in a value for money framework for construction procurement that encourages the SA Government to:

- specifically identify and quantify the government objectives to be incorporated into the procurement process for construction procurement projects, specifying the minimum level;
- communicate the prioritised list of other government objectives to business; and
- require minimum requirements for a bid to be compliant: at the next step the evaluation is based on fitness for purpose and whole-of-life costs, with the tie breaker for equal tenders being the extent of performance above the minima on the other objectives.

The Commission notes a similar approach for all procurement across government could provide greater cohesion and insight without imposing additional unnecessary red tape.

Risk management

The Commission found several similar risk management issues for construction procurement, as it did for goods and services procurement in Stage 1. They are shortcomings in data and reporting, risk allocation and guidance on risk management. In addition, the choice of delivery model and type of projects have also emerged as issues.

While the Commission saw examples of good agency risk management practice such as SA Water's, the very limited documentary evidence suggests a transaction-based approach rather than a strategic approach to risk in procurement. This will be followed up.

As an example, the Commission has found that DPTI is not able to easily retrieve and present information related to projects managed on the behalf of agencies. This is at least partly symptomatic of serious deficiencies in DPTI's data systems, a point acknowledged at very senior levels in DPTI.

Contract management

Consistent with the findings in Stage 1, the Commission has found an absence of holistic contract management reporting and performance measures.

The Commission observed the strong focus in the construction procurement process in the market approach and supplier selection phases. However, once they have occurred, the subsequent governance and oversight of the framework for construction procurement appears to attract less attention.

Capability

The Commission notes that the government has already accepted the Commission's recommendation from Stage 1 (2.10) in relation to developing a strategic plan for procurement capability development. Having now considered construction procurement capability, the Commission is of the view that a strategic and planned approach to construction procurement capability development is also needed.

A construction procurement capability strategy will need to address how technical (construction) staff and procurement staff can work together to achieve optimised outcomes. The Commission envisages this may include providing additional training for procurement-specific skills for technical specialists and advisers (e.g. engineers) to give them an improved understanding of procurement and contract design and management requirements. Legal training is very likely to be useful.

The strategy will also need to focus on supporting the capabilities required by Lead Agency representatives in fulfilling their project sponsor role under the Construction Procurement Policy: Project Implementation Process. Some of those skills are not necessarily procurement specific but are important in the overall outcome of the project and the Lead Agency's accountability.

The Commission considers that raising procurement to a strategic and high-value function within public authorities and prescribed public authorities will help to attract and retain high-performing individuals to engage in procurement activity. The professional development in the recruitment and training strategy could encourage more junior individuals from other specialties like law and business analysts to focus on a procurement career, which would help address the shortage of procurement officers over time.

Engaging with suppliers

The Commission made four recommendations on market engagement in Stage 1. They variously covered increased availability of information regarding supplier capability and future government procurement opportunities and an industry engagement guideline for government buyers to encourage effective market engagement.

Similar considerations apply to construction. The Commission seeks information on how agencies can achieve a better match between the market approach chosen and the fairness provided to the targeted pool of suppliers who are competing for the work.

Streamlining the process

The Commission has analysed the procurement processes used by DPTI for both building and civil infrastructure and has made some initial observations based on the limited information provided by the department. It will take up these and other matters with DPTI in the coming weeks.

While agencies have found DPTI's expertise on larger projects to be invaluable, opportunities to improve the process for smaller projects were mentioned. In effect, agencies have suggested the policy framework supporting construction procurement could find a better balance, particularly for smaller and specialised construction projects. One option may be to reconsider the threshold for when the PIP is applied to allow agencies to manage smaller project and free up some capacity in DPTI to focus on the larger projects.

This will be considered in the final recommendations that the Commission will make in terms of the future scope of the procurement system and the associated roles and responsibilities that agencies will have under a future system.

Matters for further consultation with DPTI

While the release of the draft report is the start of the second consultation phase on all the Commission's findings to date, throughout the draft report, the Commission has noted that there are a number of items on which we intend to re-engage with DPTI prior to finalising the report. The following is a summary of those specific items:

- DPTI's strategic approach to value in procurement;
- the strategic use of different formulae in tender evaluations;
- the application of risk management principles in practice;
- how subcontractor feedback is/will be addressed;
- the development and use of contract management plans;
- how lessons learned feedback is incorporated in future procurements;
- the difference between the civil infrastructure and building management processes;
- procurement process documentation; and
- DPTI's view of appropriate procurement metrics.

8. SA Industry Participation Policy (SAIPP) for construction and prescribed authorities

The SAIPP aims to ensure South Australian businesses are given full, fair and reasonable opportunity to compete for government contracts. A comprehensive overview of the functioning of the SAIPP has been provided in Stage 1 of the inquiry.

For construction-specific issues, the Industry Advocate engages with businesses directly and through the Industry Advocate's Building and Construction Industry Advisory Panel. This panel provides input into the development of new initiatives by the Industry Advocate.

Construction projects fall under three categories according to size:

- Between \$33 000 and \$4 million (or \$1 million in the regions): tenderers must provide an Economic Contribution Test (ECT) and above \$220 000, the client agency must give a minimum weighting of 15 per cent to the ECT score in the tender evaluation.
- Between \$4 and \$50 million: tenderers are required to provide an Industry Participation Plan (IP Plan) and the client agency must give a minimum weighting of 15 per cent to the IP Plan score when evaluating the tender.
- Above \$50 million tenderers are required to develop, with the Office of the Industry Advocate (OIA), a tailored IP Plan that considers the economic development objectives of the government.

If a program of linked small infrastructure projects is funded by the government or if the project is in a priority area of focus, a tailored IP Plan may also be developed from inception.

The Commission's analysis of the use of the SAIPP and ECT by the prescribed public authorities broadly confirms the conclusions in Stage 1 relating to procurement of goods and services. The South Australian Government has largely accepted the Commission's recommendations on those matters.

The Commission's further findings on the SAIPP relating to construction and prescribed public authorities are:

- There are clear deficiencies in the information recorded by agencies regarding their application of the SAIPP, and in some cases some deficiencies in practice, particularly the weighting. The Commission notes the OIA has work in progress that has the capacity to at least partially address these issues through better information and exercising the IA's authority to seek improvement.
- The SAIPP appears to be well-established in tendering for the state's construction work and for prescribed public authorities. The apparent fact that the ECT/IP Plan scores appear rarely to have made the difference between the winner and runner up reflects, in the Commission's view, that the policy is embedded into the way procurement is done.

In addition, the Commission notes the value to local businesses from inclusion in the supply chains of interstate and national businesses as part of the economic contribution to South Australia. This is a further extension of the Commission's view that SAIPP has a role to play in increasing the numbers of match-fit businesses in the state.

9. Other procurement issues

Metrics

A recurring theme has been that there is a lack of data and information to provide evidence on trends in the procurement system and to support monitoring of performance and identifying areas for improvement. The Commission has heard this point from both stakeholders and public authorities.

The Commission sought a summary of the measurement regimes and reporting arrangements relating to measuring the different phases of the procurement process, value for money, contract outcomes and broader outcomes such as the IPP. The information actually generated had some specific gaps; public authorities did not, apart from at individual project level, provide examples of reporting on outcomes used either internally or externally.

The central observation is that whole-of-government reporting of outcomes and collection of information by agencies appears inadequate. This situation reflects the limitations on the information that can be collected as well as the low levels of accountability in procurement spending (for both goods and services and construction procurement).

The Commission rarely observed an in-depth summary of expenditure by an agency on any of the key metrics such as locality, business size, supplier groupings (by industry) or outcome area of government such as purchasing of social enterprise goods and services. State Procurement Board of South Australia data collected up until the 2017–18 financial year used the United Nations Standard Products and Services Code (UNSPSC) classification

of expenditure to categorise expenditure by commodity and services. However, the collection of data via this method has been discontinued.

Examples in other jurisdictions sighted by the Commission include dashboards of information which can be interrogated and cross-tabulated for expenditure and contracting activities across government.

Innovation

The current procurement frameworks for construction and goods and services, in design and in practice, do not systematically enable collaboration and commercial partnership on proposals for purchasing goods and services with innovative characteristics. The underlying causes seem to be:

- The process of innovation often occurs during the market approach phase rather than at project design.
- There is a lack of understanding of the impact of procurement specification and procession on innovation.
- There is an absence of processes applied within agencies across the public sector to identify opportunities for innovative solutions coupled with poor market engagement.

The Chief Entrepreneur and the Industry Advocate have argued for the Smart Procurement Policy to become part of the government's entrepreneurship and innovation policies.

The Commission broadly agrees that the policy environment supporting innovative ideas of local business can be improved through policies that:

- enable innovative proposals to operate within the accepted framework of procurement policies and guidelines;
- provide agencies with incentives to take the risks inherent in procuring innovative products, including the approach to helping businesses develop their IP; and
- simplify procedures to support innovative tendering that focus more on capability and capacity of the proposal rather than capturing administrative information.

The Commission notes that a more capable procurement profession capable of higher discretionary judgement would underpin efforts to stimulate innovation.

10. Conclusion

As stated above, this is a draft report and, with its publication, the Commission will move to the second consultation phase with stakeholders. Feedback on the conclusions, information requests and draft recommendations is encouraged and welcomed. The Commission would also like to thank all stakeholders for their contribution to date.

Draft recommendations

Draft recommendation 2.1

To support the transition to state-wide category management and improve value for money, the Commission proposes that:

- Prescribed public authorities (PPAs) should adopt relevant whole-of-government goods and services arrangements for their common purchases unless their current arrangements achieve superior administrative efficiencies and economic benefits.
- PPAs with low-spend/low-risk purchasing of common goods and services, or where unique products cannot be sourced from those arrangements, should be excluded from the requirement to consider whole-of-government common goods and services arrangements.

Draft recommendation 3.1 (supplementary to Stage 1 recommendation 2.9)

In order to strengthen procurement capability among smaller prescribed authorities, the Commission proposes that the Heads of Procurement Community of Practice be expanded to prescribed public authorities not currently included; and include a standing construction procurement sub-committee to address construction-related issues for public authorities and prescribed public authorities.

Draft recommendation 3.2

In order to ensure all key areas of procurement capability in the South Australian public sector are addressed, the capability development strategy agreed by the South Australian Government in its response to the Stage 1 final report be expanded to construction procurement and specifically address issues including:

- incorporating the construction discipline-specific technical expertise and procurement and contract management proficiencies across all public authority staff involved in construction-related procurements; and
- the supporting capabilities required by Lead Agencies to effectively fulfil their project sponsor role mandated under *Premier and Cabinet Circular – Construction Procurement Policy Project Implementation Process (PC028)*.

Draft recommendation 3.3

In order to better track performance in construction procurement, the Commission proposes that DPTI develop benchmarking for construction procurement processes to compare performance across matters such as:

- outcomes from procurement planning, establishment of the business case and engagement with suppliers on the design aspect of projects;
- timeliness of the procurement process; and
- outcomes of the procurement process in terms of meeting the original scope.

Draft recommendation 4.1

In order to strengthen the South Australian Government's capacity to understand, analyse and improve whole-of-government procurement in line with its support for Recommendation 2.7 of the Commission's final report into Stage 1, the Commission proposes that the reform of the reporting requirements and the related short-term actions previously approved in relation to goods and services be extended to cover construction procurement.

Draft recommendation 4.2

To encourage innovative procurement offerings in government procurement, the Commission recommends that policy and practice be amended to make express provision for:

- innovative proposals to operate within the accepted framework of procurement policies and guidelines of single source procurement from suppliers identified as having innovative products or services – essentially a two-stage framework;
- agencies to accept and manage the inherent risks involved in procuring innovative products, including the approach to helping businesses developing their IP;
- procedures to support innovative tendering that focus on capability and capacity of the proposal rather than capturing administrative information which does not enable effective evaluation;
- flexibility for both business and public authorities to collaborate on a greater scale on future purchasing requirements (including goods and services and construction). Such programs or incentives can occur through, for example, category management plans, meet the buyer events and more extensive supply chain management.
- increased attention by public sector authorities to identifying areas that would benefit from innovative purchase practices.

Draft recommendation 4.3

In order to reduce the impediment to innovation and improvement that aspects of current contracting arrangements may impose, the Commission proposes that a clearer set of arrangements be put in place by:

- developing and publishing improved guidance on the State Government Intellectual Property Policy to provide a wide range of examples of particular types of procurement and the state's position on ownership of IP;
- including in the guidance contained in the State Government Intellectual Property Policy guidance on the relative merits and instructive case studies for construction procurement outlining the factors for various delivery models and greater flexibility in contract provisions; and
- providing guidance on managing IP, covering needs analysis, managing IP through the procurement process, and model clauses and contracts that address matters raised by stakeholders.

Information request

Information request 5.1

The Commission seeks views, evidence and advice on the current scoring of ECT and IP Plans in relation to construction projects, and in particular on how it could better reflect the economic contribution made by suppliers to South Australia, including strengthening South Australian businesses by including them in the value chain of interstate and national businesses and the contribution of service providers.

Definitions

The following definitions represent the Commission's understanding of the terms based on the documents that have been reviewed.

Aggregated contract

This is the practice of grouping together contracts for commonly purchased goods and services to harness greater economies of scale when procuring from the marketplace.

Chief Procurement Officer

The Chief Procurement Officer is a senior executive in a public authority who has responsibility, delegated by the authority's principal officer, for the cost-effective and efficient management of the procurement operations of the authority, subject to, and in accordance with, the policies, principles, guidelines, standards and directions of the State Procurement Board.

Closed tender

A closed tender is a procurement process where only selected suppliers, one or more, are invited to submit offers to supply goods or services to government.

Direct negotiation

This is a procurement process undertaken by directly approaching and negotiating with one or more suppliers without testing the market. It is usually undertaken when comprehensive market research indicates that there is a limited-supply market.

Ethical procurement

The conduct of employees (and/or representatives) and suppliers in undertaking and managing procurement.

Industry Capability Network

The Industry Capability Network (ICN) was established in 1985 and is funded by the South Australian Government through the Department for Industry and Skills to provide specialist supply chain services. The ICN provides purchasers with a free sourcing service to identify Australian and New Zealand suppliers capable of supplying items that would otherwise need to be imported. The ICN's technical consultants have comprehensive knowledge of national industrial capability in all tiers of manufacturing.

Open tender

An open tender involves a publicly advertised invitation to all interested suppliers to submit offers to supply goods or services to government.

Panel providers

A provider panel is a contractual arrangement established with at least two suppliers for the anticipated provision of goods or services over a specified period of time. A panel contract contains standard terms and conditions on the basis of which the goods or services will be

provided by panel providers. A panel contract may be established by a public authority, a lead agency or at an across-government level.

Prescribed procurement operation

In accordance with section 4 of the *State Procurement Act 2004*, the following prescribed procurement operations are excluded from the definition of procurement operations:

- a prescribed construction project of a cost exceeding \$150 000;
- the provision of funding to a third party by a public authority that, in accordance with Treasurer's Instructions, is classified as a grant.

Prescribed public authority

In accordance with the *State Procurement Act 2004*, a prescribed public authority is a person or body that has been declared by the regulations to be a prescribed public authority for the purposes of the Act.

Principal Officer

Generally, the Principal Officer is the chief executive officer of the public authority as declared by the regulation to be the principal officer of the authority. The principal officer is responsible for the efficient and effective management of the procurement operations of their authority, subject to and in accordance with the policies, principles, guidelines, standards and directions of the State Procurement Board. This responsibility extends to the delegates of the principal officer (*State Procurement Act 2004*, s 20).

Procurement

Procurement refers to the end-to-end process of buying goods and services that begins with defining the need, approaching the market, engaging the suppliers, contract management and closing the contract, as well as the disposal of the goods.

Procurement authority

The authority to approve a proposed course of action, strategy or recommendation relating to procurement (acquisition plan or purchase recommendation) to a specified dollar amount as issued to a public authority's principal officer by the State Procurement Board.

Procurement governance committee

A committee comprising nominated senior officers that oversee the purchase of goods and services within a prescribed delegation. May be called an Accredited Purchasing Unit (APU) or Procurement Governance Unit (PGU).

Procurement operations

In accordance with the *State Procurement Act 2004* a procurement operation in relation to an authority means the procurement of goods or services required by the authority for its operations, including (without limitation) the procurement of:

- a supply of electricity, gas or any other form of energy;

- intellectual property;
- the management of goods of the authority, including (without limitation) the care, custody, storage, inspection, stocktaking or distribution of goods of the authority;
- the management of the authority's contracts for services; or
- the disposal of goods surplus to the authority's requirements,

but does not include operations excluded from this definition by the regulations.

Public authority

In accordance with the *State Procurement Act 2004*, section 4 a public authority is:

- (a) an administrative unit or other agency or instrumentality of the Crown; or*
- (b) any incorporated or unincorporated body–*
 - (i) established for a public purpose by an Act; or*
 - (ii) established for a public purpose under an Act (other than an Act providing for the incorporation of companies or associations, co-operatives, societies or other voluntary organisations); or*
 - (iii) established or subject to control or direction by the Governor, a Minister of the Crown or any instrumentality or agency of the Crown (whether or not established by or under an Act or an enactment); or*
- (c) a person or body declared by the regulations to be a public authority for the purposes of this Act.*

The Act states that a public authority does not include public authorities prescribed in the regulations.

Risk management plan

A document that is used to specify the nature and treatment of risks throughout the procurement cycle. The level of detail will be commensurate with the procurement's complexity and value. A risk register may be used to help develop a plan.

Small and medium enterprises (SMEs)

Unless otherwise stated, SMEs refers to the Australian Bureau of Statistics' definition, being a business that employs up to 200 people.

South Australian Code of Ethics

The Code of Ethics for the South Australian Public Sector is issued under the *Public Sector Act 2009* (the PS Act), in which it is referred to as the Code of Conduct. The code came into effect in July 2015 and builds on the principles outlined in the PS Act. It sets out the professional standards expected of every employee in the SA public sector.

South Australian Product Register

The SA Product Register (the Register) is managed by the South Australian Industry Advocate and is designed to identify products that are created, manufactured and supplied in South Australia. The Register provides a practical way to find local manufacturers, creation experts and suppliers. It also measures jobs at critical points in the supply chain. The Register is designed to be used by government agencies, but access for other levels of government and the private sector is provided free of charge.

Value for money

The SPB guideline defines value for money as the optimal use of taxpayer resources to achieve the intended outcome.

Acronyms

ABN – Australian Business Number

ACO – Aboriginal Controlled Organisations

AEPP – Aboriginal Economic Participation Policy

AGD – Attorney-General’s Department

AGFMA – Across Government Facility Management Arrangements

AMA – Australian Medical Association

AMCA – Air Conditioning and Mechanical Contractors’ Association

ANZGPA – Australia New Zealand Government Procurement Agreement

ANZSCO – Australian and New Zealand Standard Classification of Occupation Code

AP – Acquisition plan

APBSA – Architectural Practice Board of SA

APCC – Australian Procurement and Construction Council

APU – Accredited purchasing unit

AUSFTA – Australia–United States Free Trade Agreement

AVMC – Adelaide Venue Management Corporation

BCSA – Baptist Care South Australia

BTFN – Business Tax File Numbers

CA – Contract awarded

CAA – Courts Administration Authority

CCS – Crown Commercial Service (UK)

CE – Contract extended

CEDA – Committee for Economic Development of Australia

CES – Client engagement service

CHAFTA – Chile–Australia Free Trade Agreement

CIPS – Chartered Institute of Procurement & Supply

CITB – Construction Industry Training Board

COAG – Council of Australian Governments

COTA – Council on the Ageing

DCP – Department for Child Protection

DCS – Department for Correctional Services

DE – Department for Education

DEW – Department for Environment and Water

DHS – Department of Human Services

DHW – Department for Health and Wellbeing

DIS – Department for Industry and Skills

DPC – Department of the Premier and Cabinet

DPTI – Department of Planning, Transport and Infrastructure

DTF – Department of Treasury and Finance

DTTI – Department for Trade, Tourism and Investment

ECT – Economic contribution test

EFAP – Emergency Financial Assistance Program

EOI – Expression of interest

EPAS – Enterprise Patient Administration System

ESCOSA – Essential Services Commission of South Australia

FAM1 – Formal approach to market date

FAM2 – Market approach closed date

FAR – Federal Acquisition Regulation (US)

FTE – Full-time equivalent

GPRS – Generic Procurement Recruitment and Selection System

GST – Goods and Services Tax

HOP – Heads of Procurement Group

HSCGB – Health Services Charitable Gifts Board

IA – Industry Advocate

ICAC – Independent Commissioner Against Corruption

ICT – Information and communications technology

IP – Intellectual property

IPAA – Institute of Public Administration Australia

IPP – Industry Participation Policy

JAEPA – Japan–Australia Economic Partnership Agreement

KAFTA – Korea–Australia Free Trade Agreement

KPI – Key performance indicator

LGFA – Local Government Financing Authority

LPCC – Legal Profession Conduct Commissioner

LWB – Life Without Barriers

MCIPS – Member of the Chartered Institute of Procurement and Supply

MTA – Motor Trade Association

NDIS – National Disability Insurance Scheme

NFP – Not-for-profit

NZBN – New Zealand Business Number

OCPSE – Office of the Commissioner for Public Sector Employment

ODASA – Office for Design and Architecture

OIA – Office of the Industry Advocate

OOHC – Out-of-home care

PAC – Procurement Approvals Committee

PC – Premier and Cabinet Circular

PCI – Procurement Capability Index (NZ)

PGC – Procurement Governance Committee

PGU – Procurement Governance Unit

PIP – Project Implementation Process

PIRSA – Department of Primary Industries and Regions South Australia

PoC – Proof of concept

PPA – Prescribed public authority

PWC – Public Works Committee

PR – Purchase recommendation

RFDS – Royal Flying Doctor Service

RFP – Request for proposal

ROSMA – Return on Supply Management Assets

RTWSA – Return to Work SA

SAAS – South Australian Ambulance Service

SACOSS – South Australian Council of Social Service

SAFECOM – South Australian Fire and Emergency Services Commission

SAFTA – Singapore–Australia Free Trade Agreement

SAHA – South Australian Housing Authority

SAIPP – South Australian Industry Participation Policy

SAPC – South Australian Productivity Commission

SAPOL – South Australia Police

SARC – Statutory Authorities Review Committee of the South Australian Parliament

SATC – South Australian Tourism Commission

SBC – Small Business Commissioner

SBI – Single Business Identifier

SBIR – Small Business Innovation Research (US)

SME – Small and medium enterprises

SP Act – *State Procurement Act 2004*

SPB – State Procurement Board

SPC – State Purchase Contract (VIC)

SP Regs – *State Procurement Regulations 2005*

SRM – Supplier Relationship Management

TAFE SA – Technical and Further Education South Australia

TI – Treasurer’s Instruction

UCSA – Uniting Country South Australia

UNSPSC – United Nations Standard Products and Services Code

VGPB – Victorian Government Purchasing Board

WHS – Workplace health & safety

1. Introduction

1.1 Context

The South Australian Productivity Commission (the Commission) was asked to undertake an inquiry into the South Australian procurement system. This inquiry has been divided into two stages. Stage 1 focused on goods and services procurement governed by the *State Procurement Act 2004* (SP Act). This inquiry was completed on 17 May 2019. The second stage focused on procurement spending not governed by the SP Act. That is, prescribed public authorities and construction expenditure above \$150 000 (excluding GST). In addition, the Stage 2 final report will make recommendations regarding the whole-of-system architecture.

Procurement of goods and services for the South Australian Government and its agencies is a substantial component of the South Australian economy, amounting to approximately \$11 billion annually or around 10% of gross state product (June 2018). The total spending broadly falls into three groups, each of which is subject to different legal and governance arrangements:

- public authorities that are required, for goods and services projects and for construction projects under \$150 000 (excluding GST), to comply with the State Procurement Board (SPB) policy framework consistent with the functions of the SPB in the *State Procurement Act 2004*;
- prescribed public authorities that are not required to comply with the policies, principles, guidelines, standards or direction issued by the SPB; and
- spending on construction projects above \$150 000 (excluding GST) is also not governed by the SPB.

Purchased goods and services underpin the provision of most public services (e.g. office supplies, vehicles, hospital equipment), either by enabling public sector employees to do their work or by contracting others to provide public services. The expenditure on capital projects also supports the delivery of public services (e.g. hospitals and schools) as well as the general economic and social wellbeing of the state (e.g. road and rail networks). As such, they need to be fit for purpose and deliver good value for the expenditure of public funds.

Procurement spending in South Australia also has a significant impact on employment, business activity and investment in the state. For many smaller businesses, government contracts represent a significant portion of their business within the state. The award of a large government contract can generate a significant amount of associated economic activity (e.g. building new facilities, hiring additional staff). On the other hand, the loss of a major government contract can result in the closure of a business and the loss of those jobs. This is reinforced in OECD 2017[3]:

Public sector productivity has a significant impact on the performance of the national economy and societal well-being. Governments are the main, and sometimes only, suppliers of key services to citizens, such as education,

health, social services, transportation and infrastructure. In fact, in several sectors, governments purchase most of the sector's services: OECD governments are responsible for 70% of final consumption expenditure on health goods and services and for 84% of final consumption expenditure on education.

The state's procurement system also incorporates selected social, environmental and economic goals that have been linked by government policy to government purchases. The challenge is how to incorporate these goals into the tender, evaluation and contract management arrangements without compromising whole-of-life costs and fitness for purpose.

Businesses and not-for-profit organisations (NFPs) have expressed concerns about the cost and red tape (e.g. delays, cancellation of tenders and excessive supporting information requirements) in tendering for government work in the context of uncertain return. These concerns have led to some reforms including simpler administrative arrangements, related policies such as the Industry Participation Policy, and attempts to cut red tape. Notwithstanding these efforts, concerns persist.

The Commission acknowledges the South Australian Government's acceptance of the recommendations to cut red tape and administrative burdens contained in the Commission's final report on Stage 1 of this inquiry.

The inquiry has spent a significant amount of time and effort to date in understanding how the tender process for construction works in practice for businesses, how much effort is involved in submitting a tender and what options could simplify the tender process without compromising reasonable safeguards on the use of public funds.

Consult Australia in its submission to the Commonwealth Government Parliamentary Inquiry into the Australian Government's role in the development of cities (infrastructure procurement section), 2018, observed:

at a time when public finances are stretched, better procurement offers government the chance to build more for less, achieving better project outcomes with fewer delays. It also makes government agencies a more desirable client for industry to do business with, which in turn will lead to more firms competing to provide their services to government.

The Commission agrees that procurement reform offers an opportunity to increase the benefits of the public spend by increasing value for money, improving productivity, supporting local jobs and industry, and supporting the government's other social, environmental and economic objectives.

1.2 Terms of reference

The Commission was originally tasked on 31 October 2018 to evaluate the effectiveness and efficiency of state government policies and practices for the procurement of goods and services and to identify options to improve procurement practices and their impacts on local industry, noting concerns expressed by small and medium businesses (SMEs) about the cost of and time expended in tendering for procurement opportunities.

The scope was originally confined to agencies and matters that fall within the scope of the SP Act, specifically excluding capital projects and prescribed public authorities (PPAs) such as SA Water and the South Australian Housing Trust.

On 15 February 2019, the government expanded the scope of the initial terms of reference to include capital spending and PPAs. The Stage 1 report focused, as much as possible, on the original scope of the inquiry. The elements of the expanded scope and the overall system architecture are addressed in this draft report.

In both Stages 1 and 2 of the inquiry, the Commission is required to have regard to:

- relevant state and federal legislation (see Box 1.1);
- South Australia's national and international obligations about government procurement (see Box 1.2); and
- the South Australian Government's election commitments (see Box 1.3).

Box 1.1

South Australian and Commonwealth legislation relevant to government procurement

The regulatory environment.

1.1 *State Procurement Act 2004 and State Procurement Regulations 2005*

The key regulatory instruments governing procurement operations for goods and services in South Australia are the *State Procurement Act 2004* and the *State Procurement Regulations 2005*.

1.2 Treasurer's Instructions (TIs)

Under section 41 of the *Public Finance and Audit Act 1987*, instructions are issued by the Treasurer and are administered by the Department of Treasury and Finance (DTF). The Act regulates the receipt and expenditure of public money. The TIs apply to each public authority as defined by the Act (except specified universities), and to all procurement activity including construction (unless specifically excluded in the TI).

1.3 Premier and Cabinet Circulars (PCs)

PCs are used to establish whole-of-government policies and will include instructions or requirements to take specific action on the implementation of those policies. The PCs apply to all public authorities, including PPAs, and to all procurement activity (including construction) unless specifically excluded.

1.4 South Australian Industry Participation Policy (SAIPP)

The SAIPP is established under the *Industry Advocate Act 2017* (IA Act). The IA Act provides for *'the appointment of the Industry Advocate and to provide for the powers and functions of the Industry Advocate'*.

1.5 Code of Ethics

Under the *Public Sector Act 2009*, all public sector employees are accountable for exercising their delegated authority and for performing their roles within the values and standards in the public sector code of conduct. Delegated authority would include delegations under the *State Procurement Act 2004* and under TIs.

1.6 Other procurement-related legislation

There are a number of other pieces of legislation, policies and agreements that have important implications for the operation of the South Australian Government procurement framework.

Box 1.2

Australian and International obligations relevant to government procurement

The South Australian Government is a signatory to the following cooperative government procurement agreement:

- *Australian and New Zealand Government Procurement Agreement (ANZGPA)*

The South Australian Government has agreed to comply as if it were a party to the following free trade agreements, which have specific government procurement chapters:

- *Australia–United States Free Trade Agreement (AUSFTA)*
- *Chile–Australia Free Trade Agreement (CHAFTA)*
- *Korea–Australia Free Trade Agreement (KAFTA)*
- *Japan–Australia Economic Partnership Agreement (JAEPA)*
- *Singapore–Australia Free Trade Agreement (SAFTA)*
- *Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP)*
- *World Trade Organisation Agreement on Government Procurement (WTOAGP)*

*Box 1.3***South Australian Government election commitments**

The election commitments on procurement included five commitments and three principles for government procurement. The five commitments comprise:

1. reviewing the aggregation of contracts
2. requiring selective market approaches to include South Australian businesses
3. establishing a pre-registration system for tenderers and contractors
4. reviewing the status of prescribed authorities
5. establishing a small unit to assist small to medium businesses in preparing their tenders.

The three principles for government procurement comprise:

- 'Value for money – purchases should deliver an efficient price over the life of the procurement, including both the initial purchase and lifecycle costs ...
- Fit-for-purpose – purchases should consistently deliver on the requirements for which the procurement was made; and
- Compliance with all legal requirements – the government must observe all its legal obligations in undertaking public procurement to avoid exposing taxpayers to any unnecessary risks.'

1.3 The Commission's approach

The Commission published an issues paper for Stage 2 on 5 June 2019 which summarised its understanding of the issues specific to construction spending and PPAs. In response, the Commission received an additional ten written submissions (57 were received during Stage 1), all of which are published on the Commission's website (www.sapc.sa.gov.au). The Commission notes that many submissions in Stage 1 contained information relevant to Stage 2. In addition, the Commission consulted through various means with individuals from industry associations, businesses and government agencies on the issues paper.

The Commission also acknowledges, with appreciation, the extensive assistance provided by SA Water and DPTI to assist with documenting their respective approaches to procurement for construction (and also goods and services in the case of SA Water).

The Commission has examined databases from:

- 18 agencies, noting 8 of them had no construction activities to report on (SA Health, Department of Education, Department of the Premier and Cabinet, Attorney General Department, Courts Administration Authority, SA Police, Department for Child Protection and Department of Treasury and Finance) and 10 of them provided information (DPTI, SA Water, Forestry SA, Return to Work SA, Department of

Environment and Water, Department of Correctional Services, State Emergency Services, SA Fire and Emergency Services Commission, Renewal SA and SA Housing);

- the SA Tenders website;
- the Office of the Industry Advocate database on Industry Participation; and
- the Commission's own random sample of 106 recent procurements across agencies.

This draft report is intended to generate further feedback from stakeholders on the Commission's draft recommendations and draft conclusions. It also contains some information requests and foreshadows further discussions with public authorities necessary to finalise outstanding issues. Once the report is released, the Commission will accept additional written submissions until 20 September 2019 and will conduct another round of consultation with external and internal stakeholders.

1.4 The current South Australian procurement system

Approximately half of South Australia's government procurement system is governed by the SP Act. Structurally the model is a central procurement board that guides policy and practice, coupled with procurement governance and processes that are substantially delegated to, and operated by, public authorities.

The object of the SP Act is to advance government priorities and objectives by a system of procurement for public authorities directed towards:

- obtaining value in the spend of public money
- providing for ethical and fair treatment of participants
- ensuring probity, accountability and transparency in procurement operations.

The SPB administers the SP Act. The operations of the SPB are overseen by the Minister for Finance. The SPB has the following functions under the SP Act:

- facilitating strategic procurement by public authorities by setting the strategic direction of procurement practices across government;
- developing, issuing and keeping under review policies, principles and guidelines relating to the procurement operations of public authorities;
- giving directions relating to the procurement operations of public authorities;
- investigating and keeping under review levels of compliance with the SPB's procurement policies, principles, guidelines, standards and directions;
- assisting in the development and delivery of training and development courses, and activities relevant to the procurement operations of public authorities;
- providing advice and making recommendations to responsible ministers and principal officers on any matters relevant to the procurement operations of public authorities; and

- carrying out the SPB's functions in relation to prescribed public authorities and any other functions assigned to the SPB under the SP Act.

The SPB issues procurement authority to the principal officer of a public authority that is appropriate to the size and complexity of the public authority's procurement operations. Based on its assessment, the SPB provides a Tier 1, Tier 2 or Tier 3 procurement authority to each public authority. The tiers are as follows (GST inclusive) Tier 1: up to \$15 000 000; Tier 2: up to \$1 500 000; and Tier 3: up to \$220 000.³

Capital procurement over \$150 000 (exclusive of GST) is also not subject to the SP Act. Capital procurement is governed by Premier and Cabinet Circular 028 which advises agencies that the Minister for Transport and Infrastructure supported by the Department of Planning, Transportation and Infrastructure has responsibility for construction policy development and implementation in South Australia. The Construction Procurement Policy: Project Implementation Process was approved by Cabinet on 12 December 2005, and updated in 2011 and 2015.

There are also thirteen PPAs listed in the *State Procurement Regulations 2005*⁴ that are not subject to the SP Act. Each PPA has its own procurement process that is tailored to its own business requirements. While most of the PPAs seem to follow the principles outlined in the SP Act, they are allowed to operate separately and are accountable to their own boards (where governed by one).

1.5 Stakeholder feedback

Specific feedback from internal and external stakeholders will be discussed in more detail in each of the relevant chapters. The following is a brief summary of the high-level feedback received from each group.

1.5.1 External stakeholder feedback

External stakeholders believe that substantial improvements can be made to the state's procurement process. They believe the system is:

- too slow in making decisions, completing contracts and closing projects;
- lacking people capable of managing large and complex procurements;
- reluctant to engage with suppliers on final project design and/or scope;
- reluctant to provide feedback to unsuccessful suppliers that could help improve future tenders
- inflexible in its approach to negotiating risk issues;
- unreasonable in expecting suppliers to meet very short timeframes in response to tenders and locking in a final price;
- overly administratively focused (too much process, too little focus on outcomes);

³ State Procurement Board of South Australia, Procurement Authority and Governance Policy, July 2018, p. 2.

⁴ The Commission notes the Motor Accident Commission which is a listed prescribed public authority ceased operations on 30 June 2019.

- overly conservative with a real reluctance to consider innovation in relation to what is procured (technology, new products and methods such as modular building for demountable classrooms/schools) and alternative contracting modes; and
- constrained by excessively low thresholds for its procurement classes.

1.5.2 Prescribed public authorities

The scale and scope of the PPAs can vary substantially. Some are large with well-established processes like SA Water and Renewal SA, while others are small with little need for detailed procurement processes like the Local Government Financing Authority and the South Australian Architectural Practice Board.

There are no clear principles that the Commission could find to explain why a public authority should be prescribed under the SP Act, nor was it clear to the Commission why the public authorities were prescribed in the first place. All PPAs expressed a preference to remain exempt from the SP Act, generally citing one or more of three reasons:

- They perceive a conflict between the flexibility that the organisations need because they operate in commercial or quasi-commercial environments (in some cases with their own boards) and the SPB's requirements. The SPB's process, policies and practices would impose excessive delays and costs and may lead to missed opportunities.
- The administrative burden for very small public authorities of the SPB's processes, policies and practices was considered disproportionate and excessive.
- The Auditor-General regularly tests PPA procurement processes, which have not been found lacking.

In summary, the PPAs' concerns about being part of a larger procurement process centred around the potential additional loss of time and agility, the level of excellence already achieved by some agencies that, in effect, met the intent of the SPB's requirements, and the additional administrative burden (reporting and auditing) that potentially outweighs any benefits. The systems in place in PPAs are generally not inconsistent with the objects of the SP Act.

1.5.3 Public authorities

In this report, the feedback from public authorities is focused on construction issues as the procurement of goods and services governed by the SP Act was contained in the Stage 1 final report. As DPTI is primarily responsible for managing construction projects, the feedback from public authorities has been divided into two parts: non-DPTI public authorities as agencies that receive a service from DPTI, and the feedback from DPTI which provides the service to public authorities and interacts with suppliers during construction.

1.5.3.1 Non-DPTI public authorities

While public authorities generally support DPTI's central role in managing construction-related projects, some specific concerns have been raised:

- the value management process during the build phase;

- the fees charged by DPTI;
- the time taken between project approval and initiation;
- the time taken to close projects;
- the perceived reluctance of DPTI to consider new approaches to construction and management of construction projects;
- the current appropriateness of the \$4 million threshold that triggers a review by the South Australian Parliamentary Standing Committee on Public Works; and
- views that the \$150 000 threshold for requiring the use of DPTI services is inefficiently low for some public authorities.

1.5.3.2 DPTI

The Commission acknowledges DPTI is currently in a change process to address some of the issues identified by external and internal stakeholders, including:

- value for money – strengthening the focus on whole-of-life costs;
- ensuring capable procurement staff and project teams are involved in the procurement process;
- subjecting major projects to more independent review at key stages;
- simplifying DPTI internal processes as far as possible; and
- making procurement data easier to access and analyse, which is currently seriously impeded by the legacy systems with which DPTI operates.

With respect to its relationship with public authorities, DPTI sees opportunities to improve:

- the outcomes that public authorities want to accomplish through the procurement;
- whole-of-life costs of the build rather than the physical structure; and
- respecting the key roles defined in the Construction Procurement Policy.

In consulting with DPTI to date, several issues have repeatedly emerged:

- High-quality upfront planning is important.
- The particular circumstances of each construction project constrain the capacity to benchmark process performance and outcomes.
- The current settings of delegations and thresholds have not been reviewed recently and impose inefficiencies.
- The size and nature of the construction market in South Australia makes it necessary to contract with national or overseas companies.
- DPTI provides good and regular feedback to unsuccessful tenderers.
- There are pressures on sustaining and building internal capability to manage projects.

- Current contract management and procurement IT systems are inadequate, particularly given current and expected business levels.
- Internal processes can be simplified.

1.6 Structure of the draft report

The draft report addresses these matters in five chapters:

- Chapter 2 examines the public authorities that are currently prescribed under the *State Procurement Regulations 2005*.
- Chapter 3 considers construction procurement by the South Australian Government.
- Chapter 4 addresses several issues common to Stages 1 and 2 of the inquiry, including some that were carried over to the later part of the process.
- Chapter 5 examines the application of the South Australian Industry Participation Policy to construction procurement.
- Chapter 6 sets out options for increasing the state's central capacity to drive a whole-of-government procurement agenda that delivers a better overall contribution to South Australia.

2. Prescribed public authorities

The terms of reference for Stage 2 of the Inquiry into Government Procurement include consideration of 'all procurement by prescribed public authorities'. The Commission has consulted extensively with all prescribed public authorities (PPAs) and considered the Department of Treasury and Finance's 2018 Review of PPAs (the PPA Review 2018; see Section 2.5). The Commission has information from other Australian jurisdictions regarding their current equivalent arrangements and is gathering other relevant information about practice in selected overseas jurisdictions.

Through its consultations, the Commission has developed an understanding of the purpose and business of the PPAs, their governance arrangements and their procurement activity. This approach has assisted the Commission to understand what prescription is, why PPAs value it, and what considerations may be relevant to considering options such as where organisations may variously sit 'outside' of the state procurement framework, 'inside', or 'inside' with a specific status.

2.1 What is a prescribed public authority?

2.1.1 The legal and policy framework

The *State Procurement Act 2004* (SP Act) defines a PPA as 'a person or body that has been declared by the regulations to be a prescribed public authority for the purposes of this Act'.⁵ The *State Procurement Regulations 2005* (SP Regs) set out the bodies declared to be PPAs in Schedule 1.⁶

The current PPAs in Schedule 1 of the SP Regs are⁷:

- Adelaide Venue Management Corporation
- Architectural Practice Board of South Australia
- Construction Industry Training Board
- Health Services Charitable Gifts Board
- Legal Profession Conduct Commissioner
- Local Government Finance Authority of South Australia
- Motor Accident Commission⁸
- Return to Work Corporation of South Australia (Return to Work SA)
- South Australian Forestry Corporation (Forestry SA)
- South Australian Housing Trust (SA Housing Authority)

⁵ *State Procurement Act 2004*, section 4.

⁶ Regulation 4, Bodies declared to be prescribed public authorities (section 4 of Act).

⁷ *State Procurement Regulations 2005*, version 1.1.2019.

⁸ The Motor Accident Commission ceased operations on 30 June 2019 and accordingly has not been considered as part of this inquiry.

- South Australian Water Corporation (SA Water)
- Superannuation Funds Management Corporation of South Australia (Funds SA)
- Urban Renewal Authority (Renewal SA).

The SP Act establishes the State Procurement Board (SPB), and the functions of the SPB. Those functions pertain to providing direction, policies and guidelines, facilitating procurement operations and ensuring compliance with those arrangements for public authorities.⁹

The SP Act therefore provides that all public authorities are subject to the SPB's directions, oversight and guidance unless prescribed. That said, the SPB's powers also include 'to carry out the Board's functions in relation to prescribed public authorities and any other functions assigned to the Board under this Act'.¹⁰ Further, the SPB may 'undertake or make arrangements for procurement operations' for PPAs with the responsible minister's approval; and a PPA is 'bound to comply with any directions given by the responsible minister on the advice or recommendation of the Board'.¹¹ The SPB has indicated that these provisions have not been used; however, on one occasion, the SPB sought and received information from PPAs during the across-government investigation into inappropriate purchasing of office consumables that was subject to a report to the Parliament in 2012.¹²

These provisions in the SP Act indicate Parliament recognised there may be circumstances where it is appropriate to exempt public authorities from the SPB's regime. The SP Act does not provide any criteria for prescribing a public authority nor does it mandate a role for the SPB to prescribe an authority. The Commission understands that the legislative history of the SP Act does not offer any guidance as to Parliament's intentions regarding the types of authorities that would warrant prescription, or any applicable criteria relevant to prescription. Whilst they did offer views in response to the PPA Review 2018 about retaining prescribed status, few organisations indicated their understanding about the origins of their prescribed status.

In the absence of being bound by the SPB's regime, most PPAs have developed their own procurement frameworks, which are variously discussed in Section 2.3.

PPAs must comply with other legislation and government policies that require disclosure, reporting or referral in relation to aspects of their procurement activity. For example, most PPAs are 'public authorities' as defined under the *Public Finance and Audit Act 1987*, generally subjecting them to Treasurer's Instructions (TIs). Some of the TIs are applicable to procurement-related activities, for example *TI17 – Evaluation of and Approvals to*

⁹ Section 4 of the SP Act explicitly excludes PPAs from the definition of a public authority.

¹⁰ SP Act, section 12(1)(i).

¹¹ SP Act, sections 18 and 19.

¹² See Procurement Working Group, *Final Report* (Laid on the Table 13 March 2012). Available at: <http://www.parliament.sa.gov.au/HOUSEOFASSEMBLY/BUSINESSOFTHEASSEMBLY/RECORDSANDPAPERS/TABLEDPAPERSANDPETITIONS/Pages/TabledPapersandPetitions.aspx?TPLoadDoc=true&TPDocType=0&TPP=52&TPS=2&TPItemID=125&TPDocName=Procurement%2bWorking%2bGroup%2bFinal%2bReport%2bMarch%2b2012.pdf>

Proceed with Public Sector Initiatives may apply in so far as a PPA's procurement activity relates to a 'public sector initiative'.

PPAs are also generally subject to Premier and Cabinet Circulars which 'are used to establish whole of government policies and often include an instruction or requirement to take specific action in the implementation of those policies. Once a circular has been approved by Cabinet it must be followed by all government departments.' The most relevant circular applicable to PPAs' procurement activity is *PC027 – Disclosure of Government Contracts*, which requires PPAs to disclose specified information about contracts of specified thresholds on the SA Tenders website (tenders.sa.gov.au).¹³ Other Premier and Cabinet Circulars are also applicable to PPAs but their relevance may be limited given the confined and/or specialised procurement undertaken by some PPAs, e.g. *PC015 – Procedures for Submissions to Cabinet Seeking the Review of Public Works by the Public Works Committee*.¹⁴

Importantly, PPAs are explicitly exempt from *PC028 – Construction Procurement Policy*.¹⁵ The reason for this exemption is not known. *PC033 – Industry Participation Policy* applies to all PPAs.

Although not forming part of the general government sector, some PPAs have elected to comply with the reporting arrangements in *PC013 – Annual Reporting Requirements* as they relate to procurement activity (which forms part of the financial performance reporting obligations for the general government sector under the *Public Sector Act 2009*).¹⁶

2.1.2 Historical basis for prescription

The SPB has advised that Cabinet approved the declaration of PPAs based on justification provided by the organisations themselves with the responsible minister's support. The SPB did not express a view in relation to the proposed prescription of any public authority. Typically, the justification provided by public authorities for prescription included: being a commercial organisation and operating on a commercial basis; having effective and well-structured procurement governance arrangements; and being disadvantaged if required to comply with the SP Act and SPB policies and requirements.

The Commission has considered these historical bases and has so far concluded that, while there may be some logic in the existing arrangements, they appear to be ad hoc. The Commission has been unable to determine if these bases have been applied consistently to consider all public authorities.

¹³ Expenditure of \$500 000 or more and less than \$4 million, and all expenditure in relation to consultants.

¹⁴ Public works are compulsorily referred to Parliament's Public Works Committee if the total amount of money provided by Parliament or a state instrumentality to be applied to construction of the work will exceed \$4 million; refer *Parliamentary Committees Act 1991*, section 16A(1).

¹⁵ Department of the Premier and Cabinet Circular, *PC028 – Construction Procurement Policy Project Implementation Process*, August 2015, p. 2.

¹⁶ The PC013 Annual Reporting Template requires disclosure of contracts valued both below and above \$10 000 for consultancies and contractors.

2.2 Who are they and what do they do?

2.2.1 Characteristics of prescribed public authorities

The purpose, size and budget of the PPAs vary significantly, as does their procurement needs, expenditure, capability and associated governance arrangements. This diversity is illustrated when contrasting, for example, SA Water with the Architectural Practice Board of SA (APBSA). SA Water delivers the state's water supply and wastewater services and manages assets to deliver those services; it has substantive, dedicated and specialised procurement and contract management functions, policies, governance arrangements and systems, and an annual procurement spend in the vicinity of \$700 million per annum. Its 43 FTE of dedicated procurement professionals are generally regarded as being very capable by industry standards. In contrast, the APBSA has a total staff of 1.4 FTE and spends approximately \$20 000 annually on contracted professional services to support the Registrar to discharge its obligations to maintain industry standards and registrations under the *Architectural Practice Act 2009*. The significant differences in the PPAs' procurement arrangements suggests there must be commensurately significant differences in the rationale for excluding these organisations from the SPB's regime.

All PPAs are established under legislation or regulation. For the purposes of this inquiry, the PPAs can be broadly characterised by their statutory purpose, business, operations and procurement activity:

- Industry standards purpose: Typically, these are small organisations that oversee, regulate, investigate or support a specified industry. Their independence from the general government sector is part of their identity. Their procurement arrangements support their statutory (administrative) functions.
- Service delivery purpose: These medium- to large-sized organisations deliver services to the community, directly or indirectly, and are also substantive contributors to the state economy through their operations and procurement activity. They are all public non-financial corporations.¹⁷
- Financial services: These small- to medium-sized organisations provide industry-specific financial services or manage financial schemes on behalf of the public (or local government) sector or for the benefit of the broader state of South Australia.¹⁸ Funds SA and Return to Work SA are public financial corporations.

¹⁷ State Budget 2019–20, Budget Statement, Budget Paper 3, Appendix D.

¹⁸ The Commission acknowledges that Return to Work SA is a service-orientated organisation and that the primary purpose of the Return to Work Scheme is to provide 'South Australian employers and their workers with personalised, face-to-face services and support to achieve the best possible recovery and return to work outcomes in the event of a work injury,' see <https://www.rtwsa.com/about-us/return-to-work-scheme>.

Table 2.1: Common characteristics of prescribed public authorities

Industry standards	Service delivery	Financial services
Architectural Practice Board of South Australia	Adelaide Venue Management Corporation	Funds SA
Legal Professional Conduct Commissioner	Forestry SA	Health Services Charitable Gifts Board
Construction Industry Training Board	SA Water	Local Government Financing Authority of South Australia
	SA Housing Authority	Return to Work SA
	Renewal SA	

Source: Office of the SA Productivity Commission Assessment

2.3 Prescribed public authorities: purpose, governance and procurement activity

This section examines the PPAs’ purposes, procurement activity and associated governance arrangements to assist the Commission to understand their exempt status. The Commission has cited various examples to illustrate the issues based on PPA feedback – not all PPA’s are cited in relation to every theme. This examination also frames the Commission’s views more broadly about the characteristics and attributes that may be relevant to a prescription regime, and consequently the value of such a regime.

2.3.1 Commerciality

Most of the PPAs that are public (financial and non-financial) corporations indicated as part of the PPA Review 2018 that they operate on a commercial basis. Those PPAs have reaffirmed this to the Commission, with the most common explanation being that commerciality demands timeliness, speed, and the capacity to respond in an agile way to support business requirements. PPAs generally indicated they would miss commercial opportunities and be subject to unnecessary administrative burdens if they complied with the SPB’s regime.

This circumstance is said to require faster approaches to, and more agile responses from, the market than can be achieved under the SPB processes and policies. This can be applicable to either ongoing services that are sourced and managed understanding contracts or new goods or services from the market. Commerciality was said to be particularly important to procurement supporting building and infrastructure.

The diversity of procurement undertaken by individual PPAs and across the cohort is significant; from irregular and low-level purchasing of office consumables to multi-million-dollar capital works alliance contracts to deliver state-significant infrastructure. For example, the Adelaide Venue Management Corporation (AVMC) indicated it is a commercial hospitality-based business operating in highly competitive domestic and international markets. AVMC exemplified the commerciality of its procurement activity, having regard to

its need to obtain event-related equipment to support a series of events that had been recently secured and were to commence within six months. Opportunities to attract local and international entertainment were said to require significant procurement-related flexibility. Another example cited by AVMC was the requirement for its contracted food and beverage suppliers to meet potentially high demand at short notice while maintaining a high-quality product in support of its event and function business. The requirement to maintain the highest quality food and beverage products stems from AVMC's role in showcasing local South Australian produce, in turn supporting local SA businesses.

SA Housing Authority (SAHA) indicated speed is essential to its trading, buying, selling and redeveloping property. SAHA needs to be responsive to uncertainty. If a procurement or construction plan changes unforeseeably, SAHA needs to be able to respond quickly. For example, if asbestos were found as part of a redevelopment this matter needs to be dealt with swiftly and effectively. SAHA uses its own panel of suppliers to respond to these types of issues as, in its view, suppliers on whole-of-government panels do not demonstrate the flexibility and responsiveness required.

Commerciality is recognised in several of the PPAs' establishing legislation, creating a statutory obligation for PPAs to operate in a commercial way.

SA Water is required to operate in a commercial and competitive manner and ensure that only efficient costs are recovered through customer pricing pursuant to its obligations under the *Public Corporations Act 1993* and *Water Industry Act 2012*. SA Water is also subject to regulation by the Essential Services Commission of South Australia (ESCOSA), which issues water sewerage service retail licences, sets minimum standards to protect consumers, and provides price determinations to ensure fair and reasonable service costs. SA Water's business and asset management plans, and its governance arrangements are reviewed by ESCOSA each four-year regulatory period.

For Funds SA, the *Superannuation Funds Management Corporation of South Australia Act 1995* prescribes that the corporation must invest and manage public funds subject to performance plans, which include target rates of return. It is the Commission's view that achieving these outcomes is intrinsically linked to the effectiveness of the (contractual) arrangements that regulate the relationship between Funds SA and its fund managers (70 relationships at the time of writing).

The *South Australian Forestry Corporation Act 2000* provides Forestry SA to be a business enterprise with the principal responsibilities being to manage state-owned plantation forests to the benefit of the people and economy of the state, manage plantation forests for other forest owners and pursue its strategic commercial directions.

The nature of Renewal SA's activities requires it to operate commercially to achieve its functions under the *Urban Renewal Act 1995*.

Public (financial and non-financial) corporations can be required to pay government dividends, income tax equivalent payments and guarantee fees. Dividends are recorded as revenues of the general government sector. Income tax equivalent payments and guarantee fees are paid to meet competitive neutrality principles under the Competition Principles

Agreement. 'Government is estimated to receive a net contribution from SA Water in 2018–19 of \$104.9 million'.¹⁹

2.3.1.1 The Commission's view

Commerciality is a broad and ambiguous reference that is variously defined as relating to commerce, trade, business and profit, among other things. Despite this, it is clear that some PPAs operate, to varying degrees, in a commercial environment where their ability to source goods or services from the market flexibly and quickly is an important part of meeting statutory obligations and supporting business requirements. However, not all PPAs made it clear to the Commission the specific disadvantages that would adversely impact on the organisation's ability to act quickly and flexibly if PPAs were required to comply with the SPB regime.

Currently, if PPAs were subject to the SPB regime, timeliness concerns would relate mainly to the requirement to seek approval from the SPB to conduct procurement activity in excess of the organisation's procurement authority.²⁰ It is difficult to predict the extent of any potential net administrative burden, delay or missed opportunities if PPAs were required to seek SPB approval as this would require consideration of a variety of factors, most prominently the procurement authority (tier) that would apply to the organisation, and the frequency of procurement activity the organisation may conduct in excess of its procurement authority. In principle, amendments to existing tier thresholds and broader changes to the level of autonomy held by chief executives could also minimise any potential burden on the current PPAs if they complied with the applicable SPB arrangements.

The Commission acknowledges that participating in the SPB accreditation and assurance programs that determine an organisation's procurement authority is a cost that does not currently apply to PPAs. Other potential costs and time implications arising from complying with the wider SPB regime, such as reporting and using mandated processes and documentation, are canvassed later in this chapter.

Although not operating on a commercial basis, the group of PPAs characterised as 'industry standards' are necessarily independent from the industries which they regulate and support. These organisations require both perceived and real independence to meet their statutory functions and purpose. However, given their generally modest and confined procurement needs, and the absence of the commerciality considerations evident in the operations of PPA corporations, it is not clear that exemption from the SPB regime is required to maintain that independence. A more pertinent consideration is the net benefit to them of compliance.

2.3.2 Risk

Each of the PPAs manages procurement risk in a way that reflects its respective business and associated risks. Several PPAs take a risk-based approach to procurement.

SA Water's risk-based approach devolves the majority of business units' purchasing needs to those units by making panels available where risks have been addressed and contract terms and conditions agreed. Business units seek their own quotes and make recommendations for

¹⁹ State Budget 2019–20, Budget Statement, Budget Paper 3, Chapter 5 – Government Business, pp. 73–86.

²⁰ A procurement authority is established under the SPB's Procurement Authority and Governance Policy.

purchases to a separate trained procurement delegate. Where these panels are not in place a complexity test is undertaken to determine whether the purchase can still be made by the business unit in line with established guidelines, or is referred to the central procurement function. SA Water separates the exercise of financial and procurement delegations to mitigate against fraud and manage probity risks – a procurement delegation and a financial delegation must not be exercised by the same person in relation to the one transaction.

Funds SA's Outsourcing Policy, its primary policy relating to procurement of 'material business activities', sets out specific risks required to be considered as part of the business case and procurement, including due diligence of potential service providers and contract/agreement minimum requirements. Funds SA's approach to risk management is approved by its board and procurement risk forms part of Funds SA's 'three lines of defence' assurance model which entails three tiers of oversight: 1. Funds SA management, 2. the Governance Risk and Compliance team, and 3. internal/external audit activity and reporting.

CITB and Forestry SA apply risk assessment guides/matrices that assess risk on a category basis (e.g. economic, social, service delivery) which is applied to the acquisition process. CITB's risk management framework is consistent with ISO 31000:2018. Procurement activity is identified in the organisational risk register. These approaches demonstrate the application of organisations' corporate risk management frameworks to their procurement activity. This was a common theme across most PPAs, including the public financial corporations.

SAHA currently observes the SPB's Risk Assessment policy and uses SPB risk assessment documentation relevant to the threshold (cost) of the procurement. SAHA is currently developing its own Risk Management Policy and Procedure after acquiring housing strategy and development functions from Renewal SA effective 1 July 2018.

Return to Work SA's (RTWSA) Procurement Guideline, Procurement Process Model includes an Initial Risk Assessment and Operational Risk Model. The quantitative assessment includes weighted risk questions and calculates a risk score to create a risk profile for each procurement. This process is derived from RTWSA's Operational Risk Model. The Commission proffers that this is an example of an approach to risk management that is necessary to support the organisation's core business also being applied to its purchasing and associated contract management activity.

Most PPAs advised they have financial and procurement delegation and authorisation frameworks in place that include procurement-related delegations (e.g. capital expenditure thresholds, contract execution, consultancy engagement), and also require compliance with government policies (e.g. Treasurer's Instructions).

2.3.2.1 The Commission's view

The SPB provides risk management guidance through its Risk Management Guideline which provides a combination of general risk management advice and principles, and specific guidance about when to develop a procurement risk management plan. The SPB also offer a Risk Management Plan template for public authorities to document their procurement risk.

PPAs have different approaches to managing procurement risk, generally reflecting each organisation's management of risk having regard to its core business. Overall, the

Commission acknowledges that PPAs have risk management frameworks, policies and procedures in place that form part of the mandated requirements of their establishing legislation. Having said that, the analysis conducted by the Commission in relation to the procurement data provided by five PPAs indicated that none of them records the risk level of contracts valued at over \$220 000. Based on the feedback received to date the Commission was unable to form a collective view of the PPAs as to whether the application of their risk management policies and practices to their procurement operations is equivalent to SPB procurement risk management arrangements.

It is the Commission's view at this point that, subject to PPAs effectively applying their organisational risk management arrangements to their procurement strategies and practice, separate procurement-specific risk management policies are not necessary. The Commission has arrived at this view because it is the quality and consistency of the application of controls and oversight that mitigates and manages risk, not simply the presence of risk management policies specified for procurement purposes. Further, effective management of procurement risk is wider than managing the risk of individual acquisitions; it must be present in all aspects of procurement-related activity and the culture of the organisation. Effective contract management over the life of the contract, effective management and maintenance of panel and pre-qualification arrangements, and management of service delivery risk where applicable (i.e. fall-back supplier arrangements in the event the primary supplier fails) are all indicative of the level of sophistication of an organisation's approach to risk management.

2.3.3 Governance and audit

All of the PPAs are established under legislation or regulation. With the exception of the Legal Profession Conduct Commissioner, all of the PPAs are governed by a board. The PPAs that are public corporations must establish and maintain internal auditing arrangements and an audit committee,²¹ and have their financial statements audited by the Auditor-General.²²

In response to the PPA Review 2018, none of the PPAs indicated any adverse findings in relation to their procurement activity from the Auditor-General or any other investigations in the last five years. Some of the PPAs also shared with the Commission their operational procurement governance arrangements, and their auditing history as it relates specifically to procurement.

AVMC indicated that its procurement policy framework and controls have been tested as part of its internal audit program and by the Auditor-General. The CEO holds monthly meetings with the CFO and key AVMC staff to plan and monitor contract management and capital expenditure. Probity is managed centrally by the AVMC's Procurement and Supply Chain Manager. The Procurement and Supply Chain Manager reports to the Audit and Risk Committee on contracts that have been in place for more than five years.

Forestry SA indicated that its procurement function was reviewed in 2017 by a third party as part of an internal audit to identify improvements and efficiencies. Recommendations from that review (improvements to procurement policy and process and alignment of those

²¹ *Public Corporations Act 1993*, section 31.

²² *Ibid*, section 32.

processes with other government policy such as Treasurer's Instructions) have since been implemented.

SAHA has a central dedicated procurement function responsible for managing procurement processes valued over \$220 000, which works in collaboration with business units, including providing contract management advice on more complex matters. The SAHA Executive consider all acquisition plans over \$550 000.

Funds SA indicated that its internal auditing regime regularly reviews the appointment and termination of fund managers, which forms the basis of their investment implementation model. Funds SA described its management of these arrangements as a 'manager of managers' model, and represents Funds SA's primary procurement activity.

Like Funds SA, RTWSA noted that its Procurement Guidelines share the principles of general sector procurement, e.g. value for money, probity and professionalism, and integrity.

SA Water's procurement governance arrangements are aligned with the business's Strategic Framework. SA Water's strategic valuing of its procurement activity and its category management approach are aimed at delivering the organisation's customer-focused outcomes and reflect the regulated and commercial environment in which it operates. SA Water's procurement decision-making processes are underpinned by contemporary procurement policies and procedures, and evolved business planning and reporting processes, which the Commission has commented on elsewhere in this chapter. SA Water's governance and approvals process is subject to ESCOSA review as part of the four-year regulatory business period.²³

2.3.3.1 The Commission's view

The governance arrangements of the PPAs that are public corporations are generally determined by legislation. Operationally, their governance is akin to their approach to risk management and stems from the nature of their business operations and appetite for risk. Their management by a board, and statutory requirements to establish and maintain internal auditing arrangements and an audit committee, and have their financial statements audited by the Auditor-General necessitate effective and transparent governance arrangements. The Commission accepts the evidence seen by it that shows these obligations are taken seriously, including in relation to their procurement activities.

Similar to the Commission's observations about risk management, the key consideration is whether there is a net benefit of subjecting PPAs that have mandated, transparent and effective governance arrangements to separate procurement-specific governance and audit. In principle, the Commission does not see value in an additional authorising regime for these PPAs, or for other organisations achieving similar levels of effectiveness that are currently subject to the SPB regime.

²³ See for example Essential Services Commission of South Australia, 'SA Water regulatory determination 2020', available at: <https://www.escosa.sa.gov.au/industry/water/retail-pricing/sa-water-regulatory-determination-2020>

2.3.4 Capability

The Commission has taken a wide interpretation of capability in relation to its consideration of the PPAs from policy, people and systems perspectives.

2.3.4.1 Policy

Most of the public corporation PPAs have developed their own procurement policies, processes and documents to support market engagement, acquisition, evaluation and contract management. Some PPAs use SPB policies or variations of those policies and practices to support their procurement activity. For example, CITB has used a variation of the SPB's simple procurement template. SAHA's Procurement Procedure provides a step-by-step approach for conducting procurement activity having regard to the SPB procurement value thresholds, including the number of quotes required, acquisition and evaluation requirements, the roles of the central procurement function and business units, where other government policies apply, and the applicable templates to administer the process. The Commission notes that SAHA is going through a period of transition following machinery of government changes in July 2018 and is in the process of developing a new procurement policy.

Not all PPAs have substantive procurement-specific policies to cover all aspects of procurement activity, and the scope and detail of policies also varies. For example, Funds SA's Outsourcing Policy is structured to support its primary procurement activity – fund management services arrangements – which the Commission regards as reasonable.

RTWSA's procurement framework encompasses procurement and financial delegations, standard contractual terms and conditions, standard tools and templates including a business case template for significant procurement activity.

Most PPAs indicated that their procurement policies are consistent with general government sector (SPB) procurement principles, and the objects of the SP Act.

Some of the smaller financial corporations and industry standards PPAs procurement policies could be construed as offering general guidance and taking a principled approach rather than a prescriptive one.

SA Water's Procurement and Contract Management Procedure is well-developed and sets out the procurement process requirements for business units across SA Water. It sits under and is aligned to the organisation's corporate policy framework and is intrinsically linked to key processes conducted by the central procurement function. SA Water's procurement policies and procedures support the organisation's category management approach and are instrumental in delivering the business plan.

The Commission's view

To support transparent and auditable procurement activity, the Commission is inclined to support PPAs using SPB policies and a common set of procurement documentation templates (e.g. acquisition plans, purchase recommendations and standard contracts) for common goods and services purchasing and contract management. That would offer some modest efficiencies and support PPAs by making available to them validated processes and documentation, negating the need for them to create a suite of policies and documents for

their own business. The Commission accepts that specialised procurement activity undertaken by the financial corporations in particular necessitates additional or different approaches to ensure all of the unique requirements of that activity can be accommodated.

Where PPAs can demonstrate their policies and procurement documentation, this approach can be considered in conjunction with the Commission's views regarding uniform procurement reporting discussed in Section 4.1.

2.3.4.2 People

The larger PPAs have dedicated procurement functions with multiple staff. Some of the medium to smaller PPAs use a delegated model where they have a specialised central procurement manager who collaborates with all parts of the business to ensure effective procurement. The remaining PPAs do not possess any notable specialised procurement expertise and use their board reporting processes to validate procurement activity. Procurement-specific qualifications and experience differed significantly across the PPAs.

SA Water's category managers and other senior roles in the central procurement function hold or are completing an MCIPS qualifications (full membership of the Chartered Institute of Procurement and Supply), bachelor's degrees in business or management and/or a six-sigma qualification. SA Water's procurement capability is managed under its Corporate Capability Framework, is evaluated on an annual basis, and is structured to meet the needs of the business. The procurement function is also subject to feedback from the business units it supports across SA Water through various channels – the focus is on performance improvement.

Some PPAs with central functions or a central procurement leadership role have recruited key procurement staff from the private sector with significant and diverse industry experience. This contrasted against other PPAs that indicated their central procurement cohort do not possess any procurement-specific qualifications and relatively modest amounts of experience, e.g. an average of three years of public sector procurement experience.

In PPAs without dedicated procurement functions or roles, staff can be limited to drawing on organisational policies and processes and their own personal experience and understanding of the business. Some of the smaller PPAs indicated they have engaged third parties to assist in managing specialised procurement processes that are not regularly undertaken by the organisation or are one-off exercises.

The Commission notes differing viewpoints from public authorities regarding challenges to recruiting and retaining procurement professionals, and the experience of some of the public corporation PPAs that have recruited procurement specialists from the private sector.

The Commission's view

There is scope for most PPAs to make investments and improvements in their procurement professional cohort. The Commission notes some of the specialised market engagements and niche professional services contracts are not traditional procurements and require specialised skills and approaches. In these instances, the individual PPA should ensure that those niche skills are either developed in-house or contracted to be deployed for that purpose.

The Commission has made draft recommendations around a procurement capability strategy (see draft recommendations 3.1 and 3.2).

2.3.4.3 Systems and technology

The extent of the presence and use of technology and systems to support procurement activity was found to be as diverse as the operations of the PPAs. The Commission considered PPA feedback regarding their hardware, software and electronic processes that are used to support the efficiency of their procurement operations.

SA Water uses several systems to support its procurement operations. The Ellipse financial management system records procurement transactions, procurement and financial delegations; facilitates payments; and costs goods and services to the correct general ledger accounts. The Zycus eCatalogue system supports users to request goods and services (like an online store), and for services and non-contracted goods provides bespoke requisition forms. SA Water also uses the Rapid Global contractor management system, an online register of accredited contractors that facilitates an online corporate induction (and carding) process for contractors and subcontractors. Various Microsoft organisational-wide systems are also used to maintain and promulgate documentation and are used by the central procurement function to support supplier management and other performance-related activity.

AVMC uses a combination of dedicated event and venue management software and general Microsoft software to manage supplier agreements.

Forestry SA uses enterprise and content management systems which enable the storage of procurement documentation. Procurement (acquisition) process information is not entered separately into these systems.

RTWSA uses a number of contemporary technologies and demonstrated significant investment in data analytics as a key enabler of its business generally. RTWSA uses an electronic assessment process to determine suitability, risk, process and compliance of individual procurements. Content management software is used to manage supplier documentation and communication, and to create contracts. A contract register is maintained from content management records. RTWSA's finance system also has limited ability to interface with content management data. RTWSA indicated it continues to explore improvements to reporting and making information available across the business.

SAHA operates a Procurement and Contract Management System to record procurement activity and for contract management purposes. That system is managed by SA Health and, as it is a legacy system, SAHA is exploring future options.

Corporate records management systems and spreadsheets were cited as being used to administer and support procurement and contract activity.

The Commission's view

The use of technological solutions to support procurement activity was strongest in those organisations that are data driven and already proficient in using reporting regimes to drive decision making. Having said that, not all of those organisations appeared able to readily report on procurement-specific indicators.

2.3.5 Procurement activity

The Commission consulted with PPAs in relation to the various aspects of their procurement activity. The type of procurement undertaken, the size of the spend, reporting and performance, and continuous improvement were considered.

2.3.5.1 Type

All PPAs have varying requirements to purchase goods and services in the form of common office consumables such as stationery and IT (hardware and software), and most source professional services on a regular or semi-regular basis. The size and volume of this purchasing differs significantly. Only four of the PPAs (SAHA, Renewal SA, SA Water and AMVC) indicated they conduct construction or capital-related procurement as part of their usual business activity. Some of the financial corporations conduct niche or specialised procurement activity (e.g. engagement and management of fund managers (Funds SA) and claims managers (RTWSA)).

The Commission understands that SA Water is the only PPA to use a dedicated category management approach to its procurement. SA Water indicated that this approach, established in the corporation's Finance Policy, reflects how the marketplace is organised. The key elements of this approach are:

- end-to-end management of the supply chain in relation to a particular category;
- a strategic and proactive approach to the category;
- sound technical knowledge of the category; and
- excellent supplier and stakeholder relationships.

The category management approach places procurement strategically in the business, aligning it with SA Water's customer-focused strategy, and integrating it with its corporate policies and expansive work program. Operationally, this approach enables the category management plans that support longer-term supplier and contract management arrangements. Category management also supports effective analysis of spend, stakeholder relations and risk, among other things. Category action plans, derived from the category management plans, provide a 'licence to operate', avoiding the need for individual approvals, and provide for recommended market approach and contracting strategies.

Some PPAs indicated they do take advantage of whole-of-government contracts and panel arrangements. Examples cited included banking facilities, telecommunications, stationery, software licensing, legal services and IT services. Some PPAs indicated they use up to four of these arrangements. Examples of sourcing goods and services outside of whole-of-government arrangements included stationery and photocopiers, security, and accounting and auditing services. PPAs in general want to retain the ability to 'opt into' these arrangements where it is advantageous but believe they may be disadvantaged if they are compelled to use them.

SA Water indicated that its non-specialised goods and services purchasing is relatively small by individual market segment, and accordingly it is of the view that this presents limited opportunities to influence whole-of-government procurement strategies.

Some smaller PPAs indicated that, while they do not formally access whole-of-government arrangements, they liaise informally with other public sector organisations to identify 'good suppliers' that they then include in their market approaches or use to benchmark rates. Some of these PPAs also indicated they had previously used whole-of-government arrangements, such as the stationery contract, but found it 'cumbersome' and now purchase directly from a national supplier, achieving reduced costs and access to specialist items (e.g. certificates) that could not be supplied through the whole-of-government arrangements.

Some of the PPAs from across the spectrum of small and large organisations conveyed that they had longstanding relationships with their current suppliers, and that these relationships were important to achieving the goods and services required to support their business outcomes and ensure consistency of quality of supply. This appeared to impact the way some PPAs approach the market. One PPA indicated it regularly confines its market approaches to select suppliers with whom it has established relationships. This approach reflected the organisation's concern about having to manage higher numbers of responses from the market during the acquisition process and the increased risk of more supplier complaints.

Another PPA indicated that for higher value procurements it identifies a pool of contractors with the relevant skills. In establishing the pool, rates for similar services are compared. This organisation did indicate that its need for specialist services in specific geographical locations shaped this strategy. It also indicated that it keeps a focus on maintaining competitive tension by changing panel participants, maintaining an appropriate size of panel providers, the type of market approach used and considering whole-of-government arrangements where a benefit can be derived.

Some (mostly smaller) PPAs have standing agreements with suppliers that are evaluated on an annual basis, but this evaluation appears to be confined to the existing supplier's performance against the PPA's expectations and generally does not involve testing the market.

The Commission's view

All PPAs purchase office consumables and other common goods and services. Some PPAs undertake very specialised 'procurement' activity that does not neatly fit into the SPB procurement framework. In the absence of evidence to the contrary, it is the Commission's view that specialised procurement and contracting arrangements do not necessarily negate the potential benefits to those organisations of using whole-of-government purchasing arrangements for the common goods and services that they also purchase. The Commission supports a change in approach from the status quo, where prescribed public authorities can opt in to these arrangements, to a default use of these arrangements by PPAs unless a net detriment can be demonstrated.

The Commission accepts that for those smaller PPAs with low-value/low-risk procurement use of whole-of-government contracts can present unnecessary administrative challenges, and accordingly there may be merit in excluding them from whole-of-government opportunities.

2.3.5.2 Size of spend

Goods and services

The Commission invited 10 of the 12 PPAs to provide actual spend data for both goods and services and construction procurement for financial years 2015/16, 2016/17 and 2017/18. The Commission requested this to identify the relative size of PPAs' procurement activity over time.

PPAs' responses were provided in a variety of forms. Based on the responses it appeared to the Commission that reporting their expenditure in procurement terms was challenging for PPAs.²⁴ Based on selective follow-up enquiries by the Commission, it is understood PPAs developed their responses using their existing accounting and financial reporting arrangements which are not generally configured to report on 'procurement' expenditure as a separate category. Accordingly, the Commission has exercised caution in the conclusions it has drawn from this data.

The largest reported annual spends on goods and services were by Funds SA and SAHA, which ranged from approximately \$150m to \$250m annually. The majority of these spends relate to fund manager and custody arrangements, and the multi-trade contractors' arrangements respectively. RTWSA's annual goods and services spends ranged from approximately \$92m p.a. to \$105m p.a., two-thirds of which relates to claims agents' arrangements. This was followed by the group of AVMC, Forestry SA and Renewal SA with annual spends ranging from approximately \$11.5m p.a. to \$61m p.a. The smallest spenders were CITB, HSCGB, LGFA, LPCC and APBSA, ranging from approximately \$30 000 p.a. to \$770 000 p.a.

The total goods and services expenditure of PPAs as reported to the Commission (excluding SA Water) increased year on year and ranged between \$540 million p.a. (FY 2015/16) and \$640 million p.a. (FY 2017/18).

Construction

Of the four PPAs involved in construction procurement, SA Water is the largest. In 2018/19 the engineering and construction services spend for delivery of SA Water's infrastructure capital plan was approximately \$500 million, representing more than 70% of SA Water's total procurement spend. Approximately 95% of this spend was with 20 specialist suppliers, all of whom have developed the specific technical capabilities required for water and wastewater assets.

The remaining 30% includes some key spend categories that are also specifically related to the development and management of the state's water and wastewater networks and infrastructure. Approximately \$15 million per annum is spent on unique water and wastewater equipment (e.g. pipes, valves, pumps, water meters), along with another \$8–10m supporting a range of prescribed consumables such as pre-cast concrete products, industrial gases, water licences, and a range of instrumentation, chemicals and materials to support SA Water's Australian Water Quality Centre, which provides a comprehensive range

²⁴ The Commission used the definitions of 'goods', 'services' and 'construction' provided in the SPB Glossary of Procurement Terms in its information request with the aim of taking a consistent approach to its analysis of PPA responses.

of water and wastewater services including sampling, analysis, advice and research. SA Water's capital delivery team also manages engineering and construction services on behalf of other agencies (e.g. DEW).

The other portion of the remaining goods and services procurement spend relates to a variety of goods and services represented largely by energy and information technology.

SAHA follows with approximately \$137 million in 2017/18, with expenditure approximately half of that in FY 2016/17 and 2015/16. The Commission understands this relates to the move from Renewal SA to SAHA of the housing acquisition, development and disposal programs from 1 July 2018.

AVMC indicated that the completion of the Adelaide Convention Centre development in 2017 concluded a period of significant investment in construction-related expenditure. The typical capital expenditure for AVMC relates to venue redevelopment and was in the vicinity of \$3.4 million in FY 2016/17 and \$4.5 million in 2017/18. Examples of this include upgrades to changerooms, building fit-outs and lift installation.

Renewal SA advised its capital expenditure (excluding land purchases) was approximately \$49 million in FY 2017/18.

Reporting and procurement performance

This section provides the Commission's summary analysis of the data provided by PPAs in terms of what procurement-related information PPAs record and can report on.

Seven of the 12 PPAs were asked to provide their data – the decision to confine the Commission's request was based on the Commission's preliminary consultation with all PPAs and the prospect of the Commission being able to conduct analysis of the data available. Five PPAs provided data – not all PPAs record procurement or contract information centrally or on an organisational basis. Some smaller PPAs record and monitor basic contract information to keep track of when contracts require review or are expiring.

The Commission examined the contract data to determine which PPAs record the fields of data that are reported by public authorities to the SPB. The Commission accepts that PPAs are not required to report or maintain data in these terms. The Commission undertook this comparative analysis to generate an understanding of the extent to which PPAs record procurement information generally and chose these fields as the general government sector benchmark. The following analysis reflects only whether the data were recorded, not its accuracy, quality or value.

- The percentage of the SPB comparator fields recorded by those 5 PPAs ranged from 74 per cent to 42 per cent.
- The contract identifier, contract name, supplier name and date of contract completion were the only universally recorded fields.
- None of the 5 PPAs recorded why direction negotiation was used, the number of quotes received, or the date the acquisition plan was approved.
- Recording of ECT or IP Plan scores was very limited.

- Four of the five did not record data in relation to contract term, the number of quotes requested, or supplier location.
- Only one PPA effectively recorded the contract award date.

Most PPAs indicated they comply with other government policies that require procurement (contract) reporting, variously citing Premier and Cabinet Circulars (PC013 – Annual Reporting Requirements, PC015 – Public Works Committee Review, PC027 – Disclosure of Government Contracts, PC033 – Industry Participation Policy), and Treasurer’s Instructions (TI12 – Government Purchase Cards, TI17 – Public Sector Initiatives, TI28 – Financial Management Compliance Program).

One PPA indicated it does not report against PC027 contracts to avoid disclosing commercial-in-confidence information. SA Water is subject to variations to TI8 and TI17 to allow the board of SA Water to enter into contracts valued up to \$11 million (GST inclusive) and to proceed with public sector initiatives with a project cost of up to \$4.4 million (which may also be delegated to four nominated senior roles).

Some PPAs indicated they report procurement activity as part of their quarterly reporting to their board, but this is in the form of corporate expenses or capital expenditure rather than categorised as procurement specifically.

Some PPAs indicated they capture supplier complaints. One indicated it records this in its systems; others indicated they are managed on a contract-by-contract basis.

SA Water has developed a benefits recording process and database as part of its category management framework. Financial and non-financial benefits, from both sourcing and contract management processes, are captured, monitored and reported by SA Water’s central procurement function. Benefits are forecast from category management/action plans and are either a purchasing result (a saving against budgeted cost) or purchasing performance (increased value for money was achieved, e.g. better-quality outcome for equal or same forecast value). Benefits must be validated by a finance delegate. The benefits target has been around 5 per cent of the total addressable spend for the past three years and has been exceeded in all three years.

One PPA indicated that contracts are benchmarked, contract evaluation occurs during the contract period, and that those evaluations feed into regular assessments by the CEO to inform decision making to extend contracts or go back to the market. Key contracts are monitored for supplier performance, by using scorecards which are complemented by regular supplier meetings.

Reflecting the size and risk of their financial obligations and responsibilities, Funds SA indicated that its monitoring of its fund manager, custodian bank and asset consultant arrangements are regular, systematic and benchmarked against performance targets. Reporting is to the Funds SA Board.

RTWSA take a similar approach with detailed KPIs being used in relation to the highest value contracts (claims managers). These are monitored daily with reporting made available across the organisation, supporting ongoing communication between RTWSA’s contract managers and claims managers. RTWSA focuses reporting on the highest value/risk

components and relies on trend data from net promoter score results from employers and claimants.

Several PPAs indicated they report procurement outcomes regularly to their boards and manage KPIs for individual contracts which are determined having regard to the procurement's value, duration and risk profile.

The Commission's view

There are clearly a myriad of existing reporting and referral arrangements not specifically related to procurement that most PPAs must comply with. It is the Commission's view that there are both organisational and state-wide benefits that can be achieved by improvements to procurement reporting. Some PPAs are already monitoring and reporting on procurement expenditure or have systems in place to be able to report with minimal disruption. For others with under-developed procurement reporting any improvement in this area would be expected to give rise to organisational benefits from the consequential analytical opportunities and contribute to an improved state-wide picture of procurement and contract activity.

2.3.5.3 Continuous improvement

Feedback from most PPAs indicated that procurement continuous improvement was not a focus. SA Water was the exception in this regard. SA Water has a dedicated role (Manager Procurement Excellence and Change) responsible for ongoing and continuous review and improvement of the organisation's procurement activity. The Procurement Leadership Group at SA Water reviews the quality management system at regular intervals. This process is aimed at ensuring 'the right things are being done at the right time for the right cost' and evaluates the effectiveness of both the business units and the central procurement function. The reviews are data-driven and can be subject to independent examination.

Although not all PPAs have a continuous improvement process specifically for procurement, most indicated that continuous improvement is part of the organisation's general business planning review process, which may include purchasing arrangements. A few PPAs indicated that improvements have been made because of their audit and associated reporting processes. These improvements included, for example, aligning organisational procurement process with other government policy.

One PPA indicated it mandates reviews of its procurement framework at least every three years, or otherwise in response to changes in business operations, legislative change or whole-of-government requirements.

Employee feedback arising from staff workshops is informing reform at one PPA, which will canvass automated workflows and simplification of documentation. Previous changes at the same organisation included adopting risk-based approaches, and a minimum standards approach giving rise to a 65 per cent reduction in documentation. Another has developed standardised templates to support acquisition and evaluation activity, and contract reviews. It is not clear to what extent this PPA drew on relevant SPB documentation.

One PPA indicated a very large contract had been reviewed independently, the results of which will inform the next procurement process.

One PPA indicated that feedback from a national regulator had resulted in an improvement in their evaluation process.

The Commission's View

With the exception of SA Water, continuous improvement of procurement arrangements did not appear to be systematically pursued. The Commission sees merit in broader attention to continuous improvement, while noting several examples of PPAs engaging in external reviews that led to improvements or adopting recommendations arising from mandated auditing activity.

2.4 Prescribed public authorities: preferences and priorities

PPAs were invited to indicate to the Commission their views on system design; namely:

- what criteria were most important in the procurement process;
- what parts of their procurement arrangements align with the SPB; and
- what procurement-related flexibility and autonomy attributes are most important to them.

The Commission invited these responses to be able to distinguish the specific and necessary procurement requirements sought by PPAs from general preferences to remain 'outside' the general government procurement framework. The issues raised by PPAs go to the core value of a prescription regime and may also offer signals for improved procurement practice to apply more broadly to all public authorities.

2.4.1 Organisational responsiveness

Commerciality was explored earlier in this chapter. Examples of organisational responsiveness included the ability to secure quantities of goods at short notice prior to price hikes, being competitive in national and international markets, and short timeframes from the identification of an organisational need to awarding a contract. Limited market suppliers able to provide the specialist services required was also cited.

The Commission understands corporations are driven by commercial outcomes and are legislatively bound to act commercially. These drivers are distinguishable from public sector agencies (public authorities) and make public corporations more attuned to removing process steps that do not add value, including procurement processes.

2.4.2 Alignment with SPB policy and process

The Commission observed that several PPAs indicated, albeit to varying degrees, that they:

- observe the objects of the SP Act;
- use SPB policies and documentation (or variations thereof);
- have opted in to whole-of-government contracts or approached those suppliers on the recommendation of public authorities;
- undertake risk assessments of proposed procurement activity;

- use evaluation panels;
- engage third-party specialists to assist with evaluations where required; and
- have financial and procurement delegation arrangements in place.

The PPAs that do not already align their procurement policies and practice with SPB arrangements raised the potential compliance costs and resource implications of doing so.

2.4.3 Use of whole-of-government contracts

Several PPAs indicated they want to retain the flexibility to opt in where it is viable and provides an advantage to the organisation but wish to avoid the disadvantages of being required to use such arrangements.

2.4.4 Limited procurement requirements

Smaller PPAs and those whose primary procurement expenditure was for specialised or niche services generally considered a requirement to use whole-of-government contracts and/or SPB policies and practices would create inefficiencies.

For smaller low-value/low-risk purchasing, using SPB policies and whole-of-government contracts was cumbersome and created administrative inefficiencies compared to direct purchasing.

For specialised procurements, most notably Funds SA's fund manager role and associated arrangements and RTWSA's claim manager arrangements, SPB procedure lacks the nuance and flexibility to manage those processes effectively.

2.4.5 Existing oversight is appropriate

All but one of the PPAs are governed by a board with audit and risk committees, and the corporations are subject to mandatory internal and external auditing arrangements. The general view of these PPAs was that additional oversight or the requirement to seek authorisations from a central government procurement function was unnecessary and would create additional cost and time burdens.

Some feedback indicated that the experience of board members was more than sufficient to manage and oversee organisations' procurement arrangements, and the boards often included industry or technical specialists with experience in the PPAs' core business. Instances of procurement-related policies and practices being reviewed and improved based on board feedback were cited.

The Commission has commented on governance and auditing in Section 2.3.3.

2.5 Review of prescribed public authorities, 2018

The PPA Review 2018 was undertaken as part of the government's election commitments.²⁵ The then Chief Procurement Officer wrote to each of the PPAs and invited them to indicate whether:

- they are still satisfied the historical bases for prescription continue to apply (referred to as 'criteria');
- there are 'governance frameworks and mechanisms in place to support the intent and the object of the Act';
- the organisation had 'any significant issues relating to the procurement function in the past five years, including Auditor-General's findings, other investigations or significant supplier complaints, and a brief description of the outcome; and
- the PPA 'considers it appropriate to remain a prescribed public authority, with supporting justification provided'.

The historical bases for prescription²⁶ were identified as:

- operating as a commercial enterprise and on a commercial basis;
- effective, well-structured internal procurement governance and operations; and
- would be disadvantaged if required to comply with the Act (and apply SPB policies).

All PPAs responded at the time, seeking to retain their prescribed status. Their reasons varied but common themes included:

- additional administrative burdens would apply if they were required to comply with the SPB's policies, particularly for smaller PPAs;
- loss of the flexibility and agility required to optimise commercial opportunities;
- having appropriate capability, policy and systems to manage its procurement activity; and
- having substantial and effective governance arrangements in place that also apply to procurement activity, with no PPAs reporting any adverse findings by the Auditor-General or third parties about procurement in the last five years.

This response was, in the Commission's view, unsurprising. The Commission understands the SPB considered the outcomes of the PPA Review 2018 and formed the view that there were no compelling reasons why these organisations should not be subject to the SP Act to facilitate greater consistency in the process for procurement operations. The Commission also notes the SPB did not further progress that review pending the outcome of this inquiry.

²⁵ Government Procurement, Maximising the Benefits 2036, 'Reviewing prescribed public authorities' status', available at: https://d3n8a8pro7vnm.cloudfront.net/liberalpartyofaustralia/pages/4840/attachments/original/1510881056/2036_Chapter_9_Government_Procurement.pdf?1510881056

²⁶ Sourced from Chief Procurement Officer (CPO) letters sent to PPAs in June 2018, provided to OSAPC by SPB; see also minute from CPO to SPB re outcome of 2018 PPA Review.

2.6 The value of prescribed status

The Commission has formed the following draft conclusions based on its assessment of PPA feedback and the PPA Review 2018:

- Current prescription is based historically on ministers' and chief executives' views. The Commission has received very little information pertaining to the original reasons for prescribing the current PPAs. There are a variety of other commercial public entities that are currently not prescribed.
- All PPAs share the view that to be subject to the SP Act would create administrative burdens and may result in lost commercial opportunities, potentially causing some PPAs to compromise their statutory and business obligations and outcomes.
- Not all PPAs provided specific examples of how compliance with the SP Act and SPB regime would compromise those obligations and outcomes. However, the Commission accepts that complex and specialised procurement activity is undertaken by some PPAs, and they need to exercise timely and flexible procurement arrangements to do their work. Some are also required by law, or subject to a regulatory regime, to act commercially.
- All PPAs purchase some common goods and services, implying benefits from using whole-of-government contracts, particularly where they may benefit from category purchasing, e.g. stationery and IT goods and services. However, where such purchasing is confined to very low-spend/low-risk purchasing a risk-based approach and direct purchasing may be appropriate where it is expeditious and ensures fit-for-purpose outcomes.
- PPAs generally observe the objects of the SP Act in their procurement frameworks and practices. Some PPAs use SPB documentation or variations of it and base their policies on SPB arrangements. Some also draw on the experience of public authorities who use of whole-of-government contracts and panel suppliers to inform their own market engagement and acquisition decisions and processes.
- There is a wide divergence in human capability across PPA procurement functions. The size and professionalism of SA Water's central procurement is unrivalled and represents the organisation's integration of procurement and contract management into the core business. The size and capability of SA Water's procurement function will not be appropriate for all public authorities. Some PPAs have adopted a devolved system where procurement is managed and monitored organisationally by a central function or central role. For others, business units are responsible for their own purchasing. There is scope to improve the capability of those conducting procurement in most PPAs; the nature of that improvement requires case-by-case analysis of each PPA's existing capability and procurement needs. The Commission acknowledges that, for those PPAs with very small and low-risk procurement needs, specific investment in procurement capability is not warranted.
- Most PPAs manage procurement risk and governance as part of their organisational approaches and models. PPAs undertaking specialised or niche procurement activity

have developed policies and practices to manage those specific risks. Some PPAs have adopted the SPB's risk management policies and documentation.

- No PPAs have reported any adverse findings by the Auditor-General or third parties in relation to procurement activity in the last five years.

2.7 Proposed reform

The Commission's preliminary view, based on the above draft conclusions, is that the current prescription regime:

- has not been universally or consistently applied;
- does not use a process of systematic evaluation to determine whether an organisation should be prescribed; and
- is of a binary nature (i.e. organisations are either prescribed or not), and therefore lacks the flexibility to balance organisational autonomy and efficiency to achieve commercial outcomes, with the potential for state-wide benefits or individual organisational benefits derived from using state-wide procurement arrangements.

The Commission is canvassing options which would see the adoption of a principles-based approach to procurement in the context of a single, state-wide system. This approach increases the extent to which all entities of the Crown are incorporated into the state-wide procurement system but will also continue to support the commercial drivers (statutory and business) of the relatively small number of organisations who operate in a commercial environment in the form of a small number of business-based distinctions.

The Commission envisages this option would require establishment of an evidence-based evaluation framework involving both quantitative and qualitative assessments of procurement needs, capability, risks, and governance and auditing arrangements. Based on these independent assessments, organisations could be distinguished and allocated to an appropriate special group.

This approach should be considered in the context of the Commission's wider vision for the future of state procurement, in particular recommendations that support improved value for money, consistent and transparent procurement reporting, and a category management approach.

To avoid the loss of the commercial benefits required by the PPAs in moving away from an exemption regime, and to minimise any potential administrative burden, the Commission is inclined, subject to further refinement after further consultation with stakeholders, to propose a sequenced reform of the prescription regime in the broad stages set out below.

2.7.1 Step 1: PPAs form part of state procurement reporting arrangements

In this step all current PPAs will commence reporting to the central government procurement function. For those PPAs with existing procurement-related reporting in place or other existing reporting capacity minimal disruption is expected. For those PPAs with under-developed procurement reporting, it is expected that they would derive organisational benefits from the consequential analytical opportunities.

This approach is broadly consistent with the direction of the Victorian Government Purchasing Board (VGBP) which requires its 'mandated entities'²⁷ to report on exceptions to policy compliance. The Commission notes that VGBP is also trialling a 'spend cube' that categorises and reports on goods and services procurement.

Consideration will need to be given to the costs to individual PPAs arising from this reform, particularly the extent to which it may impact on small authorities.

No other changes are proposed to apply to PPAs at this stage.

2.7.2 Step 2: State-wide system reforms – PPA contribution

Whilst the other reforms arising from the Commission's recommendations are being implemented, the Commission is inclined to recommend that no significant changes are implemented in relation to PPAs' procurement arrangements.

From the perspective of the central government procurement function, this stage may be an opportunity for PPAs to contribute to the process of reform by sharing best practice, increasing capability and improving the commerciality of general government sector procurement policies and practice.

The Commission envisages that the simplification of policy arising from the state-wide procurement reforms will meet the commercial needs identified by the PPAs. These changes would benefit all public authorities and may disproportionately benefit those statutory authorities and commercial or semi-commercial entities of the Crown that are currently subject to the SP Act and SPB regime.

2.7.3 Step 3: Transitioning

At the next stage of the implementation of state-wide reforms, the Commission proposes that PPAs be selectively transitioned into a single state-wide procurement system.

The Commission notes that this transition process could be done under the existing powers under the SP Act, namely:

12—Functions of Board

(1) The Board has the following functions:

(a) ...

...

(i) to carry out the Board's functions in relation to prescribed public authorities and any other functions assigned to the Board under this Act.

18—Undertaking or arranging procurement operations for prescribed public authorities and other bodies

²⁷ 'Mandated entities' are departments and other agencies required to comply with the VGBP policy framework. Work is underway to expand the number of mandated entities and to harmonise construction and goods and services procurement frameworks.

The Board may, with the approval of the Minister, undertake or make arrangements for procurement operations for—

(a) a prescribed public authority; or

(b) a body other than a public authority or prescribed public authority.

19—Public authorities bound by directions etc of Board and responsible Minister

(1) A public authority (including every member or officer of the authority) is bound to comply with—

(a) any applicable policies, principles, guidelines, standards or directions issued or given by the Board; and

(b) any directions given by the responsible Minister on the advice or recommendation of the Board.

(2) A prescribed public authority (including every member or officer of the authority) is bound to comply with any directions given by the responsible Minister on the advice or recommendation of the Board.

These provisions would enable the responsible minister and SPB to develop transitional arrangements to gradually move PPAs into the state-wide system.

2.7.4 Stage 4: A single system

PPAs will be individually transitioned into the single state-wide system subject to their individual readiness and having regard to the implementation of state-wide procurement reforms.

Consequent on effective transition to the state-wide procurement framework PPAs will be removed from Schedule 1 of the SP Regs.

The Commission proposes this process begin with draft recommendation 2.1.

Draft recommendation 2.1

To support the transition to state-wide category management and improve value for money, the Commission proposes that:

- Prescribed public authorities (PPAs) should adopt relevant whole-of-government goods and services arrangements for their common purchases unless their current arrangements achieve superior administrative efficiencies and economic benefits.
- PPAs with low-spend/low-risk purchasing of common goods and services, or where unique products cannot be sourced from those arrangements, should be excluded from the requirement to consider whole-of-government common goods and services arrangements.

3. Construction

3.1 Background

The terms of reference for Stage 2 of the Inquiry into Government Procurement widened the Commission's remit and now includes consideration of construction expenditure. As part of the Stage 2 inquiry, the Commission has consulted extensively with all relevant public authorities and interested stakeholders. In addition, the Commission has consulted with other Australian jurisdictions regarding their procurement strategies for construction and reviewed other relevant information about practice in selected overseas jurisdictions.

This chapter provides some background on construction procurement by public authorities and considers the specific issues associated with this category of procurement.

3.1.1 What is 'construction' for the purposes of this procurement inquiry?

The definition of 'construction procurement' for the purposes of the SAPC inquiry is the definition of procurement associated with a 'prescribed construction project' as provided in the *State Procurement Regulations 2005*:

- (2) *A prescribed construction project—*
- (a) is a project that primarily involves the procurement of construction work; and*
 - (b) encompasses—*
 - (i) the acquisition and installation of fixtures, plant, equipment, appliances and fittings in conjunction with the construction work; and*
 - (ii) the acquisition of survey, planning, design and other services in conjunction with the construction work; and*
 - (c) does not encompass the acquisition of goods and services for the ongoing maintenance of a building or structure.*
- (3) *In this regulation—*
- building work has the same meaning as in the Building Work Contractors Act 1995;*
- construction work means—*
- (a) building work; or*
 - (b) the whole or part of the work of excavating or filling of land not constituting building work;*
- Treasurer's instructions means instructions issued by the Treasurer under Part 4 of the Public Finance and Audit Act 1987.*

The exclusion of prescribed construction projects from the *State Procurement Act 2004* (SP Act) effectively means that construction procurement valued over \$150 000 (excluding GST) does not come under the scope of the SP Act or the associated State Procurement Board (SPB) procurement policy framework.

It is important to note that, for the purposes of this inquiry, although the term ‘capital’ may be used instead of ‘construction’ in this report, it is taken as having the same meaning as that provided above.

3.1.2 Value and volume of contracts and spend

3.1.2.1 Construction procurement spend

The Commission sought information from public authorities whose construction procurement activity was significant.²⁸ Six public authorities were asked to provide their procurement spend on prescribed construction activity which includes spend where the authority was the lead agency for the project, or had sole responsibility for the project. A summary of the information provided for two financial years is in Table 3.1. In response to the Commission’s request for DPTI’s annual procurement expenditure for construction procurement valued over \$150 000 (GST exclusive) for the past three years, DPTI advised the Commission that spend can vary significantly but inclusive of building projects can range from \$500 million to \$1.5 billion per year.

Table 3.1: Construction procurement spend on prescribed construction activity

Agency	2016–17	2017–18	Total
Department of Human Services	\$644,000	\$980,000	\$1,624,000
Department for Education	\$49,747,000	\$215,329,000	\$301,274,000
Department for Health and Wellbeing	\$326,574,000	\$266,899,000	\$838,071,000
Department for Environment and Water	\$13,566,101	\$9,889,464	\$23,455,565
Department of the Premier and Cabinet	\$20,617,039	\$72,419,792	\$101,534,705

Source: SAPC consolidated data provided on request by public authorities

3.1.2.2 Contract value and volume

The Commission has used two data sources to obtain information on contracts and on tenders for the inquiry:

- information obtained via the database for the SA Tenders and Contracts website where public authorities disclose awarded contracts (as per Premier and Cabinet Circular 27 or PC027) and advertise tenders; and
- data provided by public authorities and PPAs on request to the Commission.

²⁸ The Commission undertook a desktop analysis of tender information on SA Tenders and budget statements to obtain an indication of public authority construction procurement activity.

3.1.2.3 Commission data

In order to undertake quantitative analysis of the current PPAs and capital project related supplier selection process to the same extent as was undertaken in Stage 1, the Commission requested that:

- all PPAs provide their procurement database (except for the authorities for which procurement spend and/or FTE numbers were low: Architectural Practice SA, Construction Industry Training Board, Health Services Charitable Gifts, Legal Profession Conduct, Local Government Finance SA and the Motor Accident Commission, which is being wound up);
- DPTI provide its database for all capital projects valued above \$150 000 (excl. GST) undertaken for DPTI or on behalf of other agencies (contract executed between 2015 and 2018, exclusive of secondary purchasing from panel arrangements, inclusive of major projects);
- all other government agencies with a total capital investment spend above \$50 million for either 2017–18 or 2018–19 (except the Department of Energy and Mining whose capital spend mostly comprises grants) provide their database for all capital projects valued above \$150 000 (excl. GST) not undertaken by DPTI on their behalf.

The list of fields requested was based on a selection of fields from the SPB database, with the addition of three fields (number of quotes received, variation to the contract and capping of liability). Those fields were chosen to allow comparison with Stage 1 of the inquiry, and to specifically address some of the construction issues raised with the Commission.

Authorities were asked to provide the data related to all contracts executed between 2015 and 2018, exclusive of secondary purchasing from panel arrangements and inclusive of major projects. The Commission consolidated this information into a single database for analytical purposes.

Those authorities were also asked to provide a random sample of purchase evaluations for capital projects valued above \$150 000 (excl. GST), for the Commission to undertake analysis in greater detail, as was done in Stage 1. This is discussed in Section 5.2.3.

3.1.2.4 Results

Quality of the data

The Commission found the availability of data to vary significantly (see Table 4.1). It is important to note that this does not necessarily mean that the data are not collected or recorded, but rather that the data are not readily available in a consolidated format and required a significant amount of work to assemble. Seven out of nine agencies found it onerous to provide the information requested and required extensions to provide the information. This suggests that the information is difficult to extract from the repositories in which it is kept. This is consistent with the Commission's observations about data limitations in Stage 1.

It is also important to note that a lot of the data are recorded partially (e.g. only 6 per cent of contracts have a date recorded in the 'Date tender close' field) and/or required cleansing.

The areas for which little information is recorded centrally in public authorities (in number or usability) are:

- the ECT or IP Plans scores;
- the location of suppliers;
- the reasons for use of direct negotiation;
- the number of quotes requested and received;
- data on timeliness.

The fields recorded by most agencies are:

- name of the contract;
- supplier's name;
- category (goods, services, construction); however the data is highly inconsistent between agencies;
- market approach; however the data is highly inconsistent between authorities;
- contract value.

It is also clear that there is a lot of duplication in the entry of the same data for authorities, and limited or no linking of databases, including:

- own agency system;
- SPB database for goods and services for non-prescribed public agencies;
- SA Tender website for 'pipeline of work' and 'tender and contract information';
- OIA reporting for construction and prescribed public authorities.

3.1.3 Governance arrangements: how is the spend managed?

3.1.3.1 Regulatory environment for construction procurement

Regulation for all government procurement

Public and prescribed authorities are required to comply with the following policies and legislative instruments irrespective of whether the procurement is for goods and services or for construction activities.

Table 3.2: Regulation applying to goods, services and construction procurement

Regulation applying to goods, services & construction procurement	
Treasurer’s Instructions	
TI 8 Financial Authorisations	Specifies the conditions and requirements for financial authorisations based on specified thresholds to enable authorities to enter into a contract, make a payment and vary a contract.
TI 12 Government Purchase Cards	Specifies chief executives’ responsibilities for authorisation and use of purchase cards to specific threshold limits.
TI 17 Evaluation and Approvals to Proceed with Public Sector Initiatives	Requires the chief executive to evaluate public sector regulatory initiatives in line with the Better Regulation Handbook (including capital projects) and obtain appropriate approvals to proceed with initiatives.
TI 28 Financial Management Compliance Program	Specifies chief executives’ responsibilities for ensuring contractor/supplier performance and payment reductions for supplier failure.
Premier and Cabinet Circulars	
PC027 Disclosure of Government Contracts	Requires chief executives to ensure all ‘eligible’ and ‘significant’ contracts are disclosed on the SA Tenders and Contracts website within 60 days of contract execution (sign off).
PC013 Annual Reporting	Requires chief executives to include details on consultants and contractors engaged during the financial year in agency published annual reports.
PC033 Industry Participation Plan	Applicable to all government procurements by all agencies valued above \$33 000.
PC038 Unsolicited Proposals	Provides a framework and process for the assessment of unsolicited proposals.
South Australian Industry Participation Policy (SAIPP)	Supports PC033 and provides a high-level framework to deliver the requirements of section 4 of the <i>Industry Advocate Act 2017</i> .
SA Aboriginal Economic Participation Strategy	Focuses on leveraging opportunities for Aboriginal employment and business enterprise from government procurement, building the capability of the Aboriginal business sector to compete for government and private sector tenders, and creating increased opportunities for Aboriginal employment.
International obligations	The SA Government is a signatory to, or has agreed to comply with, various free trade and government procurement agreements that include procurement obligations or ‘rules’ that

Regulation applying to goods, services & construction procurement	
	must be complied with for those procurements that are within scope.
Skilling South Australia Procurement Guideline	Replaces the Workforce Participation in Government Construction Procurement Policy for projects over \$50m and focusing on apprentices and trainees accounting for 15% of labour hours.

Source: SAPC analysis

Regulation specific to construction procurement

There are three arrangements or frameworks that govern the procurement of South Australian Government construction projects:

- SPB’s procurement policy framework as per the SP Act applies to the procurement of construction valued at \$150 000 (GST exclusive) or less. PPAs are excluded from the framework.
- The Construction Procurement Policy: Project Implementation Process applies to all ‘prescribed construction projects’. Prescribed construction projects are those construction procurement projects that are prescribed from the SP framework by regulation (and valued over \$150 000). Under the policy, DPTI is responsible for the management of construction projects in the civil and non-residential (commercial) construction sectors. PPAs are exempt from this policy.
- PPAs have their own policies and guidance for procurement activity which may include procurement relating to construction projects (irrespective of value). Detailed discussion on PPA activity is provided in Chapter 2 of this draft report.

In addition to the above, all public authorities (prescribed included) are required to comply with PC015 Procedures for Submissions to Cabinet Seeking the Review of Public Works by the Public Works Committee (PWC). Section 16A of the *Parliamentary Committees Act 1991* requires that public works are compulsorily referred to the PWC if the total amount of money provided by Parliament or a state instrumentality to be applied to construction of the work exceeds \$4 million. No public monies can be expended on the actual construction of the work until the PWC has presented its final report.

Construction Procurement Policy: Project Implementation Process

PC028 states ‘*Cabinet has approved that the Minister for Transport and Infrastructure²⁹ supported by the Department of Planning, Transport and Infrastructure (DPTI) has responsibility for construction policy development and implementation in South Australia*’ (PC028, p. 2).

That circular refers to the Construction Procurement Policy: Project Implementation Process (PIP), which is administered by DPTI and is applicable to all public authorities (excluding PPAs) to every ‘prescribed construction project’ (valued over \$150 000 excluding GST).

²⁹ The Commission notes that PC028 has not been updated to reflect the change in portfolio for the Minister to the Minister for Transport, Infrastructure and Local Government.

Key roles and responsibilities

The PiP explains the following key roles and responsibilities:

- Lead Agency – a public sector agency responsible and accountable for the construction project as its sponsor and funder. The lead agency is responsible for aligning project planning with the state’s strategic priorities, and for effective development of business cases for specific projects or programs. They are required to work with DPTI during construction project delivery, utilising and not duplicating DPTI expertise.
- Lead minister (of the Crown) – a person appointed by (or under the authority of), the sovereign or executive head of a government to a high office of state who is the minister of the lead agency funding the project.
- Infrastructure agency – the public sector agency responsible and accountable for implementing policies, guidelines and processes for construction procurement. The infrastructure agency is DPTI, which provides centralised expertise in construction procurement and construction industry interface and required systems and processes for effective procurement of prescribed construction projects. Under the policy, DPTI is responsible for the management of construction projects in the civil and building (commercial) construction sectors.

Other roles related to construction procurement include:

- Department of Treasury and Finance (DTF) – provides advice on financial and budgetary aspects of projects;
- Infrastructure SA – provides independent advice to government on infrastructure planning, investment, delivery and optimisation;
- Office for Design and Architecture SA (ODASA) – led by the SA Government Architect, it provides advice on design, architecture and urban design for major projects, programs and guidelines;
- Department for Environment and Water (DEW) – manages Crown land and provides advice on sustainability, climate change and conservation issues;
- Office of the Industry Advocate (OIA) – administers the SAIPP.

Process

The five-step Infrastructure Planning and Delivery Framework is aimed at providing strategic planning for construction projects and includes a number of ‘gateway’ approvals. The Project Implementation Process or PiP integrates with the framework at the completion of step 4 (approval provided via gateway four for project funding method) and provides detailed guidance to implement step 5 (delivery of the project). Step 5 is essentially the PiP and involves six phases and three further gateway approvals.

Figure 3.1: Extract from the Construction Procurement Policy showing integration with the 5-Step Framework

5-Step Infrastructure Planning and Delivery Framework	Step 1	Strategic analysis and identification of infrastructure needs Gateway One – Strategic infrastructure priorities approved by Government.	
	Step 2	Outline of case for change and project scoping Gateway Two – Project defined for investigation and development of business case.	
		Project planning and substantiation – leading to a full business case Gateway Three – Project substantiated and business case completed.	
	Step 4	Project funding method and resource allocation Gateway Four – Funding model agreed, project included in an approved government program and a decision made to proceed to Step 5: Delivery of the Project.	
	Integration	Step 5	Delivery of the Project
	Project Implementation Process	5.1	Concept Gateway Five Approval Approval that the project developed during the 5.1 Concept phase of the Project Implementation Process is consistent ⁵ with the parameters approved by Government in regard to project scope, quality, budget and program. Approval to commit expenditure required to progress Design, Documentation and Tender phases.
		5.2	Design
5.3		Documentation Gateway Six Approval Approval that the project developed during the 5.2 Design and 5.3 Documentation phases of the Project Implementation Process is consistent ⁵ with the parameters approved by Government in regard to project scope, quality, budget and program. Approval to call tenders and commit to the market.	
5.4		Tender Gateway Seven Approval Approval that the project tendered during the 5.4 Tender phase of the Project Implementation Process is consistent ⁵ with the parameters approved by Government in regard to project scope, quality, budget and program. Approval to proceed to construction by committing the balance of the project expenditure and awarding construction contracts.	
5.5		Construction	
5.6		Review	

Source: Construction Procurement Policy Project Implementation Process, p. 24, available at: https://www.dpti.sa.gov.au/_data/assets/pdf_file/0005/157838/Construction_Procurement_Policy_-_Project_Implementation_Process_2015_po38.pdf

DPTI advises that although there are process similarities between civil construction and building construction procurements, there are differences because DPTI delivers civil construction itself, compared to building infrastructure which it delivers for and on behalf of Lead Agencies (as clients). As a consequence, references to the role and responsibilities of Lead Agencies in the PiP do not apply to civil construction projects. The Commission notes that:

- building construction projects are undertaken in accordance with PCO28 and the PiP process outlined above with Lead Agencies managing steps 1 to 4, and DPTI managing step 5; and
- civil construction projects are undertaken via an Infrastructure Planning and Delivery Framework with DPTI’s 3PMO (program management office) responsible for steps 1

to 4, and the Procurement and Contracting Directorate responsible for the procurement process.

Governance arrangements for construction procurement

Construction procurement governance in DPTI

As the result of a procurement governance review, DPTI amalgamated the Procurement Committee and the Construction Procurement Committee in 2015. The Procurement Committee is chaired by the Executive Director People and Corporate Services Chief Corporate Officer and includes representation from across DPTI. The committee is accountable to the Chief Executive for the effective governance of the procurement of goods, services and construction. According to the committee's terms of reference regarding construction procurement projects its roles are:

- for projects designated as 'HVRCO'³⁰ (high value/high risk/high complexity or high opportunity for change procurements), review draft procurement strategies and approve procurement strategies and calling of tenders;
- on request, approve contract management plans and/or purchase recommendations;
- review the performance of strategic contracts on a quarterly basis, review the performance of DPTI prequalification schemes biannually, and approve proposals to remove prequalified contractors from prequalification schemes.

The Commission notes that:

- DPTI has advised that procurement projects (including construction) require approval from the DPTI Procurement Committee depending on value and complexity. It is not clear if this is consistent with the committee's responsibilities as outlined in its terms of reference; and
- The committee's terms of reference state that its membership includes private sector representatives (1 to 2 members); however it currently has no private sector representation.

Figure 3.2 demonstrates how DPTI categorises programs and projects to ensure the correct level of governance is applied using financial and non-financial elements.

30

DPTI advises that a project is designated as 'HVRCO' by the Director, Procurement and Contracting Directorate based on an assessment of the risk consequence as 'major' or 'critical' in accordance with DPTI's Risk Management Policy (DP086).

Figure 3.2: Financial categories applied by DPTI



Source: DPTI Project Management Framework, DPTI intranet.

Non-financial categories based on key contributors to risk include:

- strategic visibility – political priority, community imperative, strategic/policy timing and input to state objectives;
- budget value – benefit–cost ratios, economic, social, safety and environmental factors, input to departmental objectives; and
- investment risk – considers governance risk (procurement model, client risk, funding model and cross-division management), plus delivery risk (technology, schedule, resource, dependency and location risks).

DPTI advises that each non-financial criterion is assessed by a representative stakeholder group and based on a risk rating assigned to the criteria. These scores are then summed, with scores over 10 representing an upgrade to the next highest financial category.

The Procurement and Contracting Directorate within DPTI is responsible for the procurement process, irrespective of whether the procurement is a civil or a building infrastructure procurement. This includes development of tender documentation, approaching the market, selection of supplier and award of contract.

Differences in DPTI internal governance for construction procurement projects depend on the type of construction procurement project – civil (transport) or building (infrastructure):

- *Civil* projects are largely delivered by DPTI’s Major Projects Division as its own client. DPTI advises that the governance requirements depend on the complexity, risk and value of the project. Governance requirements include gateway reviews and DPTI’s Portfolio Management Office (PMO) has oversight of steps 1–4 of the framework. Collaboration across multiple divisions is usually required and many projects involve separate steering committees established for both the initial procurement phase as well as the project delivery phase.

- *Building infrastructure* projects are delivered via the process outlined in the policy and PiP. Consequently the 'Lead Agency' has a key role in the decision process as well as participating in Steering Committee(s) and other governance arrangements. DPTI's Building Projects Directorate monitors the progress of such projects.

In addition to the building infrastructure and civil construction procurement projects, DPTI manages the Across Government Facilities Management Arrangement (AGFMA) contract for purchasing lower-value, low-risk construction projects/works (valued up to \$1m). The DPTI Facilities Management Governance Group provides governance to the Facilities Management Services Arrangement under AGFMA. The Governance Group includes representation from executives from each participating agency.

DPTI has advised the Commission that:

- The internal DPTI governance arrangements for civil projects encompass the planning, delivery management and asset maintenance and management. Lead agencies have their own internal processes to ensure compliance with their respective strategic priorities and objectives.
- A new DPTI governance framework is in the process of being developed that will include an Executive Finance Committee and a Major Projects Executive Committee with terms of reference.

Construction procurement governance in public authorities

Overall governance for construction projects

In general, those agencies that undertake larger capital works projects (in value and/or volume) have a specific capital works committee and/or a project management office (PMO) that oversees capital works projects.

As discussed, public authorities also purchase off the AGFMA when undertaking minor works projects under \$150 000 and small, low-risk construction works valued at \$150 000 to \$1 million. DPTI manages the governance arrangement for the AGFMA.

Governance for individual construction projects

The governance arrangements for individual construction procurement projects will depend on whether the project is a building infrastructure project, a civil construction project, or a project being delivered via the AGFMA.

For building infrastructure projects:

- A service level agreement (SLA) is developed and distributed to key stakeholders to formalise the roles and responsibilities of the Lead Agency and DPTI.
- The DPTI Procurement Officer drafts an acquisition plan that formalises the roles and responsibilities for the project including the project manager, evaluation team, technical advisors, budget/cost estimators, etc.
- The Lead Agency's minister has overall responsibility for the project. The Lead Agency normally appoints a senior executive to be project sponsor and to provide leadership and direction to the project team. Larger or complex projects may also

require a steering committee. The project team includes key stakeholder representatives from the lead agency and from DPTI as required.

- There is a structured process involving gateways that proceed serially unless the project is a strategic project or fast tracked. In those cases, the process provides for some parallel processing to remove time delays.

For civil construction projects, mainly transport projects:

- Various divisions within DPTI work together to deliver the project and DPTI's PMO provides support and advice on the projects. High-value/high-risk capital projects include a gateway review which includes short independent reviews of a program or project prior to key decisions being made to identify opportunities for improvement.

Accreditation

An agency's procurement construction governance arrangements may be influenced by whether they have obtained accreditation from DPTI. The department undertakes agency accreditation for construction projects up to \$1 million (GST exclusive) in value in accordance with the Agency Self-Management Approval Assessment Framework for Delivery of Lower Risk Construction Projects (the Accreditation Assessment Framework). DPTI assesses the capabilities of a non-infrastructure agency to deliver low-risk building construction projects by reference to:

- the type and risk profile of projects or programs of work that may be undertaken by the agency;
- the existing capability (knowledge, skills and systems) to manage the risks;
- the public authority's approach to safety; and
- the resources available to government in public authorities.

DPTI advised the Commission that, since September 2017, 22 projects have been managed through a construction procurement accredited agency. Four of those projects were building construction related and the remainder civil construction projects. It is not clear what proportion of total building infrastructure projects that represents. As a result of its accreditation from DPTI, DEW has a slightly different governance arrangement for construction as they have developed their own construction templates and processes to support accredited projects/programs. DPTI has advised that they have the discretion to reject requests for accreditation if they consider that the authority does not have access to appropriately skilled and experienced staff to manage the project.

3.2 Construction issues

3.2.1 Value for money

Value for money in construction involves assessing both financial and non-financial factors including, but not limited to:

- whole-of-life costs including maintenance, operation, licensing and transitioning out or disposal costs;

- fitness for purpose, quality, service and support offered;
- risks involved;
- contribution to sustainability objectives (social, environmental and economic targets);
- compliance costs associated with the regulatory framework; and
- contribution to the achievement of procurement-related or other identified government objectives.

In the construction space, strategies that may contribute to the achievement of value for money outcomes include³¹:

- developing a shared understanding across government agencies and with industry and the market on what is, and is not, value for money in construction procurement;
- proactively identifying value by integrating specific procurement objectives in strategic planning;
- conducting appropriate market and risk analysis;
- providing performance specifications and incentives to measure value, reward value-adding and encourage innovation;
- providing flexibility to revise scope, budget and timeframes;
- streamlining and aligning approvals and processes to avoid delays;
- setting appropriate contract periods and planning for contract completion and transition;
- developing and managing relationships with strategic partners;
- ensuring all parties (contractor and purchaser) have the required capabilities throughout the procurement process and contract; and
- undertaking options analysis to identify which procurement strategy and model will be most appropriate for the complexity and nature of the project.

Determining the appropriate strategy to achieve value for money depends on the nature, risk, complexity and specific circumstances of each construction procurement project. Managing value requires having the skills, information and capability to make the right choices or selections to obtain the optimal balance of benefits in relation to cost and risk. In the absence of a skilled workforce, strong guidance is required.

An approach that optimises value, rather than minimising cost, needs to be:

- focused on achieving the optimal balance between quality, whole-of-life cost, time and other government objectives;

³¹ Queensland Government, Develop a procurement strategy, Building, Construction and Maintenance, available at: <https://www.forgov.qld.gov.au/develop-procurement-strategy>

- structured, auditable, accountable and repeatable; and
- multi-disciplinary (where appropriate) to maximise the innovative potential of all project participants working together in an integrated project team.

The ongoing continuous assessment of value can be referred to as 'value engineering'. This process involves ongoing assessment to determine whether better value alternatives or solutions may be available (for example, gateway reviews at specific key decision points).

The Commission has researched and analysed value for money with respect to construction procurement in South Australia by reviewing good practice approaches, considering feedback provided by businesses, associations and public authorities, and by analysing data obtained via existing databases and through its own random sample of 106 construction procurement tenders provided to the Commission by public authorities. The discussion below provides commentary on the Commission's initial findings and draft recommendations on construction procurement value for money for the SA Government.

3.2.1.1 Stage 1 findings and conclusions on value for money

The Commission's final report on Stage 1 of the Procurement Inquiry included the following findings on value for money for goods and services procurement:

- Governments in Australia and abroad are increasingly using procurement as a policy tool to support other strategic objectives. Consequently, the measurement and achievement of value for money is more than measuring and achieving financial benefits and savings.
- Businesses expressed their view that value for money is poorly defined and not well understood, applied or measured.

In its response to the Commission's final report, the SA Government supported the recommendations on value for money and provided the following commitments:

- revise and develop an improved SPB Value for Money in Procurement Guideline to better assist government agencies in applying and determining value for money;
- better practices identified by the Commission in other jurisdictions will be considered in drafting the new guideline;
- the revised guidance will be incorporated into current SPB training courses. A series of specific information sessions will also be held; and
- businesses, business associations and not-for-profit organisations will be informed of the revised value for money guidance in the following ways:
 - The materials will be published on the SA Tenders and Contracts website.
 - Businesses will be provided with the revised guidance as part of each tender (where appropriate).
 - The Office of the Industry Advocate will communicate the guidance material to businesses as part of regular industry engagement forums.

3.2.1.2 Strategic planning for value

Government procurement is increasingly required to meet multiple objectives with limited resources. The various stakeholders in a construction project may reasonably all have different perspectives on what represents value. Strategic planning for value helps decision makers at all levels reconcile those differences and supports the purchaser to progress towards the achievement of the agreed objectives with limited resources.

An overall strategic plan or guidance from government on its strategic priorities helps to ensure that public authorities maximise opportunities to leverage procurement's impact on specific government priorities. This approach requires sufficient flexibility and resources to shift an organisation's strategy from reactive, transaction purchasing to more proactive, value-based procurement strategies.

Setting clear strategic priorities is important for decisions further down the chain, such as how different evaluation criteria should be prioritised or whether investment in new technologies is worthwhile.³²

A shift to planning for value requires a shared understanding between the different stakeholders on what constitutes 'value' with respect to construction procurement. An overall strategic plan links the government's objectives to strategic decisions and, as a result, the daily work carried out by government procurement officers.

Planning for strategic value can provide significant benefits for the economy. The Commission received feedback on the importance of planning for larger programs of construction work that can have a significant impact on the achievement of value for money in construction.

The Institute and ACA have concerns regarding the management of government stimulus packages in relation to achieving value for money outcomes. Value for money is strongly linked to levels of activity within the construction sector. Stimulus packages inherently introduce a concentrated body of work into the market. When this is done with inflexible program end dates and insufficient resources within government to develop and manage delivery of these projects, the market becomes artificially inflated and the value achieved is negatively impacted. (AIA and ACA stage 2 submission)

In this instance, stimulus packages could be better designed so as to avoid those peaks of work (e.g. by limiting numbers in certain timeframes).

Strategic planning for value may be undertaken at the whole-of-government, public authority and individual project level.

At the whole-of-government level, there are limited examples of value for money strategic planning approaches that are specific to construction procurement in other jurisdictions. However, the Commission's research indicates that value for money (particularly with respect to broader considerations of value) is a growing area of focus for many jurisdictions

³² OECD, *Productivity in public procurement*, 2019, p. 86.

– particularly given ongoing fiscal constraints, rising demand and therefore cost of construction inputs, and incorporation of sustainability objectives.

Table 3.3 provides examples from two government jurisdictions that have established and implemented strategic planning for value with specific reference to construction projects.

Table 3.3: Examples of strategic planning for value specific to construction procurement

Government jurisdiction	Strategic planning for value – construction approach
<p>New Zealand</p>	<p>The NZ Government Guide to Risk and Value Management provides the key principles on risk and value management for construction procurements and explains how these principles can be incorporated into the project life cycle.</p> <p>Value management is used to identify business needs and manage risks that may be associated with the procurement solution that offers best whole-of-life value. A measured, well understood and effectively managed risk approach is seen to add significant value to the outcomes of a project. Ongoing communication enables stakeholders to identify, measure and review value at regular intervals.</p> <p><i>'Value management provides a structured approach to the assessment and development of a project, to increase the likelihood of achieving these requirements with optimum whole of life value for money.'</i>³³</p>
<p>Queensland</p>	<p>The Queensland Government's procurement framework includes the category 'building, construction and maintenance' (BCM). Information provided on the website includes guidance on planning for procurement and demonstrating value for money for BCM. To choose the optimum procurement strategy for BCM projects to maximise value one must consider:</p> <ul style="list-style-type: none"> ➤ risk allocation between parties by selecting the best contracts and clauses; ➤ use of performance specifications to encourage innovation; ➤ maintaining flexibility to secure changes to scope at a reasonable cost; ➤ use of incentives to reward value-adding outcomes; ➤ setting appropriate contract periods; ➤ time required to maximise opportunities for regional and SME participants; ➤ capability of the market and purchaser; and ➤ application of a 'local benefits test' to high-expenditure or high-risk procurement.

Source: based on SAPC consultation with other jurisdictions and consideration of relevant policies.

Planning for value at the public authority or agency level requires consideration of the public authority's core purpose, strategic and business plans, as well as considering the authority's own capability and that of the existing and potential supplier base. A key consideration at the public authority level is the positioning of the procurement function within the organisation. This includes both when and how the procurement function is incorporated into the authority's strategic priorities and projects/programs.

SA Water provides a good example of a public authority that has developed a strategic approach to planning for value. SA Water's business planning process and outcomes sets out the authority's purpose and what the procurement team are delivering. There are strong links between the business plan and how value for money is extracted from its sourcing and

³³ NZ Government Procurement, *A Guide to Risk and Value Management*, 2016, p. 11.

contract management activities. SA Water’s business plan also links with its Category Management Strategy and Structure where specific, long-term category plans are developed across a variety of spend categories. SA Water’s Corporate Capital Delivery Program outlines the procurement strategy for its capital construction program and value for money is further built into procurements through the specific market engagements and evaluation processes.

At the individual project level, a value assessment of the construction procurement project at the commencement of the project can assist the options analysis (business case) and help describe stakeholders’ needs and priorities. An options analysis incorporating benefits analysis can identify the key priorities and constraints and consider the government’s, and public authority’s, objectives. The options analysis can specify the purchaser or client’s values and priorities, the project’s needs and objectives, and key project constraints and risks. The options analysis can then provide information for the project brief which will outline the requirements, objectives and priorities to be agreed by all stakeholders. An additional value assessment may be required when determining the appropriate procurement delivery model to ensure the model or method chosen best meets all of the agreed project objectives and is most likely to achieve value for money.

The Commission has observed consistent consideration of value for money in the early planning stages of individual projects. With respect to defining, incorporating and measuring value for money in construction procurement projects, DPTI advised the Commission:

- All new civil infrastructure projects must meet the minimum benefit–cost ratio requirements that form part of the business case that is prepared and considered before funding will be allocated and the procurement can commence. Benefits realisation then forms part of the project brief and is reviewed at each of the civil project gateway reviews.
- It is up to the relevant Lead Agency to undertake their own value for money analysis in building project procurements.

According to the information provided by DPTI, with respect to building project procurements, the value for money assessment depends on the Lead Agency’s ability to develop a project brief that incorporates all strategic priorities, is timely, and is agreed by all stakeholders.

Public authorities who have been Lead Agencies for building construction projects provided feedback to the Commission on the identification and assessment of value for money for such projects. The Commission was advised:

- DPTI considers value for money in the design and construction phase.
- Consideration of price and non-price elements can be influenced by DPTI’s evaluation approach in situations where there is a low number of tender submissions, as that can be viewed by DPTI as a perceived ‘price risk’ associated with that tender.
- DPTI’s no longer uses prequalification performance scores in evaluation processes, which provides no incentives for consultants or contractors to provide value from their prior project experience.

- There is minimal reporting on value for money outcomes except for cost management reports and post-construction reports for handover.

Based on the information provided by public authorities (including DPTI), the Commission is forming a view that there are different perceptions between DPTI and public authorities on the identification, assessment and measurement of value for money objectives in building construction projects. This includes how value for money strategic objectives are identified, converted to measurable specification criteria, then assessed and measured, and who decides. The Commission will follow up with DPTI and Lead Agencies.

Planning for a shared understanding of value

In Stage 1 of the Procurement Inquiry, the Commission noted the importance of briefing the market on planned procurement opportunities. Not only does this provide the market with sufficient time to prepare for potential tenders, it also provides the market with a clearer appreciation of the government’s strategic priorities via its future procurement program and promotes a shared understanding of what is (or is not) included as ‘value for money’.

All Australian government jurisdictions publish information on forthcoming procurement opportunities for construction projects. This starts with the annual budget announcements on capital works programs. For example, the SA Government’s 2019–20 budget announced \$11.9 billion in infrastructure spending for new metropolitan and regional roads and key infrastructure.³⁴ In addition, each jurisdiction will provide lists of planned construction procurement activity or projects as indicated in Table 3.4. The type of information, the level of detail, and the frequency that the information is updated varies across jurisdictions.

Table 3.4: Publishing of planned construction procurement activity, by jurisdiction

Jurisdiction	Planned construction procurement activity published
Australian Government	The Department of Infrastructure, Transport, Cities and Regional Development’s National Infrastructure Construction Schedule (NICS) provides contractors with information on infrastructure pipelines, tendering and contracting. Each agency is required to publish an annual procurement plan on the AusTender website. Each activity includes the UNSPSC which enables the list to be searched according to whether it is construction or not.
Victorian Government	The annual Victorian Infrastructure Plan Projects Pipeline provides information on existing and new planned projects. Public Construction – Guidance 5.1 requires agencies to publish forward notices of open and selective construction tenders. Publication is on the agency website or Tenders Vic website. Activities are published anywhere from 4 to 52 weeks ahead of the market approach depending on complexity.
New South Wales Government	NSW Infrastructure Pipeline Portal and document provides annual information on infrastructure proposals under development valued over \$50m. Agencies in accredited clusters must publish an annual agency procurement plan with goods, services and construction planned procurements.
Queensland Government	Forward procurement notices are published on QTenders. ‘Backing Queensland Jobs’ 2018–2021 Procurement Plan provides a summary of forthcoming procurements including construction procurements.

³⁴ <https://statebudget.sa.gov.au/#BuildingSA>

Jurisdiction	Planned construction procurement activity published
	Building Queensland Infrastructure Pipeline Report is an annual publication on proposals valued over \$50m.
Western Australian Government	The WA Department of Finance website includes an 'Upcoming capital works projects' webpage that lists announced projects expected to be tendered for construction within the next 18 months. It is updated quarterly. Early tender advice notices are published on the Tenders WA website and can be searched using UNSPSC codes. The WA Department for Main Roads publishes an Infrastructure Delivery Plan for planned works above \$3m.
Tasmanian Government	The Future Opportunities webpage includes information and links to planned procurements including planned infrastructure opportunities (updated quarterly), plus a full capital investment program list. It includes estimated values.
Australian Capital Territory Government	Future tender notices are published on the Tenders ACT website. The Major Projects Canberra website provides information on future capital works tender opportunities.
NT Government	Publishes an online and downloadable 10 Year Infrastructure Plan which is updated annually. Also provides an interactive business intelligence dashboard to enable further information and analysis on procurement projects. Publishes a monthly update on planned projects categorised into civil and building projects.
SA Government	DPTI provides: <ul style="list-style-type: none"> via its website, a downloadable pdf Forward Work Plan 2018 listing major projects to 2022 including the estimated value (within a range); for the past 2 years, an annual projects pipeline industry briefing; and a downloadable pdf list of 'building projects' in the planning phase. Infrastructure SA will be developing a pipeline of projects consistent with the 20-year infrastructure strategy to be published.

Source: SAPC interjurisdictional analysis.

As indicated in Table 3.4, DPTI provides information on a whole-of-sector basis on planned construction projects for the market via downloadable lists and annual industry briefings. DPTI advise the Commission that the Procurement and Contracting Division has developed a strategic plan for 2018 focusing on investing in people; smarter systems; customer and market focus; delivering value; and operational excellence. Guidance policies and documents are included on the DPTI intranet for procurement planning processes for individual projects.

The Commission notes that:

- All jurisdictions provide a list of infrastructure projects in the pipeline, noting that Infrastructure SA is in the process of developing such a list.
- Although a list of future tenders is included on the SA Tenders website, the list is extremely limited at any point in time and often the closing date for the tenders has already closed (indicating that the tender has already been released).³⁵

³⁵ SA Tenders and Contracts website, Future Tenders page, example taken on 19 August 2019.

- The consolidated list of planned procurement activity produced by the SPB biannually does not include construction procurement given the limitations of the SPB's scope.
- It is not clear why there are two separate lists of planned procurement activity available from DPTI.

SA Water utilises several supplier panels to deliver the significant majority of its infrastructure capital plan. All panel suppliers are informed of forthcoming tendering opportunities on a quarterly basis. SA Water publishes forward notifications to the open market using the SA Tenders and Contracts website on those occasions when it procures outside of existing panel arrangements. SA Water also conducts industry briefings to inform potential suppliers on their proposed procurement strategy for the forthcoming regulatory period.

The Commission acknowledges DPTI's work on engaging with industry on future opportunities via the published lists and annual briefings. The Commission has, to date, seen limited information on DPTI's overall strategic plan or approach to value as it relates to construction procurement. The Commission is forming the view that further work is required to leverage the reforms and work DPTI has already undertaken to develop, and embed, a strategic approach to value in construction procurement. The Commission will be further exploring this with DPTI and other key stakeholders for the final report.

3.2.1.3 Factors of value for money in construction

Financial factors

In order to assess the importance of the cost factor in the procurement of construction projects in South Australia, the Commission looked at:

- the consideration of whole-of-life costs;
- the frequency of selecting the lowest quote;
- the weighting provided to the cost factor.

Whole-of-life costs

An important consideration of value is the concept of whole-of-life costs and benefits. These are the costs relating to an asset or service from the commencement of the project, through to its operation and maintenance, to its disposal or transition to a new asset or service. When determining the appropriate procurement model, the solution should represent the lowest net present cost while meeting the scope, time and quality criteria agreed in the project brief or business case.

The Commission was provided with feedback on whole-of-life cost considerations and value for money in construction procurements in South Australia:

Value for money in relation to capital works projects is generally measured in terms of the cost per square meter for construction. However, the total cost of maintaining and operating a building over its life far exceeds the initial capital cost. Government generally builds assets that it owns and operates over an extended period. Therefore, prudent investment at the capital works

phase of the project, which allows for thorough development and testing of maintenance and operational considerations, will result in a better value for money outcome over the life of the building. (Australian Institute of Architects, submission for Stage 1)

As part of the Stage 2 inquiry, the Commission obtained a random sample of 106 construction tender evaluations by SA Government public authorities. A database was developed to assist with the Commission's analysis and assessment of existing construction procurement processes and practices in the SA Government.

Out of 106 purchase evaluations, the whole-of-life cost of a project was infrequently mentioned. In one case, it was mentioned as an added benefit provided by the winning tender but the benefit was not measured or considered as part of the tender price. It is therefore unclear how 'whole-of-life costs' are being considered by public authorities when assessing tenders.

Frequency of selecting the lowest priced quote

For four contracts out of 106, it was not possible to determine the actual price of the tender (a schedule of prices was provided instead: price per item, per metre, per hour, per site, etc.).

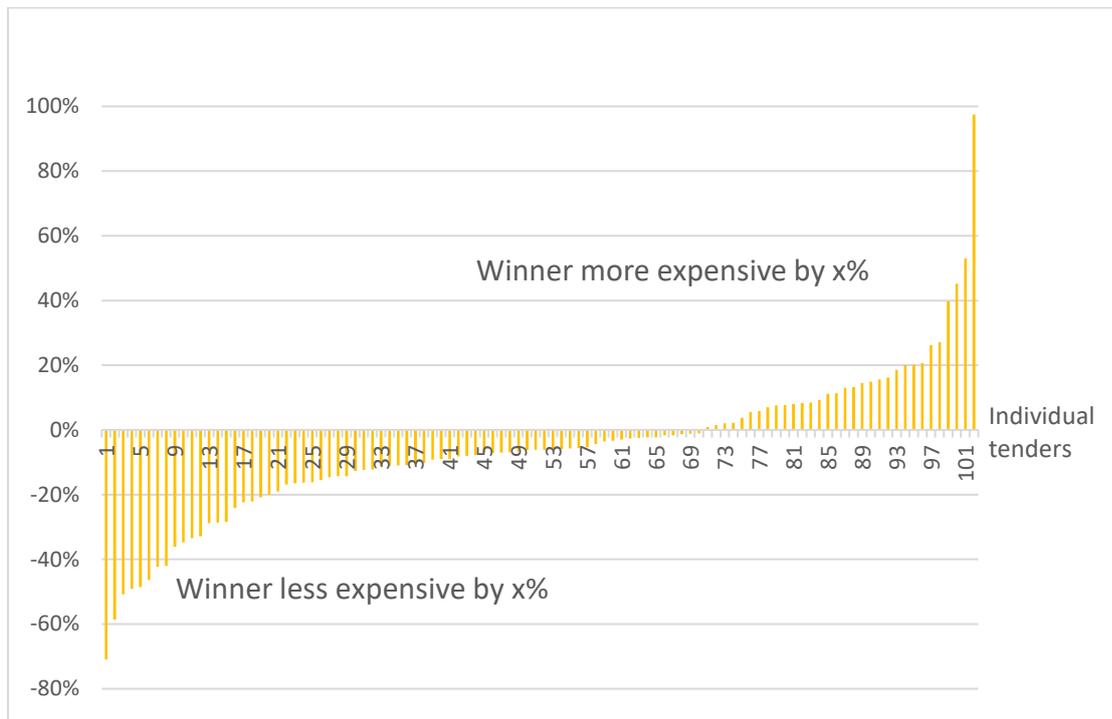
For the other 102 purchase recommendations:

- For 70 contracts (69 per cent), the winner's price was less than the runner-up's price.
- For 32 contracts (31 per cent), the winner was more expensive than the runner-up.

In 37 per cent of cases, the public authority chose an option where the winning price was at least 10 per cent cheaper than the runner-up (see Figure 3.3).

Those figures are in line with what was observed for the procurement of goods and services.

Figure 3.3 – Price difference between the winning and second ranked for 102 tenders



Source: OSAPC analysis of 106 random tenders, August 2019

Those numbers vary slightly with the value of the procurement:

- Around 73 per cent of procurements under the value of \$1 million (excl. GST) were won by the lower price offer.
- Around 60 per cent of procurements above the value of \$1 million (excl. GST) went to the lower price offer.

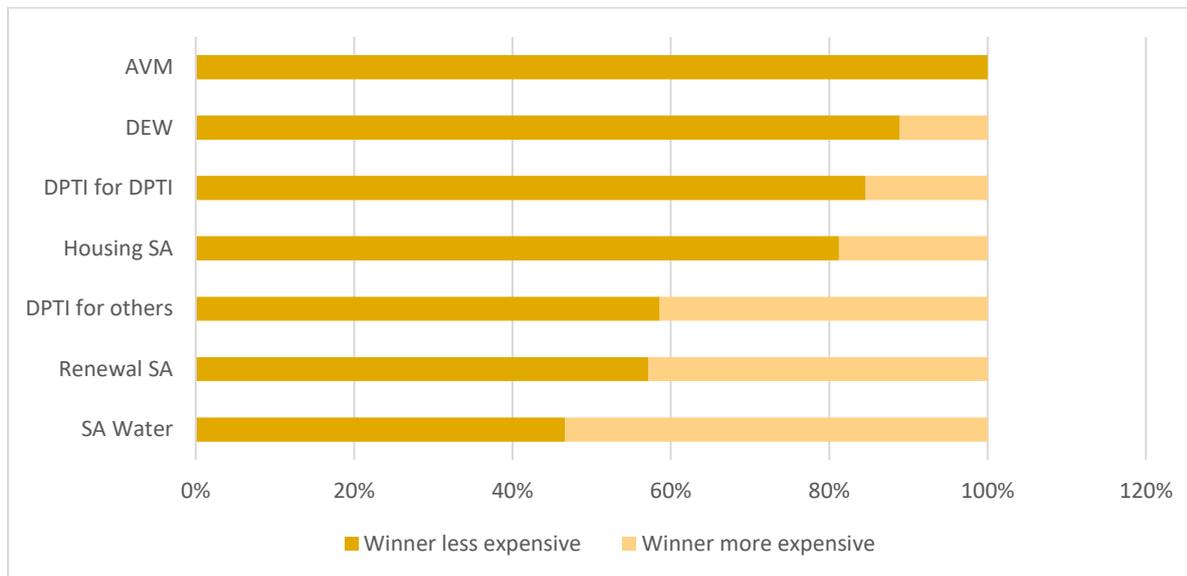
Where the lower price option was chosen:

- In 12 per cent of cases, another factor than price was the determining factor (capability, experience, timeliness, etc.).
- In 38 per cent of cases, a complex range of factors, including price, determined the outcome.
- In 50 per cent of cases, price was the determining factor.

The evidence above suggests that price plays a higher role in the procurement of construction projects than goods and services contracts. This can partly be explained by the higher use of panels and prequalification lists as a market approach for construction procurement projects.

There were also differences in the propensity of agencies to select the lower price option. In practice, from 47 per cent to virtually 100 per cent of purchases went to the lower price offer (see Figure 3.4).

Figure 3.4 – Choice for lower price option per agency



Source: OSAPC analysis of 106 random tenders, August 2019

The propensity to award contracts based on lowest price is an issue that cuts across many jurisdictions – sometimes with serious consequences. For example, as a result of the UK Government’s austerity measures, it was claimed that competitive tendering was used to drive down cost which, combined with inadequate risk management (including due diligence monitoring), resulted in undeliverable contracts and contractors going into liquidation or administration. The UK Parliament’s inquiry into the collapse of the construction firm Carillion in 2017 found that the market had taken note of the government’s preoccupation with price and that there was less focus on assessing quality (including the supplier’s risk profile) when evaluating and awarding contracts. The consequences of supplier failure can be particularly acute for a government given the contractor can be engaged to provide complex services to vulnerable sectors of the community, and/or may impact on subcontractors of a particularly large contract.³⁶

Weight given to the price factor

Out of 106 tender evaluations, 15 did not provide a weighting for price:

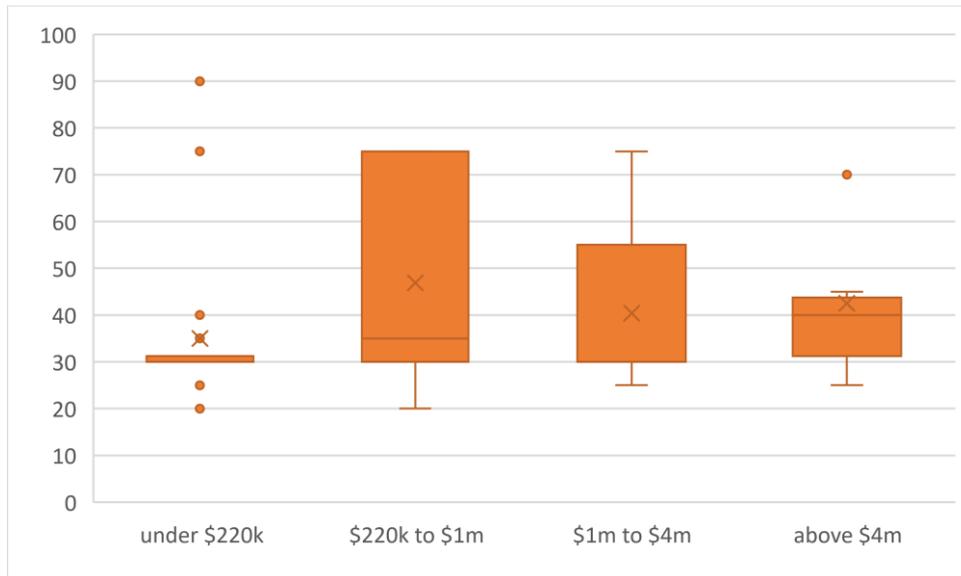
- 11 were for DPTI’s civil projects: those involved a tender assessment where non-price criteria and IP Plan scores were used as a multiplier of the tendered price.
- Three were for contracts under \$325 000, and were assessed on price only, from a panel of suppliers (in other words, price had a weighting of 100 per cent).
- One used a value for money criterion, weighted at 20%, which compared the price with the non-price score, and this ratio with the lowest ratio observed.

Out of the 81 contracts for which price was a weighted criterion:

³⁶ https://publications.parliament.uk/pa/cm201719/cmselect/cmpubadm/748/74810.htm#_idTextAnchor063, paragraph 71

- There was no correlation between the value of the contract and the average weighting applied to the price criterion.
- The variability of price weightings applied for contracts valued between \$220 000 and \$4 million was very high and decreased as the contract value increased (see Figure 3.5).

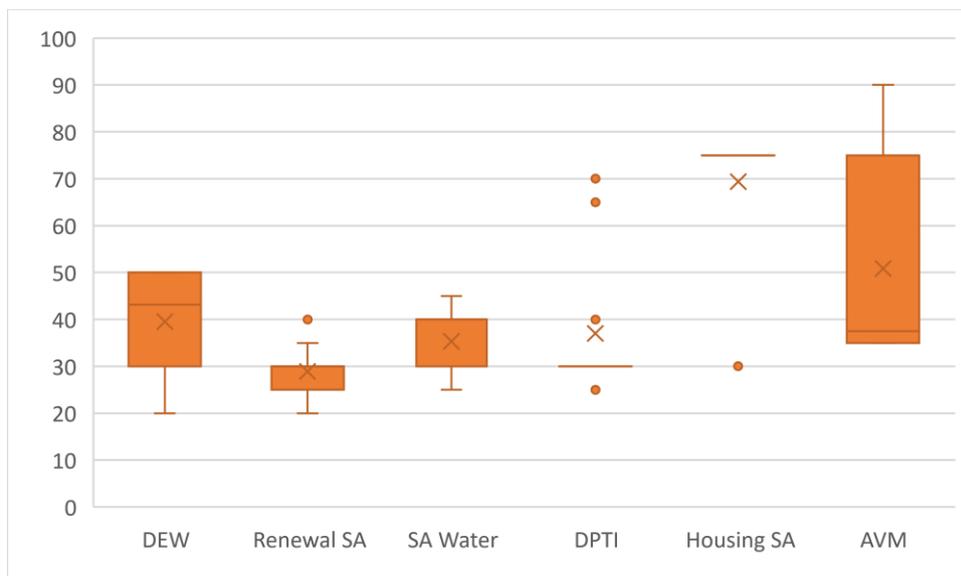
Figure 3.5 – Weight given to the price factor by contract value



Source: OSAPC analysis of 106 random tenders, August 2019

The weighting seemed to be influenced more by the agency undertaking the scoring (see Figure 3.6), with little consistency across government. The Commission will investigate this matter.

Figure 3.6 – Weight given to the price factor by agency



Source: OSAPC analysis of 106 random tenders, August 2019

The Commission also notes cases where expenses were incurred to source experts to assist with the scoring of non-price criteria, yet the weighting applied to price was high, possibly pointing to inconsistency in what the public authority values.

Non-financial factors including other government objectives

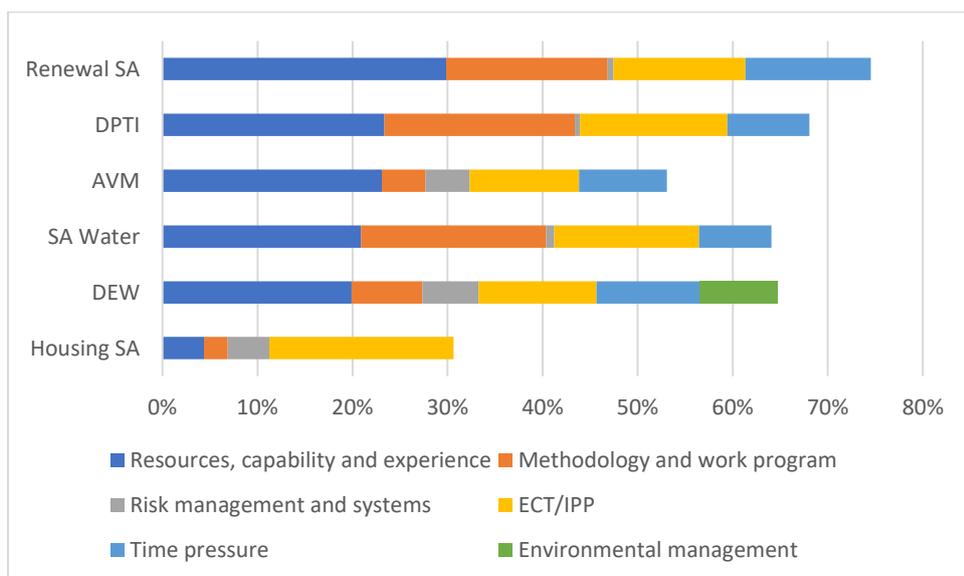
The most common non-price factors integrated by public authorities into the assessment of value for money for construction projects, in order of weight and application, are:

- the SAIPP (25 per cent);
- the methodology (24 per cent);
- the experience of the team (18 per cent); and
- the capacity of key personnel (16 per cent).

All other criteria account for less than five per cent each (this percentage is the sum of the weightings applied to the 106 random tenders collected by the Commission, for one criterion, divided by the sum of all weightings applied to all criteria).

Looking at the average weighting given to each criterion by each agency, the Commission has grouped some criteria to make the results more readable (see Figure 3.7). Renewal SA, DPTI and SA Water have quite comparable approaches. DEW, AVMC and Housing SA give a larger importance to risk management (around five per cent) and Housing SA has an uncommon set of weightings. DEW considers environmental management in its assessments, which delivers policy outcomes the department is responsible for. No other government objectives have been translated into criteria in the sample considered by the Commission.

Figure 3.7: Weight given to non-price factors by agency



Source: OSAPC analysis of 106 random tenders, August 2019

Examples of other government objectives that have been taken into account for construction projects undertaken by the SA Government include:

- initiatives to support the *Green Industries SA Act 2004* including the circular economy, waste management hierarchy and South Australia's Waste Strategy 2015–2020 (looked at on a project by project basis);
- the South Australian Industry Participation Policy (SAIPP), incorporating the Aboriginal Economic Participation through Procurement initiative (through tailored IP Plans); and
- the potential introduction by the Australian Government of incorporating recycling materials into public construction projects.³⁷

Consideration of 'other government objectives' with respect to government procurement can be viewed through two interlinked perspectives:

- incorporation of government objectives or priorities that are not directly related to the procurement such as environmental, social or economic policies; and
- accounting for 'externalities' that are incurred or received by a third party who has had no control (or often involvement) in the creation of that cost or benefit.

Examples of externalities with respect to government construction procurement include:

- positive externality – building infrastructure in a regional area which can inject new investment into that area in the short term and create longer-term value for existing and new businesses; and
- negative externality – awarding a contract to a supplier who, in servicing that contract, causes pollution in a local waterway which in turn affects local agricultural production.

An important quality of externalities is that they have spill-over effects that are not incorporated into the price or value of the procurement process and consequently in the contract.

Externalities are a form of market failure and, as such, are often the reason why a government will intervene in the market via taxes, incentives and/or other government policies. Consequently, it is important that government considers other government policies and externalities when undertaking public procurement activity – particularly for larger projects and/or those that have a disproportionate impact on vulnerable sectors of the economy and society.

In practice, it can be particularly difficult for individual agencies to account for, and capture, such 'externalities' as it is not always possible to identify and quantify a direct link between the externality and a particular contractor or contract. Externalities may be incorporated into the procurement process by integrating government strategic objectives or policies that target specific externality categories such as pollution. The integration of other government objectives (social, environmental and economic) into the tender evaluation process can be a complex task – particularly as both the process and impacts can vary depending on the nature of the procurement project itself. Any strategic response to integrating other

³⁷ <https://www.theguardian.com/australia-news/2019/jul/19/minister-flags-ambitious-recycling-targets-to-kickstart-waste-market>

government objectives must be sufficiently flexible to provide a mechanism by which other government objectives are incorporated in both price and non-price considerations, while allowing for specific circumstances where appropriate.

The Commission requested public authorities to provide information on whether, and how, other government objectives are incorporated into value for money for construction projects:

- DPTI advised that it incorporates objectives relating to the SAIPP (including the Aboriginal participation policy) in the acquisition planning process and that it forms part of the evaluation criteria. DPTI did not provide the Commission with information on incorporating other government objectives apart from SAIPP, although the Commission understands that there may be mandated Australian standards relating to environmental requirements.
- Most other public authorities reference the SAIPP when referring to other government objectives, although some provided other examples which are summarised in the table below.

Table 3.5: Examples where other government objectives have been incorporated into construction procurements

Public authority	Examples where other government objectives have been incorporated into construction procurements
Dept for Environment and Water (DEW)	Specialist contractors are required to undertake minor construction work in regional or remote areas. Criteria may be included to encourage participation by smaller, regional suppliers.
SA Health	A key contributor to a 27 per cent reduction in energy consumption over the last 15 years was energy targets incorporated into construction procurement projects.
Arts SA	Achieved a reduction in electricity consumption and greenhouse gas emissions by incorporating specific criteria in the project to upgrade lighting for the Art Gallery of SA.
Dept for Correctional Services (DCS)	In 2016/17, a contract awarded to redevelop the Adelaide Women’s Prison included a requirement for the contractor to provide on-the-job training for women prisoners which is known as ‘The U-Turn Construction Pathways Program’. The program is a collaborative training and construction program providing opportunities for prisoners to learn new skills, gain qualifications, participate in real worksite environments and ultimately gain employment in the construction industry. Women prisoners are trained in many aspects of construction while carrying out onsite works, which leads to the prisoners gaining a Certificate II in Construction Pathways. To date, 25 women prisoners have participated in the on-the-job training and 7 have been successfully employed in the construction industry since their release.
DPTI	Achieved a 10% target to engage displaced automotive workers and Aboriginal employees as part of the Northern Connector project.

Source: SAPC consultation with public authorities.

The Commission notes that there does not appear to be a clear positive relationship between the size of construction procurement spend and the degree to which other government objectives are incorporated into construction procurement projects. According to information provided to the Commission, the only consistent application of other

government priorities in construction procurement is the SAIPP. This is probably because the SAIPP is mandated, it is embedded in the procurement process, and it is well known and promoted. It is concerning, given the environmental, economic and social challenges in South Australia, that the government does not appear to have the appropriate tools to be able to strategically and proactively leverage the \$11.9 billion in infrastructure spending announced by the SA Government in the last budget, beyond a project-by-project system.

The Commission is forming the view that, given the experience of the SAIPP, incorporating other government objectives requires them to be embedded in the process, possibly via mandated requirements, with strategic leadership buy-in.

Examples in other jurisdictions where a strategic framework incorporates other government objectives into procurement policies and practices were discussed in the final report for Stage 1. With specific reference to construction procurement, approaches undertaken in other jurisdictions to incorporate 'sustainable' or 'social' objectives are discussed below.

- Since 1 September 2018, Victorian Government agencies who are procuring goods, services and construction are required to comply with a Social Procurement Framework. The five-page guide on its application to construction procurement requires:
 - Agencies must incorporate social procurement objectives and outcomes into construction procurement planning for all individual projects and programs under the framework (irrespective of value).
 - Projects valued over \$20 million must have a separate social procurement plan.
 - Public construction tenderers must demonstrate in their response how they will deliver the sustainable and social outcomes, and such commitments will form part of the contract if successful.
 - A minimum weighting of five to ten percent is recommended for social procurement related evaluation criteria and includes all suppliers through the supply chain.
 - The framework complements, but does not replace, Victoria's Local Jobs First – Victorian Industry Participation Policy.
- In 2018, the Australian Government developed its Sustainable Procurement Guide in support of Commonwealth Procurement Rules requiring tenders to be evaluated on financial and non-financial costs and benefits including sustainability elements. Sustainability refers to the 'triple bottom line' objectives: economic (e.g. local jobs), social and environment. The guide includes guidance on the concepts of sustainable procurement, and options for including considerations of sustainability in the procurement process and decisions. With respect to value for money, the guide provides examples and issues to consider when undertaking a value for money assessment with particular reference to whole-of-life costs and benefits that incorporate other government objectives.

- Scotland's Zero Waste organisation provides a Construction Sustainable Procurement Guide on considerations and requirements with respect to other government policies throughout the different phases of the construction procurement process. For example:
 - The pre-procurement phase provides information on all relevant 'other government policies' that may need to be considered and market engagement strategies.
 - The procurement phase provides information on the specifications that could be included that address other government objectives.
 - The contract phase includes guidance on the types of clauses and performance requirements to ensure the achievement of those other objectives.

3.2.1.4 Evaluating for value for money outcomes

The tender evaluation method scores the tender responses to identify the tenderer who has provided the most economically advantageous tender for the purchaser. It is based on finding the best price–outcome ratio to successfully complete a project.

The contracting authority must have freedom to choose the criteria and weightings to apply (for example, requirement: ability to meet deadline, criteria: price 30%, experience 25%, capability 30%, resources 15%) in order to highlight where the value will come from. The consideration of criteria and their weighting was addressed in the previous section.

The method/formula, criteria and weightings chosen and how they are scored is an important stage where value can be created or lost.

This section focuses on the actual integration of those criteria and weightings to rank the tenderers. It is a function of who conducts the assessment and what methodology is followed.

Choice of evaluation team

Effective procurement requires well-qualified procurement professionals. The Commission considers capability in Section 3.2.4.

From an evaluation perspective, it requires capable people in the panel assessing the tender (is the panel representative of the primary stakeholders of the contract: client, designer, builder, end user? Are the people experienced in the type of project being tendered?) so that all issues can be raised and negotiated prior to a tender being awarded. The actual compositions of the assessment teams within public authorities has not been investigated yet by the Commission.

The Commission, through the analysis of 106 tender evaluations, started recording the number of administrative errors observed in those evaluations (those are the errors that the Commission noticed, noting it wasn't the prime purpose of the Commission when reading those evaluations). An initial analysis identified a total of 33 human errors in those evaluations. These errors ranged from:

- the contract value changing between documents;
- to the inclusion or exclusion of GST not being appropriately considered when reporting prices;
- to the ECT/IPP scores being incorrectly reported in the tender evaluation;
- to weightings being incorrectly applied, to price scores being swapped between tenderers, to the price criterion being scored differently by panel members, etc.

This highlights the need for better quality control over the tender assessment part of the procurement process. Reducing the amount of human manipulation is highly advisable, including through the use of decision support systems.

Choice of evaluation method

The value for money objectives and choice of evaluation method need to be developed and agreed during the acquisition planning phase of the construction procurement process. This ensures the market approach method, criteria and respective weightings will reflect the price and non-price objectives in the schedule.

Based on this information, suppliers can make a calculated decision to tender for a project, depending on their chance of winning the bid. If the chances are low, the tenderer is likely to refrain from tendering, saving them time and money, but also saving time to the client agency in the assessment of the bids. If choosing to bid, the tenderer is then in a position to respond specifically to those criteria and include information that assists with risk assessment by the purchaser prior to contract award. In order for tenderers to provide the most fit-for-purpose bid, it is therefore important that they be provided with all the information needed to make decisions on how to best address the needs of the client agency.

It appears that, currently, while the list of award criteria is made clear in the tender documents, it is unclear if the respective weightings and the formula used to calculate scores and rank the tenderers are. Anecdotally, the Commission heard that they are not. Without that information, it is difficult for tenderers to structure their pricing. The Commission will examine these matters further with agencies.

The Commission also noted some instances where non-negotiable requirements (e.g. project to be delivered by a certain date or under a certain budget) have not been clearly articulated in the tender documents, leading to tenders not being considered despite tenderers investing significant cost and effort in the bid. It is critical for public authorities to clearly identify the non-negotiable parameters that render a bid compliant or not. This will reduce waste and frustration for suppliers and optimise the tender assessment.

The Commission observed in the random sample that each public authority uses a different formula (or set of formulas) to rank tenderers. The choice of a formula can influence the outcome of a tender. Therefore, it is important that the formula used creates a match between the preferences of the tendering entity and the outcome of the tender evaluation. At this stage, it is very unclear if public authorities achieve this match. The Commission will examine this further.

The use of relative scoring has been banned in some jurisdictions including Portugal,³⁸ the city of Rotterdam and the Dutch National Police because of its associated risk of rank reversal (non-competitive bids influencing the outcome of a tender). Yet, it is frequently used in South Australia (as it is in the Netherlands, Sweden and the UK). The Commission has started reviewing academic papers on the merits of different formulas used in supplier selection and will present its findings in the final report. The Commission has also observed, through the random 106 tender evaluation, examples where the intended outcome was distorted through the choice of a formula and will provide, in the final report, case studies to illustrate this point.

The Commission received feedback on the impact of the choice of evaluation method on the value for money outcomes:

Suggestions as to a process of consistent, best value bids are worth consideration. Consult Australia has long advocated for the use of a 'two envelope' system: separating price and non-price information, evaluating each bid according to the tender's [sic] ability to perform the work, before then moving to price considerations for those bids with the ability to perform the required tasks. This would drive a more diligent scoring system as it pushes value and experience more than price, giving a value-based selection rather than a price-based decision. (Consult Australia SA, p. 6)

Effectively drafted and appropriately weighted non-price criteria will elicit responses directly addressing the risks that are to be managed by the consultant/contractor.³⁹

This, in turn, supports the evaluation team to identify the tenderer that will best deliver the planned value for money and project objectives.

The Commission researched methodologies or mechanisms that may be used to incorporate other government objectives in the tender evaluation. The Commission notes that, in order to provide a smooth transition and promote greater acceptance of any reforms, changes to evaluation techniques or processes should, as much as possible, incorporate or be embedded in existing evaluation processes.

By engaging in practical and meaningful implementation, the quest for sustainability can be transformed from a perceived burden to an opportunity for innovation, development, and greater global social and environmental outcomes for both current and future generations.⁴⁰

The traditional methods for assessing non-price factors in tenders is to review the competency of the tenderer by reference to their experience, past performance, available resources and systems (capability).

³⁸ https://www.researchgate.net/publication/307575475_Conditions_for_rank_reversal_in_supplier_selection

³⁹ Scott Alden, Understanding the models for integrating sustainability into the procurement process, February 2018, p. 11. Available at <https://www.holdingredlich.com/blog/understanding-the-models-for-integrating-sustainability-into-the-procurement-process>.

⁴⁰ Ibid.

Methodologies for evaluating other objectives as part of a value for money assessment of a procurement include pricing methods that incorporate consideration of externalities including hedonic pricing and analytical hierarchy process. Sustainability and externalities may be integrated into the tender evaluation via hedonic pricing methods and analytical hierarchy process methods. The Commission will examine the practicality of such methods.

3.2.1.5 Measuring the achievement of value

As was done in Stage 1, the Commission has measured the performance of procurement of construction projects in South Australia against the European Commission’s value for money indicators (see Table 3.6).

Table 3.6: SA’s value for money performance for construction on EC indicators

Description	Measurement in SA	SA performance
1. One bidder indicator:		
Proportion of contracts awarded where there was only a single bidder in the competition (unsatisfactory > 20 per cent)	Commission’s data from random sample of 106 purchase recommendations from 6 agencies.	5.3 per cent of contracts awarded in 2017–18 involved a procurement process where a single bid was received. <i>SA meets the EC performance threshold for this indicator.</i>
2. No calls for bids indicator:		
Proportion of procurement procedures negotiated without being preceded by a published call for tender (unsatisfactory > 10 per cent)	Proportion of contracts awarded using a direct negotiation approach.	19 per cent of contracts awarded in 2017–18 involved a direct negotiation. <i>SA does not meet the EC performance threshold for this indicator.</i>
3. Aggregation indicator:		
Proportion of procurement procedures that involved more than one contracting authority (unsatisfactory < 10 per cent)	Data unavailable at a whole-of-government level.	<i>Unable to measure</i>
4. Award criteria indicator:		
Proportion of contracts awarded on the basis of price only (unsatisfactory >80 per cent)	Commission’s data from random sample of 106 purchase recommendations from 6 agencies.	In less than 2 per cent of cases, the contract was awarded based on quoted price only. <i>SA meets the EC performance threshold for this indicator.</i>
5. Decision speed indicator:		
Mean time between deadlines for receipt of offers and award of contract (unsatisfactory >120 days)	Data reported on timeframes	Average mean time of 105 days for the period 2017–18. <i>SA meets the EC performance threshold for this indicator.</i>
6. Reporting quality indicator:		

<p>Proportion of contracts awarded containing no information about contract value (unsatisfactory > 3 per cent)</p>	<p>Premier and Cabinet Circulars 27 and 13 include requirements on the publication of information on contract value. CEs can veto publication of contract information.</p>	<p>An average of 7 per cent in 2017–2018 of all contracts published on the SA Tenders and Contracts website contained no \$ value. <i>SA does not meet the EC performance threshold for this indicator.</i></p>
--	--	---

Sources: Anthony Flynn, 'Measuring procurement performance in Europe', *Journal of Public Procurement*, Vol. 18, Issue 1, pp 2–13 (2018); State Procurement Board, *Board Procurement Annual Reporting data for 2017–2018 (data reported by public authorities)*; SA Tenders and Contracts

South Australia rates about average, with good performance for 'one bidder only', 'award criteria' and 'decision speed', poor performance on 'no calls for bids/openness of tenders' and 'reporting quality', and no data received by the Commission on aggregation of contracts. This is a better result than the comparable assessment for SA goods and services procurement.

This assessment suggests some areas where additional value for money can be achieved, including: limiting the number of cases where direct negotiation is used; increasing transparency on the award of contracts; centrally collecting information on aggregated contracts; and periodically monitoring procurement performance across public authorities, which is currently limited by data constraints.

The Commission looked at contract variations as a measure of performance. Three public authorities reported on contract variations. Variations occurred in small, medium and large contracts, for reasons including changes in scope (the main reported cause), time extensions and design omissions (in a very small proportion of cases).

Strategic review

Determining the impact of procurement activity on the achievement of government objectives can be challenging given that procurement will likely be one of many policy levers used to influence a government priority.

Therefore, measuring the influence of each policy area requires a coordinated approach and comprehensive measurement framework.⁴¹

Information was sought from public authorities on how value for money is measured. The responses indicated that there are some project-specific performance measures included and reported on for individual construction procurement projects. These are particularly relevant when undertaking gateway reviews and reporting for governance purposes (for the project team, procurement committee and/or Parliamentary Works Committee).

That said, with the exception of reporting requirements for the SAIPP, at the whole-of-agency or across-government level there is minimal consolidated reporting on value for money objectives and performance. This may be partly due to a lack of ICT capability within and across public authorities that enables the capture, analysis and reporting of consolidated data. The Commission notes that there is no policy or mandate regarding the reporting of

⁴¹ OECD, *Productivity in Public Procurement: A Case Study in Finland*, 2019, p. 18.

value for money performance at a holistic level on a consistent, ongoing basis. This is consistent with the Commission's findings from Stage 1 regarding the lack of other forms of measurement and performance.

3.2.1.6 Commission's working conclusions and recommendations

Tender selection: Transparency in formulas and selection process

The European Commission, in its Financial Regulation applicable to the general budget of the Union,⁴² specifies that 'the tender specifications shall contain the following: (a) the exclusion and selection criteria; (b) the award criteria and their relative weighting'.

It is the Commission's view that more transparency on these matters would be useful in South Australia, in construction procurement by public authorities, in order to increase the efficiency of the process.

Acquisition plan

The Commission has been told that value can be lost from an acquisition plan done without due consideration. It notes the comments by DPTI on this point.

Other government objectives

As discussed in its final report for Stage 1 of the Procurement Inquiry, the procurement function is *increasingly being used as a tool to contribute to other government objectives. Those objectives or priorities have not, traditionally, been considered as part of a procurement 'value for money' assessment. There are numerous reasons why other government objectives are being incorporated into procurement activity including maximising the efficient use of scarce resources (both financial and non-financial), addressing externalities and other market failures, and ensuring the government's existing and future activities comply with the regulatory framework. The Commission notes the inclusion of wider objectives within the NSW and Victorian procurement regimes.*

Drawing these elements together, the Commission is inclined to propose a structured approach to achieving better value for money by requiring a clear specification of quantified minimum levels of government objectives for significant procurements that collectively are part of the requirements for a complying tender. Complying tenders would be evaluated for the best combination of fitness for purpose and whole-of-life costs. The Commission will consult on this suggestion with stakeholders in the coming weeks.

The Commission is seeking feedback and comments on its findings and proposed reform with respect to value for money and other government objectives.

3.2.2 Risk management

3.2.2.1 Background

Public infrastructure projects involve different types of risk, including design, site and construction, operation and markets, and political and regulatory conditions. Some risks are project specific, such as site risk, while others are system-wide. In addition, risks are not

⁴² http://ec.europa.eu/budget/library/biblio/publications/2018/financialregulation_en.pdf

uniform over the life of an infrastructure project, with risks being more numerous at the start-up phase of a project and generally less numerous during the operating phase. Effective risk management optimises the highest expected value to the community.

Effective risk allocation and management means that risks are borne by those most able to mitigate them; are efficiently priced; and are allocated in a way that shares the benefits and the costs of a materialised risk.⁴³

There are a limited number of ways that risks can be allocated. Risks can be:

- retained by the government;
- transferred to, and retained by, the private party;
- transferred to the private party but then reallocated to third parties, including to subcontractors, covering by insurance or passing on to end-users.⁴⁴

3.2.2.2 Approach taken

The Commission has considered the risk management approaches of both a public authority (DPTI) and a prescribed authority (SA Water) to understand how, in practice, construction procurement risks are managed and how risk-based approaches form part of construction procurement strategies of government departments.

DPTI

The department works with the construction sector frequently and in some depth and monitors current trends and issues within the sector. The level of engagement helps the department identify potential risks and ways to manage them.

It is clear to the Commission that risk management is a high priority in DPTI policies and practices. DPTI applies its corporate risk management framework (which includes its risk management policy) to procurement projects. The risk management framework covers:

- establishing the risk context
- identifying risks
- analysing risks
- evaluation
- treatment
- monitoring and reviewing risks
- communication and consultation.

DPTI's process flowcharts classify projects as simple and complex by financial thresholds: less than \$33 000, \$33 000 to \$220 000, \$220 000 to \$550 000, and above \$550 000. The

⁴³ Australian Productivity Commission of Australia, Inquiry Report, Public Infrastructure, No. 71, 27 May 2014, p. 123.

⁴⁴ E.R. Yescombe, 2007, *Public-Private Partnership: Principles of Policy and Finance*, Elsevier, Great Britain.

implications of the determination of the risk profile of a project and how best to allocate risk are summarised by DPTI in Figure 3.8.

Figure 3.8 – Matrix of contract options - project risk/risk transfer to contractor

<p>High Project Risk</p> <p>↑</p>	<p>High Risk/Low Transfer</p> <p>Tenderer selection ROI/Selected Prequalified tender field Price selection Part Tenderer selection</p> <p>Contract Forms <u>Traditional</u> (AS2124) – Fully documented with clerk of works supervision.</p> <p>Culture 'We strictly control you to ensure you meet our requirements'</p>	<p>High Risk/Shared Risk</p> <p>Tenderer selection Facilitated, staged value selection process exploring the potential relationship Tenderer selection</p> <p>Contract Forms <u>Managing Contractor - Relationship</u> (GC21) – open book, progressive price firming, Collaborative Deed, coach.</p> <p>Culture 'We trust you and together we will have stretch objectives, shared risk and reward, collaboration.'</p>	<p>High Risk/High Transfer</p> <p>Tenderer selection Selected prequalified tender field Value based selection Tenderer selection</p> <p>Contract Forms <u>Early Contractor Involvement</u> (ECI) – Constructability advice then guaranteed price and time, liquidated damages.</p> <p>Culture 'We need your advice early but then it's your job to deliver'</p>
	<p>Medium Risk/Low Transfer</p> <p>Tenderer selection Prequalified tender field Price selection Tender selection</p> <p>Contract Forms <u>Traditional</u> fully documented with supervision by PSCs and construction advisers.</p> <p>Culture 'We control you to ensure you meet our requirements'</p>	<p>Medium Risk/Shared Risk</p> <p>Tenderer selection Prequalified tender field Value selection Tender selection</p> <p>Contract Forms <u>Managing Contractor</u> (GC21) Open book, progressive price firming. <u>Construction Manager</u> (AS4122 PSC contract)</p> <p>Culture 'We trust you to work with us'</p>	<p>Medium Risk/High Transfer</p> <p>Tenderer selection Selected prequalified tender field Value based selection Tenderer selection</p> <p>Contract Forms <u>Novated Design Construct</u> (AS4300) – State documents important elements using PSCs, PSC's novated to contractor to complete design.</p> <p>Culture 'We will tell you what's important, then it's your job to deliver'</p>
	<p>Low Risk/Low Transfer</p> <p>Tenderer selection Public tender call Price selection Tender not tenderer selection</p> <p>Contract Forms <u>Traditional</u> (AS2124) – fully documented supervision by PSCs and random construction adviser visits.</p> <p>Culture 'We direct you how to meet our requirements'</p>	<p>Low Risk/Shared Risk</p> <p>Tenderer selection Prequalified tender field Price/Performance selection Part tenderer selection</p> <p>Contract Forms <u>Traditional</u> (AS2124) fully documented with role for PSCs in reviewing works for consistency with design <u>Design Construct</u> (AS4300) part documented.</p> <p>Culture 'We will direct and leave it to you as applicable.'</p>	<p>Low Risk/High Transfer</p> <p>Tenderer selection Selected prequalified tender field Value based selection Tenderer selection</p> <p>Contract Forms <u>Design Construct</u> (AS4300) with Principal's Project Requirements only.</p> <p>Culture 'We leave it to you to meet our requirements'</p>
<p>Low Project Risk</p>	<p>Low Risk Transfer</p>	<p>Transfer to Contractor →</p>	<p>High Risk</p>

Source: DPTI, Understanding DPTI Building Construction Procurement, Updated January 2012

Box 3.1 – DPTI shared risk principles

DPTI shared risk principles

Generic DPTI documentation for procurement involving building construction refers to shared risk procurement models. A range of principles and key considerations are associated with these models, and they are described in the documentation:

- *Risk and reward* – linking measured performance to a contractor risk and reward system. Good performance on achievement of milestones or management of contingency is rewarded by improved return, perhaps by using bonuses, while poor performance results in reduced return to the contractor. Reward can also be linked to innovation and continuous improvement. The generic documentation states that risk and reward initiatives have proved to be right in principle but difficult to administer in practice.
- *Damages* – liquidated damages are not often used in contracts as they are generally ineffective in social infrastructure projects where the actual commercial loss cannot be established or is very difficult to demonstrate. Exceptions are fit-out projects or revenue-earning facilities such as convention or entertainment venues.
- *Incentives* – can be built into contracts to encourage the contractor to meet selected government objectives (e.g. improved training opportunities for apprentices, trainees and graduates during the life of the construction or on landmark projects to encourage community involvement and ownership of the project in support of improved services or to achieve excellence in ecologically sustainable development).
- *Contractor role* – requires managing entrenched industry views and processes and the relationships between professional service contractors, contractors and clients. The approach requires open information sharing, shared problem solving and shared innovation.

Source: Department of Planning, Transport and Infrastructure, Understanding DPTI Building Construction Procurement, Updated January 2012

The Commission has not yet seen guidance for procurement officers on how to apply the principles in practice and will follow up with DPTI on this point.

SA Water

SA Water has a well-documented procurement risk management framework comprising:

- policy principles covering corporate objectives such as a category management approach and the broader community and environmental impacts;
- guiding methodology on category management, risk-based procurement, corporate procurement procedures and the limitation of liability framework; and
- corporate documentation to document category management actions, strategic supplier dashboard, regulatory and business plans and the corporate risk register.

Governance of procurement risk management is supported within the corporate governance arrangements for managing risk. A procurement risk register is part of the corporate risk register and is subject to monthly review cycles by category, procurement team and on an individual project basis. The review cycle includes an innovation focus.

The risk management processes cover:

- supplier financial health;
- supplier performance management;
- segmentation of suppliers;
- business planning;
- procurement plans;
- limitation of liability; and
- risk-based audits.

Box 3.2

SA Water – Example of risk-based procurement methodology

SA Water uses a risk-based procurement strategy which aims to simplify low-value, low-risk purchases using a centre-led approach. The risk-based procurement methodology is aimed at addressing the majority of business partner procurement needs by implementing overarching arrangements or panels of suppliers where many of the risks have been addressed and contract terms and conditions agreed as part of the establishment of these overarching arrangements with suppliers by the central procurement team. This approach makes economical use of SA Water's procurement capability as well as simplifying purchasing arrangements for business units.

Business unit representatives are trained in how to obtain quotes from suppliers under these arrangements and make recommendations for the associated purchases via a separate trained Procurement Delegate who either resides within the local business unit or is referred to the central Procurement Team, depending on the associated economies of scale.

Where overarching arrangements and panels are not in place, business unit representatives are trained to seek quotes from the market after conducting a complexity test. Where the complexity test identifies the purchase as 'simple' then the business unit representative may seek quotes from the market under a set of guidelines and make a recommendation to their separately trained Procurement Delegate or refer the purchase to the central Procurement Team who conducts a final quality check prior to awarding a contract.

Where the complexity test identifies the purchase as 'complex' or the value is greater than \$200 000, these purchases are referred directly to the central Procurement Team to conduct the procurement.

Source: Based on information provided to the Commission by SA Water.

3.2.2.3 Stakeholder feedback

Stakeholders feedback on risk fell into two groups: the allocation of risk between government and the head contractor; and between the head contractor and subcontractors.

External stakeholders believe the government is driven to minimise the risk it retains (without necessarily reducing or managing the total risk inherent in the project) through contract terms and conditions that transfer risk to other parties. External stakeholders unsurprisingly see this as unreasonable in key areas, exploiting asymmetries of information and power between contracting parties, and often resulting in project risk in those areas being transferred to those least capable of managing it. The view amongst the business sector is that this transfer inevitably results in a risk premium being built into the tender price. Businesses believe that public authorities are aware of the risk premium.

Consult Australia observed that some public sector clients are using their market power to adopt a position that presents systemic risks to the economy and to business confidence.

External stakeholders have also observed that if projects have uninsurable risks and liabilities, then these disincentives push contractors to the simplest, easiest and least innovative solution. The overall outcome in terms of cost and functionality (and missed innovation) can be sub-optimal for the state.

The Australian Institute of Architects (AIA) indicated that a recent DPTI review of consultant contracts found some examples that unfairly attribute risk to consultants. This includes levels of insurance exceeding the actual financial risk to the client and removal of established limits for liability. The AIA and other stakeholders are continuing to work with DPTI to address these issues.

3.2.2.4 Findings

The Commission has observed that application of risk ratings in construction procurement appears significantly better than that used for goods and services procurement, although significant improvements can be made. The Commission remains of the view that the guidance on risk management can to be improved across the sector.

The Commission found several similar issues in the management of risk issues for construction procurement to goods and services procurement in Stage 1 of this inquiry. They are shortcomings in data and reporting, risk allocation and guidance on risk management. The choices of delivery model and type of projects also have a bearing.

The Commission has found individual examples of good practice in the management of risk, such as SA Water. That said, the Commission also observes the current DPTI project classification is based on financial thresholds (see Figure 3.2) not overtly on a risk basis (noting some correlation between size and risk would apply). It is unclear at this point what role Figure 3.8 plays in practice in risk-based assessment by DPTI. To this point, a structured approach to treatment and reporting of risk has not been evident in the documentation reviewed by the Commission, apart from the approach undertaken by SA Water. In most cases, risk is dealt with on a project-by-project basis.

The South Australian Auditor-General's reporting and review of agency operations over the last four to five years has identified deficiencies in the design and application of risk

management. At this stage, on the evidence available to it so far, the Commission considers that risk management is well-recognised by agencies but remains an issue in construction procurement. DPTI's formal response to the Commission's information request came very late in the process of drafting this report and has not been digested.

Data and reporting

The evidence to date points to difficulties in DPTI's relevant management systems in retrieving and presenting information related to projects managed on the behalf of public authorities. The deficiencies, reflecting in part the design and age of the systems, are acknowledged at very senior levels in DPTI.

The absence of efficient systems, procedures and reporting increases the possibility that projects are not being managed effectively from a risk management perspective. The Commission has addressed this in draft recommendation 4.1.

Risk allocation

In its research, the Commission found governments approach the allocation of risk in one of two ways. The first considers the size of project or projects undertaken, while the second considers the nature of the relationship between the client and contractors.

In its inquiry into public infrastructure in 2013–14, the Commonwealth Productivity Commission found that, for large projects, Australian governments were increasingly consulting with industry over the way a project may be packaged (in terms of breakdown of work and size of contracts). This is done to ensure competition by:

- reducing overall project complexity — if the work is too large or complex, there may only be one or two suppliers able to complete the entire package of work;
- reducing the level of risk transferred to any one market participant — again, only a small number of suppliers may be able to take on the risk related to an entire project.

This is consistent with the briefing provided by DPTI on its forward pipeline of work. DPTI indicated that it is considering risk reduction by reducing the complexity of some projects by tendering smaller contracts for work to address issues like service relocations and other latent conditions prior to tendering the larger projects.

One stakeholder commented that current financial thresholds for large projects receiving some Commonwealth funding require national qualifications. They consider this requirement effectively excludes local suppliers that would have capacity to undertake disaggregated components if different project approaches were taken. The example given was the approach taken in building the Flinders Medical Centre in stages rather than the approach taken with recent larger projects that were tendered as a single project (e.g. the new Royal Adelaide Hospital).

SA Water has provided information to the Commission on its approach to managing the supply chain through major framework partners. These are suppliers considered critical to the operation of SA Water; part of the supply chain management involves framework partners achieving high levels of collaboration and integrity in the management of suppliers

and risk. This long-term supply system is also likely to increase the opportunities to seek innovative solutions, given the experience of other sectors.

Guidance

The Commission has reviewed the extent and content of guidance material on the DPTI intranet. The material is mostly technical and procedural, and it does not appear to reinforce methodologies that can be consistently applied across the organisation. Without this guidance, the consistency of risk ratings, mitigation and evaluation is likely to be less effective. The Commission will explore this matter further with DPTI in the coming weeks.

In addition, based on the Commission's review of tender documents and consultation with external stakeholders, the application of the existing risk management tools seems overly conservative. This could be remedied through better training and more detailed guidance material; however, it is possible that a cultural change program will also be necessary as the existing tool set seems adequate. The Commission will follow up with DPTI on these matters.

3.2.2.5 Working conclusions and draft recommendations

DPTI has advised the Commission that improvements to its risk management approach are being developed. Existing systematic issues are said to result in too high a focus on low-value, low-risk projects, a lack of data and reporting, a low level of strategic importance attached to planning for risk and managing it to support better procurement outcomes, and poor management of risk through the project supply chain.

Based on its self-assessment, DPTI believes improvements can be made in:

- ongoing engagement with industry more broadly;
- developing better models for risk allocation that improve outcomes for both the client and contractors;
- better understanding within the department and industry about the impacts of changes in scope and delay on major projects;
- greater focus on risk across the department in respect to the contract management phase of construction projects.

In summary, while there are good practices in some agencies, the Commission observes that the level of capability to manage risk has been a constraint to best practice in construction procurement. The system needs more capability in negotiating contracts to ensure that the appropriate balance of risk is reflected in contracts with suppliers (i.e. those that are best placed to manage the risk assume responsibility for that risk).

More skills and procurement capacity in agencies would improve risk audits, monitoring of supplier health and risk management aspects of business and procurement plans. The Commission makes observations related to organisational capability in risk management in Section 3.2.4.

The Commission sees merit in better recording the outputs of risk management efforts, such as by category of expenditure and by project delivery types, which would provide

information and insight into the purchasing profile and activities of government departments. In addition, project reviews following construction completion may well benefit from recording the outcomes of risks, where they eventuated for improvements to the process in the future.

This information is a foundation for identifying opportunities to continuously improve procurement and find whole-of-government improvement opportunities.

In terms of risk allocation to contractors in the supply chain for construction projects, the Commission considers that SA Water's approach to managing its supply chain by encouraging best practice among its tier 1 suppliers represents an opportunity to minimise the adversarial and risk-shifting approach on these projects. The approach recognises that the health of suppliers in the chain affects all other suppliers and shows how the client (government) expects smaller businesses to be treated.

3.2.3 Contract management

3.2.3.1 Introduction

This section focuses on contract management relating to construction procurement. It complements the earlier examination of contract management for procurement of goods and services in Stage 1 of this inquiry.

Effective contract management ensures the supplier and the public authority meet their contractual commitments to time, cost, quality and other agreed matters. It requires systematic and efficient planning, execution, monitoring and evaluation to ensure that both parties fulfil their contractual obligations with the goal of achieving value for money and the intended results for the community.

Feedback from stakeholders and consultation with public authorities raised:

- the impact on suppliers in terms of payment, risk and due diligence of head contractors;
- transactional approaches to contract management by public authorities that miss realising the full value; and
- shortcomings in the quality and collection of data and the use of systems to support management of contracts.

The Commission has relied on information from DPTI on their processes and information to support the findings in this section. For reasons previously mentioned, much of this information has yet to be incorporated into the Commission's analysis.

3.2.3.2 Approach taken

The management of contracts within DPTI is undertaken by relevant staff in the building management division in the case of building infrastructure and staff in the major projects division in the case of civil infrastructure. The management of the AGFMA contract is also performed by the building management division. The staff are supported by departmental management and oversight committees depending on the nature of the project, usually the type of infrastructure and significance in monetary terms.

Upon acceptance of an offer by suppliers and execution of a contract, DPTI starts a contract management process, which appoints a contract manager, ensures service continuity and transition issues are addressed, and organises the record keeping and payment schedule.

For some but not all projects, a contract management plan is developed, which becomes the primary document used by agencies to facilitate and document key strategies, activities and tasks. The plan ensures contractual obligations are fulfilled; facilitates a performance review of the contract; and monitors contract outcomes. While the SPB has mandatory requirements for contract management plans above \$4 million (GST exclusive), DPTI contract management plans are not mandated by value, risk or project.

Once the contract is established and arrangements have been put in place, contract management focuses on managing project risks, engaging with suppliers to deliver outcomes and manage performance issues, and gathering relevant user or stakeholder feedback.

3.2.3.3 Stakeholder feedback

Protection provided to subcontractors

The Commission heard numerous examples from businesses in Stage 1 and 2 of the inquiry of issues argued to affect subcontractors including:

- late payments to subcontractors by prime contractors causing significant financial stress for small businesses;
- assertions of insufficient due diligence by public authorities in selecting a prime contractor that may be at significant risk of failure – poor management of this risk may contribute to exposing subcontractors to serious consequences; and
- the shifting of risk down the supply chain to subcontractors.

Late payments

In their Stage 1 submission, the AMCA stated:

The client (government) considers that it pays the contractor (the builder) within 30 days, but fails to recognise, or put in place, any visibility that the businesses (sub-contractors) who:

- *supply the materials (which must be paid for from 7–30 days)*
- *pays the wages (7–14 days);*
- *build structure, install equipment, fixtures, finishes and fittings (that must be purchased and paid for) are paid in 30 days*

Notwithstanding the combined cost of material, payment of wages and the building and installing, comprises more than 75 per cent the total building project cost, being supplied by and paid for by sub-contractors – the sub-contractors, are not paid in 30 days.

In most cases, sub-contractors are not paid on time, regardless of what their contractual terms are under the sub-contract or related to any government policy.

The Small Business Commissioner has likened the payments terms and arrangements between sub-contractors and prime contractors as small business acting as banks for larger businesses. On the evidence from its consultations, the Commission considers both that there is some truth in this partial view, the complete picture includes the position for prime contractors in recouping contract variations. The difficulties in ensuring timely payments to subcontractors in construction projects is widely noted across Australia.

This issue also affects businesses in the design phase of projects. The AIA (Architects Industry Association) have indicated that delayed payments to architectural practices in South Australia place the businesses under significant financial pressure. Delayed payments can result from:

- the common practice of consultants being asked to continue to work on later stages of the project before the fee is agreed; if delays in invoicing and payment occur, this can cause cash flow problems for the businesses;
- variation to a consultant's fees, which invokes a special condition inserted into the standard contract that requires the consultant to continue working prior to approval of a variation;
- changes in procurement methodology, evidenced in the Transforming Health projects, with consultants expected to continue work while the projects were transferred from a managing contract to a design and construct contract. While this took place – a period of some months – no payments were made to the consultant.

Due diligence of contractors in the supply chain

The construction sector has a high rate of insolvencies and financial stress. This is due to the nature of the projects – the pyramidal supply chain, the length of the projects and length of time between achievement of milestones. Stakeholders have said to the Commission that better upfront assessment of supplier health and improved monitoring of contractors through the life of the project would mitigate the risks to government and business.

Stakeholders consider efforts by departments, through procedures such as due diligence checks, have not been effective to date in mitigating effects on suppliers in the industry. The Small Business Commissioner's submission stated that *'In each of the detailed investigations I have conducted, it is clear that proper and detailed financial due diligence of the failed contractor was not undertaken by the respective agencies.'*

The AMCA submission stated that in various state and federal enquires and reporting on building company insolvencies, statutory declarations on payments to subcontractors 'are more honoured in the breach than in the observance'.

Shifting risk to subcontractors

Stakeholders, including the AMCA, the CEPU and the Small Business Commissioner, have asserted all forms of risk are shifted through the building and construction contractual chain away from those most capable of managing risk down to those least capable of managing that risk. This claim deserves closer scrutiny.

These stakeholders assert that implementation of head contractor agreements imposes subcontract conditions that bear little resemblance to the contract with the client and the head contractor; and that the subcontractor has little or no bargaining power to negotiate fairer contractual terms. The Commission heard specific evidence on that point.

Use of standard contracts

Consult Australia and O'Connor's Mechanical Engineers and Constructors have identified that more frequent use of standard contracts would be an important reform to assist better contract management and project outcomes. Such contracts may reduce the need for costly legal review or negotiation and allocate risk and reward more efficiently.

Consult Australia have told the Commission that standard contracts for professional and technical services have been adopted to some extent by DPTI but they argue that, where agencies attach special conditions, the benefits of using a standard contract are reduced as it re-introduces the need for extended negotiation of the new terms.

Contract management

Business stakeholders consider DPTI work, and work for public authorities more generally, on the premise that in a building project for government work, the only recognised contractual relationship is between the client (DPTI) and the builder.

AMCA SA stated it was not aware that DPTI has processes in place to monitor consistent terms and conditions throughout the contractual chain, at the time of the issuing of head contracts and subcontracts, and their operation. It was also not aware of the proportional allocation of risk, or the application of the government's commitment to pay within 30 days. This information gap may be due to various reasons.

Specialist Contractors SA asserted that, up until recently, DPTI has taken little account of timely payment to subcontractors, the consistency of the scope of work through the contractual chain, the shifting of risk down the contractual chain, or the unconscionable contract terms placed on subcontractors that are at odds with the conditions in the head contract. DPTI does not sight, at any time, the final subcontracts from the builder to the subcontractor. It is not clear why they should do so. The Commission will take this up with DPTI in the coming weeks.

The Commission has been told that in many sub-contracts the role of the impartial, independent superintendent no longer applies. A main contractor appoints its own employee as a contract administrator. Even if a Superintendent is engaged, the common law obligations can be contracted out by a main contractor in a subcontract to remove the obligation for the superintendent to act fairly and justly. Both AMCA SA and Consult Australia have indicated that clauses of this type are common in larger commercial building subcontracts.

3.2.3.4 Findings

Head contractor relationship with subcontractors

Material provided to the inquiry makes clear the significance of this relationship, which appears to be central to financial difficulties encountered by contractors in the sector. The Commission notes the obvious point that for construction projects the government's relationship is with the head contractor, not with its subcontractors. In that sense, while the government's obligations are defined, the government has an interest in the stability of the industry, including subcontractors.

The key issues for subcontractors in public infrastructure projects are payments to subcontractors, financial health of head contractors and the allocation of risk in the contract, such as latent conditions.

The Commission was told that late payments, by both government and the head contractor, are significant issues. These issues are said to occur due to:

- the length of time between project milestones and the cash flow of head contractors;
- the poor level of information kept on work being done, completion dates and which party has done the work – this relates to the pyramid nature of the supply chain discussed earlier;
- poor financial management systems and lack of integration of financial systems of multiple parties to a project; and
- the terms and conditions used by departments to engage consultants and their role in the design phase of projects.

The Commission suggests there are at least three issues to address:

- appropriate allocation of risk in the contract that mitigates the overall risk that is distributed between the head contractor and subcontractors;
- efficient and timely payment of claims to minimise the impact on the head contractor and subcontractors; and
- potentially verifiable expectations on head contractors on payment of subcontractors.

The Commission was advised of policy steps being taken by government agencies to promote prompt payments. The matter requires further investigation.

Some stakeholders have proposed:

- Legislation to set maximum time for business-to-business transactions or through the South Australian *Late Payments Government Debts (Interest) Act 2013*. This is outside the Commission's terms of reference.
- requiring payments to subcontractors and suppliers to meet a standard 30-day term from date of invoice, unless validly disputed, as part of the department-supplier contract (invalidating the 'pay when paid' clause); and

- introduction of a Fair Payment Code enforced through contractual documentation or the IPP.

The Commission has also noted the use by other jurisdictions interstate of project trust accounts or trusts to ensure payment of both head contractor and subcontractors when milestones are achieved. Article 71 of EU Directive 2014/24 on procurement enables government agencies of member countries to manage the payment of all suppliers on construction projects. Stakeholders have identified the option of including a clause in the government's contract with the head contractor that provides the contract manager with the powers to demand a full list of third-party subcontractors or suppliers and proof of payment. The Commission is not aware whether the collection of this information is standard industry practice. Aside from the mechanism of contractual compulsion, the Commission considers that such information could be provided to the government as standard procedure.

The Small Business Commissioner has recommended options to reform and improve due diligence procedures of agencies and to ensure the effects of poor financial health or insolvencies are minimised in the industry:

- require the completion of a statutory declaration by the head contractor prior to signing the contract declaring that the entity is solvent, has no overdue tax debts, no overdue Return to Work SA payment or superannuation payments and no outstanding legal disputes over payments;
- where agencies utilise prequalification arrangements, reassess entities on a regular basis using up-to-date financial information;
- a centralized process where agencies can access contractor information;
- a statutory declaration by the head contractor detailing that all subcontractors and suppliers have been paid; and
- develop policy detailing government expectations, assessment requirements, contract and risk management and step-in arrangements including compensation of the parties affected by the failure.⁴⁵

The Commission notes that several of the Small Business Commissioner's recommendations are consistent with, or part of, the Commission's recommendations in Stage 1 that have been accepted by the South Australian Government.

SA Water have shown the Commission a sophisticated system of recording and monitoring supplier financial health and supplier performance and its performance on key contractual outcomes. Such a system may have some relevance to construction procurement in the wider public service.

The Commission has consulted with DPTI on the use of standard industry contracts, the inclusion of special conditions and other latent conditions that are in existence in the industry. DPTI is aware of the use of latent conditions clauses and has indicated that codifying clauses for use by industry would not be helpful. Rather, its view is it would be more productive to develop principles and ensure that they are applied to subcontracting by

⁴⁵ Small Business Commissioner of SA, submission, pp. 6–7.

head contractors. When tenders are being awarded head contractors would be required to demonstrate evidence that subcontracting arrangements comply with the principles.

Data and reporting

DPTI has a contract management system, which is primarily a contract register. It relies on manual updates to record all information and its accuracy against dates is unreliable from a data entry perspective. DPTI uses the SA Tenders website for the market approach phase of each construction project.

DPTI's internal procedures detail the various reporting elements that contractors provide through the course of projects. The reporting is not mandatory, unlike SPB processes for goods and services procurement. Apparently, most but not all contractors produce a monthly report on the performance of the project, covering: status on progress and program; finance; safety; quality; risks and opportunities; and issues such as environmental effects, community engagement and workforce participation.

A range of regular internal reports produced by DPTI provide a status update on individual projects and highlight issues and risks. These are sent to the PMO, the Major Projects Review Board, the Executive Committee of the Department and the CE. The Commission has not been able to establish yet from DPTI the purpose of the reporting and coverage of projects.

The detail provided by DPTI to this point does not provide any indication of the role that the contract management plan plays in the process. Contract management plans are defined in the process flowcharts for both building and civil infrastructure. The Commission has not been advised on what plans are used, what guidance is provided by the department to officers on their use, and any department or category reporting generated through monitoring of the plans. The Commission will follow up on these matters with DPTI in the coming weeks.

Management of contracts to increase value of projects

DPTI has advised the Commission that contract performance information mainly relates to reporting on issues identified by the prime contractor, such as expenditure and achievement of milestones. The information contained in the DPTI contract management template for simple construction projects does not contain any outcomes measures.

A performance rating meeting and subsequent Performance Rating Summary Report are used by DPTI to measure overall performance of the contract while the work is being performed. This information is provided to the contractor, DPTI Procurement, DPTI Contracting and DPTI project areas and can be used for:

- review of contractor prequalification level;
- general improvement of DPTI practices for future projects; or
- updating of DPTI contract-specific requirements and master specifications.

Lessons learnt meetings are used to identify what was done, what worked well and what can be improved.

The Commission will follow up with DPTI on the methodology for using contract management information and associated outcomes.

Evaluation of contract performance not undertaken/utilised

At the end of the project for significant contracts, a performance rating meeting between DPTI and the contractor is held, and a report is produced incorporating lessons learnt from the project. The lessons learnt report covers issues identified during the course of the project and how they were addressed.

The evaluation phase for building infrastructure is usually undertaken by client agencies. The Commission has sighted examples of close-out reports conducted by DHW for works conducted on behalf of that department. These reports provide insight into project outcomes, including financial and non-financial outcomes such as environmental impacts.

It is unclear to the Commission what roles the client agency and DPTI have in the evaluation phase, whether there is any duplication and the governance arrangements for evaluation. Accountability for evaluation and process improvements may be an area for reform to ensure value is derived from this process.

3.2.3.5 Working conclusions and recommendation

The Commission has heard stakeholders’ views on the effects of construction projects and contractual arrangements on businesses in the supply chain. The role of the head contractor is central.

The Commission has considered mechanisms to mitigate the effects of supply chain issues on subcontractors including the financial health of head contractors and the allocation of risk. The Commission supports DPTI’s suggested reform to develop principles and guidance for contracts between head contractors and subcontractors, compliance with which will be a condition of engagement of head contractors at the tender stage.

3.2.4 Capability

3.2.4.1 Introduction

The importance of procurement capability in construction

The Commission examined the capability of the public sector procurement cohort extensively in Stage 1 of this inquiry, making four recommendations aimed overall at supporting an effective and professional procurement community and taking a strategic approach to identifying and meeting current and emerging capability needs. Those recommendations have been supported by the government.⁴⁶ This section focuses on public sector construction-related procurement capability.

The Commission previously concluded that capability development must underpin the transformation from agency-specific transactional purchasing into strategic approaches to deliver optimised, state-wide value for money and to achieve wider government public policy

⁴⁶ ‘The South Australian Government’s Response to the South Australian Productivity Commission Inquiry into Government Procurement Stage 1’, Recommendations 2.9–2.12, pp. 11–12, available at: https://dpc.sa.gov.au/__data/assets/pdf_file/0009/109845/SAGov-Response-Procurement-Inquiry-2019.pdf.

objectives. The state's procurement professionals are key enablers to establishing and sustaining key long-term supplier relationships, optimising procurement processes and contractual arrangements and committing to continuous improvement.

The same applies to construction-related procurement activity. The duration, complexity, risks and benefits arising in relation to construction procurements are often more pronounced than those applicable to procuring and contracting for goods and services. State infrastructure can also substantially impact on the state budget and can generate significant economic and social benefits.⁴⁷

*Projects are getting larger and increasingly complex, and will require new approaches. How the public sector make decisions, handles procurement, selects contract models and handles risk will have significant bearing on the functionality and efficiency of our infrastructure.*⁴⁸

Some of the factors that informed the Commission's consideration of construction-related procurement capability are also in the Australian Infrastructure Audit 2019:

- poor planning and inadequate scoping which leads to poor business cases and sub-optimal procurement outcomes;⁴⁹
- the importance of establishing and maintaining effective longer-term commercial relationships built on trust and mutually beneficial outcomes given the duration of construction projects, particularly for larger infrastructure where the complexity of the project and types of contracts used (e.g. alliance and public-private partnerships) necessitate increased levels of collaboration and 'commercial symmetry'⁵⁰ between the public and private sectors;
- the use of subcontractors by prime contractors in major construction projects, which impacts small business participation and economic activity;
- the increasingly sophisticated standards by which the success of state infrastructure is measured, and the uncertainty brought by global interdependence and digital disruption, which demand more effective planning and strategic foresight than ever before;⁵¹ and
- public infrastructure investment, which has the potential to generate increases in GDP.⁵²

Infrastructure Australia observed '*the public service is undergoing a transition, which requires new skills and an increased focus on project management, contracting and*

⁴⁷ Infrastructure Australia, Australian Infrastructure Audit 2019, '4. Industry efficiency, capacity and capability – market depth and skills', p. 210.

⁴⁸ Infrastructure Australia, Australian Infrastructure Audit 2019, 'Executive summary', p. 19.

⁴⁹ Ibid, p. 236.

⁵⁰ Ibid.

⁵¹ Infrastructure Australia, Australian Infrastructure Audit 2019, '2. Future trends', p. 97.

⁵² Infrastructure Australia, Australian Infrastructure Audit 2019, '4. Industry efficiency, capacity and capability – market depth and skills', p. 210.

procurement.⁵³ The immediate challenges to public sector construction procurement capability are:

*Despite meaningful progress in key jurisdictions and large agencies, the public sector is inadequately skilled and resourced to undertake a high volume of sophisticated procurement activity, including the oversight of projects during the delivery phase. Inadequate public sector procurement expertise can result in the taxpayer being exposed to inappropriate risks or costs, and compromising the capability of projects to achieve user outcomes.*⁵⁴

These observations simply underscore the need for the state to have the people capability to effectively manage the state's construction plans, and that a structured and realistic procurement capability development plan will effectively support development in the future.

Given DPTI's lead role in public sector construction procurement established under government policy, its views are fundamental to the state's self-evaluation of capability. The views of Lead Agencies⁵⁵ regarding both DPTI's capability, and their own capability in the mandated collaborative approach to the state's building construction procurement are also important. Any contrasting views between DPTI's self-assessment and Lead Agency opinions may offer areas for focus in terms of future reform.

South Australian Public Sector Construction Procurement Capability Framework

Consistent with the statutory limitations of the SPB's remit,⁵⁶ the functions of the SPB that are relied upon to support procurement capability relate explicitly to 'procurement operations' as defined.⁵⁷ Unsurprisingly, the SPB's capability development framework does not address construction. The Commission commented on the SPB's existing capability framework, training opportunities, recruitment tools and associated reporting arrangements in Stage 1 of this inquiry.⁵⁸

Construction procurement capability across the system is split in line with the different roles of DPTI and lead agencies under the *Premier and Cabinet Circular PC028 – Construction Procurement Policy Project Implementation Process* (PC028).

PC028 makes DPTI the state's infrastructure agency and establishes infrastructure procurement as a separate stream from goods and services. DPTI considers that specialised, construction-specific skills are distinguishable from goods and services because building and

⁵³ Ibid, p. 212.

⁵⁴ Infrastructure Australia, Australian Infrastructure Audit 2019, 'Executive summary', Challenge #30, p. 45.

⁵⁵ 'Lead agency' is not defined in either Premier and Cabinet Circular 028 – *Construction Procurement Policy Project Implementation Process*, or the DPTI-administered *Construction Procurement Policy: Project Implementation Process*. It refers to public authorities who are mandated under those policies to work in collaboration with DPTI in relation to 'prescribed construction projects' as defined in the *State Procurement Regulations 2005*.

⁵⁶ *State Procurement Regulations 2005*, regulation 5 – Exclusions from definition of procurement operations; and *State Procurement Act 2004*, section 4, definition of 'procurement operations'.

⁵⁷ *State Procurement Act 2004*, section 12(1)(g), and indirectly sections 12(1)(b), (e), (f) and (h) relating to policies, principles and guidelines of public authorities; compliance; otherwise supporting or facilitating procurement operations; and advising responsible ministers on procurement operations, respectively.

⁵⁸ South Australian Productivity Commission, *Inquiry into Government Procurement Stage 1 – Final Report*, 9 August 2019, pp. 84–101.

civil construction projects need to be managed individually as bespoke projects as opposed to a category. The Commission accepts that assessment. Construction procurement has historically been undertaken by technical officers (e.g. engineers) with the technical expertise, who are also expected to be capable in project and contract management. DPTI notes the complexity of construction procurement can require the input of many staff to support the procurement of any given construction project.

DPTI has advised that capability development in construction procurement is supported by:

- DPTI capability framework: the department's corporate performance development arrangements – this framework does not include procurement capability specifically;
- on-the-job training: DPTI's strategy is 'to grow our own construction procurement professionals' by creating and actioning opportunities for junior staff in the procurement team or other procurement activity;
- SPB capability development: DPTI leverages training programs offered by the SPB and supports the undertaking of CIPS training; and
- tertiary qualifications: DPTI and UniSA worked together to develop postgraduate courses in project management/contract management to address the needs of the industry – DPTI currently has over 20 officers undertaking these courses.

Lead Agencies are:

responsible for the initial planning, budgeting and approval elements of the construction project and ultimately accountable for the management and operation of the asset that results. The Lead Agency is the project sponsor or 'owner' and ensures there is appropriate governance and that the project meets the requirements of government and agency strategic asset management plans. It is responsible for the provision of government services and consequently defines the extent, quality and location of services.⁵⁹

PC028 provides that in working with DPTI, Lead Agencies should not duplicate the construction expertise centralised in DPTI.

Lead Agencies may be accredited by DPTI to undertake construction procurement under PC028. DPTI has advised that accreditation is generally on a project-by-project basis, but that agencies are not accredited where DPTI believes the complexity of the work requires DPTI expertise not available in the Lead Agency.

DPTI is implementing an Agency Self-Management Approval Assessment Framework for Delivery of Lower Risk Construction Projects (the Accreditation Assessment Framework) which would account for additional requirements such as the non-infrastructure agency's approach to safety.

DPTI is accountable for the Across Government Facility Management Arrangements (AGFMA) through which non-infrastructure agencies can, in lieu of accreditation, procure planned small construction works for jobs greater than \$150 000 (excluding GST) but less than

⁵⁹ Construction Procurement Policy Project Implementation Process.

\$1 million (excluding GST). Small construction works under \$150 000 (excluding GST) are non-mandated under AGFMA. However, if an agency chooses not to go through AGFMA, then they must undertake the small construction works through DPTI. The Commission observes there is an inherent conflict of interest between DPTI's roles as evaluator and service provider.

DPTI has approved accreditation for Lead Agencies to manage 22 construction projects since September 2017 (four for building construction and 18 minor civil construction).

The next section explores what the Commission heard from the business community and industry, its analysis, and draft conclusions in relation to construction procurement capability.

3.2.4.2 What the Commission heard

The Commission heard business concerns over DPTI's construction procurement capability:

With greatest respect to the current staff of DPTI, SCSA is concerned that several organisational reviews and re-structures undertaken over the last five years has resulted in a significant loss of skilled staff with substantial corporate history. (Specialist Contractors SA)

Other issues relating to the tender process have arisen due to inconsistent expectations and procedures resulting from high staff turnover and significant change within DPTI in recent years. (AIA and ACA, Stage 1 submission)

Businesses submitted that a lack of capacity and/or capability has flow-on impacts on the tender process:

The AMCA SA is concerned that several reviews and re-structures undertaken over the last five years have resulted in the loss of skilled staff with a substantial corporate history. (AMCA)

A loss of expertise in client departments has resulted in poorly resolved briefs and a lack of alignment between DPTI and client department requirements. This can result in a lack of clear tender parameters. (AIA and ACA, Stage 1 submission)

ACA, Consult Australia and AIA SA been participating in discussions with DPTI to develop a new suite of SA specific contracts. This process has been protracted and after 4 years not resulted in an outcome. Consultant peak bodies were recently advised that the review was on hold for the remainder of 2019 due to the high volume of work and a lack of resources within DPTI. (AIA and ACA, Stage 2 submission)

The Commission has been advised that DPTI indicated in May 2019 that the revised target date for a new suite of contracts will be the end of 2019 or early 2020.

Skills and experience gaps

The Commission was told of specific gaps in construction procurement capability in contract management, risk management and procurement options analysis.

Capability gaps constrain the capacity to apply discretion in procurement. The less capable the team, the more the choice of the procurement model will reflect an allocation of risks to tenderers (even where the agency is better placed to mitigate them). For example, alliance models rely on the expertise, judgment and skills of the individuals involved and communication between the client and suppliers. In the absence of quality communication, design and construct requirements are mixed into the alliance arrangements which can then dilute the benefits and incentives of the alliance model.

The capability to ensure the right choice of procurement model is important. Different models require different levels of capability and capacity to deliver.

The Small Business Commissioner proposed that:

The State Government should expand and mandate its commercial acumen training program. This training program should be extended to all staff that are involved in major contract development and contract management areas. Key areas to focus on include:

- *Financial and risk management*
- *Key personnel background checks; and*
- *Regular review of risk management plans when risk changes. (Office of the Small Business Commissioner)*

Project briefs

DPTI advised that it spends an increasing amount of time assisting lead agencies to develop project briefs. An incomplete or insufficient project brief developed by the lead agency (for building infrastructure) affects the speed to market and consequential delays impacting on value for money.

DPTI advised the roles and responsibilities of the Lead Agency are critical at the project brief stage, and in signing off the design at relevant milestones (e.g. concept report). Throughout the concept phase and the detailed design phase, the Lead Agency project officer must attend design workshops and project control group meetings to manage the design development, contribute to scope-related decisions, and to ensure agency requirements are being met. DPTI indicated that waiting for the design to be completed prior to Lead Agency review and design rework can often be the cause of delays and additional costs.

3.2.4.3 Commission's view

Matching skills to requirements

The expectations for a public authority's procurement function has been changing over time as it has become an enabling function to achieve government objectives and improve organisational performance. Public authorities must specify, measure and manage a wide range of procurement activities that require a range of procurement and project skills and expertise that are ideally matched with the procurement activity. For example, low-value/low-risk transactions may be well managed by routine transactional procurement strategies and non-specialist procurement staff. More complex procurement requirements require a more 'relational' approach to procurement and contract management involving

market intelligence analysis, in-depth category knowledge, and sophisticated negotiation and contract management skills to support complex contractual arrangements.

Procurement professionals are increasingly required to assess 'value' and to incorporate non-financial (social and environmental) outcomes. A review commissioned by the SPB in 2018 on SPB policies and guidelines found that public authorities in goods and services procurement want further guidance on measuring and quantifying value for money in the evaluation process to give them the tools and skills to compare suppliers based on environmental and socially responsible indicators in addition to price and quality.

Developing procurement capability requires an understanding of:

- the nature of the procurement activity undertaken – such as where the activity sits on the simple low-risk/complex high-risk spectrum;
- the relationship with the market – direct, collaborative, cooperative; and
- how to choose the right procurement model options.

Developing the capability to steward these complex systems of various relationships, working with (and through) a full range of external providers, means we need to rethink individual competencies, organizational capabilities, and how we might reshape the enabling environment.⁶⁰

Public authorities have the task of effectively matching roles, skills and expertise to where they are needed most, and having appropriate enabling arrangements in place.

Agency feedback: existing public sector construction procurement capability resources

DPTI advised the Commission that although it has a central Procurement and Contract Management Directorate, the number of DPTI staff actively involved in procurement/contract management is several hundred given DPTI's core function involves procuring and contracting for infrastructure projects. Procurement staff are frequently involved in multiple projects simultaneously and their role often crosses over between the procurement and contract management phases. DPTI advised that it is not unusual for a civil infrastructure project to involve 50 staff to ensure adequate technical and specialist input.

Table 3.7 contains information on FTEs in public authorities who work in procurement and/or contract management.

Table 3.7: Current procurement and contract management FTEs by agency

Public authority	Procurement role	Part procurement role	Contract management specialisation	Construction specialisation
DCS	15	12	2 (of the 15)	1
DE	13		2 (of the 13)	
PIRSA	1.8			

⁶⁰ Janine O'Flynn, 'Rethinking relationships: clarity, contingency, and capabilities', *Journal Policy Design and Practice* Volume 2, 2019 - Issue 2: Perspectives on Capacity and Effectiveness in Policy Design.

Public authority	Procurement role	Part procurement role	Contract management specialisation	Construction specialisation
SATC	3			nil – contracted out
SAFECOM	1.8			
SA Water	40			
SA Health	53	64	5 (of the 5)	
DHW	1	2		
AGD	3			
DPTI				
<i>Civil infrastructure</i>	30		30 (of the 30)	30 (of the 30)
<i>Building infrastructure⁶¹</i>	4		4 (of the 4)	4 (of the 4)
DHS	14			
CAA	2			
DCP	5	18.8 ⁶²		
DIS ⁶³	4	64	64 (of the 64)	
DEM	6	39	39 (of the 39)	
TAFE SA	3			
DEW	4			
DPC	3			
DTTI	1		1 (outsourced)	
SA Police	6 + 2 part-time			9 ⁶⁴
TOTAL	209			

Source: Information provided by public authorities on request to the Commission.

The Commission observes:

- Most agencies were unable to advise on the number of professional procurement FTEs outside of the central procurement unit who have procurement and/or contract management as part of their role.
- Apart from DPTI there are few agencies that have professional procurement FTEs that specialise in contract management (work full-time on contract management).

⁶¹ DPTI’s building infrastructure day-to-day project and contract management responsibility is generally undertaken by the outsourced Lead Professionals Services Consultant.

⁶² Represents DCP’s Service Contracts and Licensing team responsible for contract management of out of home care arrangements.

⁶³ DIS and DEM contract manager numbers are individuals that are additional to procurement unit staff and are allocated as owning contracts in 2018 – some of these may be outsourced.

⁶⁴ Represents officers in SAPOL’s Facility Management & Strategy Unit and Capital Works Unit who work on project procurement.

- The information corroborates agency advice that their procurement staff generally work on both contract management and procurement (although some only do procurement process).
- The lack of construction procurement professionals outside DPTI reflects the current governance arrangements for PC028 (but raises questions about lead agencies' capability required to fulfil those collaborative requirements).

3.2.4.4 Current procurement construction capability frameworks

A procurement strategy that clearly links procurement capability with the government's objectives and priorities provides clarity to procurement professionals on their core and complementary objectives and how they can be achieved. A procurement capability framework consists of the key elements or components that support the delivery of organisational (public authority) outcomes, and in turn whole-of-government and state objectives.

Capability for goods and services procurement is supported through:

- the functions of the SPB in the *State Procurement Act 2004*, including 'to assist in the development and delivery of training and development courses and activities relevant to the procurement operations of public authorities' (section 12(1)(g));
- the responsibility of a principal officer of a public authority (chief executive or equivalent) to ensure that 'there is capability in the public authority to conduct procurement operations to standards required by the Board' (SPB Procurement Authority and Governance Policy); and
- the SPB Accreditation and Assurance Program, and various training and engagement initiatives.

The Commission has flagged the statutory limitations of the SPB (see Section 3.1.2) to exclude prescribed construction procurement projects valued over \$150 000 (excluding GST). The Commission acknowledges that public authority officers who attend SPB training and capability initiatives will be able to apply learnings to either goods and services or construction procurement as they may be applicable. A key consideration is, clearly, the extent to which construction is a specialised area requiring specialised skills.

DPTI procurement construction capability framework

DPTI does not have a specific construction capability framework. Its corporate capability framework (the framework) is designed to achieve 'optimised, safe and effective operations and workforce' and is constructed around five categories of capability: building relationships; personal attributes; achieving results; leadership and growth; and performance enablers. Each of the 'core capabilities' have 'performance enablers' applicable to each of the four streams (levels of seniority). An extract of the performance enabler of financial acumen is set out in Table 3.8.

Table 3.8: Extract from DPTI Capability Framework – Financial Acumen Performance Enabler

Performance enablers	Stream 1: team member	Stream 2: leader	Stream 3: senior leader	Stream 4: executive leader
Financial acumen	Has good numeric and financial skills. Understands and follows appropriate financial processes within their delegation.	Has a sound understanding of budget management and DPTI procurement processes to drive value for money. Acts within delegation.	Has a thorough understanding of financial forecasting and budget management for the section. Manages budget efficiently and responsibly within delegation and DPTI procurement processes.	Applies strategic management of financial and budgetary compliance and governance responsibilities.

Source: DPTI Capability Framework

The Commission notes that the framework is designed to be used by all individual DPTI officers who, after identifying which of the four streams is most appropriate for themselves based on their role and classification, will then review the capability requirements and expectations and use the information for their individual performance and development plan.

Construction procurement capability frameworks in other jurisdictions

Table 3.9 summarises the procurement capability frameworks that are currently implemented in other government jurisdictions in Australia.

Table 3.9: Other Australasian procurement capability frameworks

Jurisdiction	Capability framework	Description
New South Wales	NSW ProcurePoint Training	Provides tools and guidelines including: <ul style="list-style-type: none"> ➤ an online tool to determine what training may be best ➤ foundational procurement training – online and professional development opportunities ➤ intermediate procurement training – Institute of Public Administration Australia (IPAA) training ➤ advanced procurement training – diplomas (through IPAA) ➤ procurement systems training – eProcurement and systems training ➤ community of practice – quarterly meetings ➤ ICT procurement training – specific to ICT procurement skills ➤ construction procurement training – GC21: general conditions of contract for construction face-to-face training open to government and suppliers (at a cost of \$600), MW21 training – available on request ➤ procurement role descriptions – provides information on roles and links to capabilities for that role.

Jurisdiction	Capability framework	Description
	Procurement Professionals Capability Set	Intended to be used in conjunction with the NSW Public Sector Capability Framework. Provides a description of the capabilities required for successful performance for procurement roles. Consists of 10 categories with capabilities varying according to 5 different levels. Developed by the NSW Public Service Commission and applies to all procurement activity (whether goods, services or construction).
Victoria	Procurement Capability Framework – applies to goods and services	It provides a consistent outline of the knowledge, skills and attributes required by procurement practitioners in the Victorian Public Service (VPS) to operate at a level that ensures the following VGPB policy objectives are met. Capability is devolved to the agencies who use the framework to assess and match roles and responsibilities to capability behaviours. Incorporates a Complexity and Capability Assessment Policy and Guideline that maps capabilities against the VPS Employment Capability Framework. VGPB are in the process of updating the framework to incorporate future skills development and to enable transferability of procurement capability between construction, infrastructure, and goods and services procurement.
	Guidance for Public Construction Procurement in Victoria	Public construction procurement comes under the <i>Project Development and Construction Management Act 1994</i> (Vic). The Assistant Treasurer is responsible for construction procurement and Ministerial Directions set out the key principles and mandatory requirements. Various tool kits, guidance documents are provided on the DTF (Vic) website. Reference to mandatory capability requirements and principles (including particular reference to capability's role in continuous improvement) is provided in the directions and guidelines.
Queensland	Procurement Capability Strategy – 'Skills2Procure'	Responsibility of the Chief Procurement Officer Qld. Qld procurement is structured as a single framework with 6 categories including building construction and maintenance. Procurement training is provided via the Skills2Procure framework that provides access to formal and informal training and development opportunities for staff undertaking procurement and contract management related roles and tasks. Incorporates: <ul style="list-style-type: none"> ➤ procurement certification training – in partnership with IPAA and NSW, staff can undertake nationally recognised qualifications and certifications across 4 levels ➤ procurement learning and development panel (for short course training) ➤ procurement leadership council – participating agencies can access the Gartner Procurement Leadership resources ➤ whole-of-sector programs – Queensland Treasury partners with UQ to deliver workshops and programs, and Enterprise Leadership Program QUT (includes innovative offers training) ➤ continuing professional development – accessing professional development opportunities outside Qld government (CIPS, IFPSM, IACCM, etc).

Jurisdiction	Capability framework	Description
		In addition to the above, Qld procurement has developed in-house codes to track procurement capability to assist with risk management and future considerations.
Western Australia	Procurement Capability and Training	<p>Procurement capability initiatives and training to support goods and services procurement in WA public sector include:</p> <ul style="list-style-type: none"> ➤ public sector procurement awareness and training programs ➤ community services sector capability awareness and training ➤ information sessions for private sector ➤ capability resources developed in consultation with WA public sector ➤ sector engagement on capability improvement initiatives ➤ online module training. <p>Capability resources include a procurement competency matrix (PCM) which is aimed at assisting with the alignment of sector-wide strategies for the procurement workforce and succession planning, staff attraction and retention, capability development and performance management. PCM identifies and defines the technical procurement competencies required by procurement professionals in the WA public sector. The PCM is co-branded with the Public Sector Commission (PSC) and was developed in conjunction with agencies across the Western Australian public sector.</p>
New Zealand	NZ Procurement – Improving Your Procurement Initiatives	<p>Aims to build strategic procurement capability to help raise the procurement skill levels across the state sector. Offers 4 key elements, of which 2 are:</p> <ul style="list-style-type: none"> ➤ training and education – provide opportunities for graduates, online training course and regular information sessions for public procurement officers ➤ Procurement Capability Index – a self-assessment tool that agencies are required to use to measure and report on their PCI. Provides senior leadership with an evidence-based assessment of agency strengths and opportunities for improvement. Comprised of 27 elements across 8 categories that include leadership, talent management and delivery management. <p>Several guides and tools are available expressly for construction procurement, including for capability matching, risk management and procurement strategy.</p>

Source: SAPC interjurisdictional analysis

With respect to other jurisdictions, the Commission observes:

- Most jurisdictions have a capability framework with information and guidance on capability initiatives at the individual, organisational and jurisdictional levels.
- The scope of the frameworks depends on the jurisdiction’s underlying regulatory framework, but most can apply to goods, services and construction projects.
- Procurement capability initiatives are often linked to the jurisdiction’s equivalent of the Office of the Commissioner for Public Sector Employment by way of a capability framework for the public service.

- All provide initiatives/training partnered with, or outsourced to, third party training and education providers including associations or universities/TAFE.
- Frameworks may include strategies to address the different capability challenges from attracting and retaining skilled staff through to upskilling existing staff.

The Commission notes that the government has already accepted the Commission's recommendation from Stage 1 (2.10) about developing a strategic plan for procurement capability development. Having now considered construction procurement capability the Commission is of the view that a strategic and planned approach to construction capability development is also required. The government has also accepted the Commission's Stage 1 recommendation 2.9 to sponsor a community of practice for heads of procurement professionals including the potential establishment of sub-committees to focus on specific procurement areas.

Draft recommendation 3.1 (supplementary to Stage 1 recommendation 2.9)

In order to strengthen procurement capability among smaller prescribed authorities, the Commission proposes that the Heads of Procurement Community of Practice be expanded to prescribed public authorities not currently included; and include a standing construction procurement sub-committee to address construction-related issues for public authorities and prescribed public authorities.

A construction procurement capability strategy also needs to address how technical (construction) staff and procurement staff can work together to achieve optimised outcomes. This may include additional procurement-specific skills for technical specialists and advisers (e.g. engineers) to give them a potentially improved understanding of procurement and contract design and management requirements. There may be value in exposing procurement professionals to confined but value-adding technical knowledge to improve their understanding of the specific technical aspects of a procurement process (such as legal and contracting principles). The Commission's intention here is to support all public authority participants to contribute to a rigorous and efficient procurement process.

The strategy also needs to address the capabilities required by lead agency representatives in fulfilling their project sponsor role under the Construction Procurement Policy: Project Implementation Process. Some of those skills are not necessarily procurement specific but are important in the overall outcome of the project and the lead agency's accountability and include, for example, business case drafting and project management skills. An adequate understanding of the technical aspects of the specific procurement being undertaken would also be advantageous and contribute to transparency and validation throughout the project's phases.

Draft recommendation 3.2

In order to ensure all key areas of procurement capability in the South Australian public sector are addressed, the capability development strategy agreed by the South Australian Government in its response to the Stage 1 final report be expanded to construction procurement and specifically address issues including:

- incorporating the construction discipline-specific technical expertise and procurement and contract management proficiencies across all public authority staff involved in construction-related procurements; and
- the supporting capabilities required by Lead Agencies to effectively fulfil their project sponsor role mandated under *Premier and Cabinet Circular – Construction Procurement Policy: Project Implementation Process (PC028)*.

3.2.4.5 Developing a construction procurement capability strategy

The Commission has considered several specific capability areas or enablers and identified examples, including from interstate consultations, to support the Commission's proposed recommendations for construction and wider procurement capability development.

Risk management

The Victorian Government Purchasing Board (VGPB) 'Complexity and Capability Assessment' policy and associated tools and guides demonstrate how complexity and capability interweave in the pursuit of achieving value for money. This approach requires public sector agencies to undertake assessments of capability subject to sophisticated assessment criteria and determine a score which informs whether internal or external capability building is required. People, technology and process are assessed, among other contributing factors.⁶⁵

The Commission considers this approach is a key underpinning of devolved procurement where chief executives are accountable for their procurement activity. This is further supported by system-wide reporting⁶⁶ that provides transparency and maps trends and highlights areas where public authorities may require additional focus on risk management.

Contract management

The Commission found that the issues it observed in relation to contract management for goods and services were also observed in Victoria by the VGPB. In brief, the VGPB indicated that government audits have identified contract management issues arising despite a successful acquisition process. The issues are focused around the absence of continuity of contract management from acquisition through to the management phase of the contract, and with risk and additional costs emanating once control of the contract passed from procurement function to business units. VGPB considers these issues are best addressed by

⁶⁵ Victorian Government Purchasing Board, 'Complexity and Capability Assessment Policy', available at: <http://www.procurement.vic.gov.au/Buyers/Policies-Guides-and-Tools/Complexity-and-Capability-Assessment-Policy>

⁶⁶ See for example 'Procurement complexity', VGPB Annual Report 2017–18, pp. 21–26.

each agency, and each agency's accountability and ownership of contracts is crucial in such a devolved system.

The Commission considers there are a variety of reasons for these common contract management issues. A lack of early involvement of the business unit during the acquisition phase, poor handover processes between procurement function and business unit once the contract has been entered into, and the need to better develop contract management capability at business unit level are all relevant considerations. Structurally, a category management approach, which tends to see more centralisation of the contract management function and earlier buy-in from contract users, i.e. business units, may mitigate these issues (noting the experience of SA Water). The concerted efforts to lift contract management capability in other jurisdictions are explored below.

Community of practice

The VGPB coordinates a community of practice that meets four times a year and has grown over the last few years from 30–40 to over 200 participants. The forum is leveraged to share common interests, case studies and best practice, and often invites academics or industry specialists to share innovative practices from overseas and the private sector. The group is also leveraged to communicate and raise awareness on procurement related matters such as upcoming free trade agreements and policy or guidance reforms, and to disseminate and discuss common issues arising from audit activity.

Qualifications and skill mix

Despite the value some PPAs and prescribed authorities have identified in having staff with procurement-specific qualifications (e.g. MCIPS), the Commission has also observed more diversified approaches to qualifications for procurement staff.

DPTI advised it is desirable but not essential for staff working in procurement to have formal procurement qualifications. Given the limited formal programs available for the development of procurement capability, DPTI leverages SPB training programs and supports officers who have, or are undertaking, CIPS accreditation. DPTI noted that most procurement courses are geared more towards goods and services procurement, rather than construction procurement. DPTI has collaborated with the University of SA to develop postgraduate courses in project management/contract management, and also embeds technical staff in projects to develop their procurement capability. This is a positive element: it is unclear at this point how much use is made of this facility.

Victoria has not adopted procurement industry accreditation as a baseline for procurement capability. Instead they have acknowledged the diversity of backgrounds, skills and experience that can positively contribute to the procurement cohort skill mix. The VGPB is in the process of updating their procurement capability framework and is focusing on core procurement skills such as commercial acumen, negotiation and contract management to support procurement professionals across government. The framework is structured around three levels of proficiency (basic, intermediate and advanced) with accompanying behaviours. The new framework aims, inter alia, to increase transferability of procurement capability between construction, infrastructure, and goods and services activities.

Queensland's Procurement Certification (Skills2Procure) program offers procurement-specific training up to Advanced Diploma level. A range of whole-of-sector short courses are also offered in collaboration with the University of Queensland focusing on procurement and finance. Other resources include the Procurement Leadership Council (offered primarily for the four largest procuring agencies), which provides access to procurement professionals from the world's leading companies and benchmarking tools and best-practice resources. There is also the Procurement Speaker Series which builds advocacy for procurement as a profession and highlights the importance of procurement to government. The Queensland public sector's Strategic Workforce Council is deploying awareness training and whole-of-sector programs focusing on project management including procurement in practice.

Queensland is also interested in exploring cross-government procurement staff exchanges and similar industry/public sector exchange opportunities, particularly on a category basis. The Commission notes the opportunity for South Australia.

The Commonwealth Government's inquiry into its role in city development recommended *'that the Australian Government, in conjunction with State and Territory Governments, establish a national training program for public sector infrastructure procurement'*. The House Standing Committee identified a need to take wider and longer-term views when assessing infrastructure to ensure *'that return on investment should be calculated over the life of the infrastructure ... and that cost-benefit analysis should be required to take into account wider economic, social and environmental benefits associated with individual infrastructure projects within a broader planning framework'*, among other things.⁶⁷

The evidence heard by the Committee that 'project appraisal methods should be consistent with a broader and more sophisticated view of procurement' is consistent with what the Commission has heard about transitioning procurement capability from transactional skills to supporting strategic approaches requiring more holistic perspectives and commensurate qualifications, skills and experiences. The Australasian Procurement and Construction Council (APCC) is also supportive of a multi-disciplinary approach to resourcing public sector procurement activity.⁶⁸

This perspective has been validated by a report commissioned by Consult Australia which recommended practical next steps:

the mixture of expertise required to undertake a successful procurement, governments should consider restructuring procurement teams to encourage the key players to work collaboratively. Together, legal experts that understand contracting, insurance specialists, practitioners with project experience and procurement experts can evaluate value for money and

⁶⁷ House of Representatives Standing Committee on Infrastructure, Transport and Cities, 'Building Up & Moving Out', Inquiry into the Australian Government's role in the development of cities, pp. 405–406.

⁶⁸ Future Procurement Skills Requirements – A More Strategic Procurement Approach (August 2018), p. 17, available at: https://docs.wixstatic.com/ugd/473156_002d1f7cccc24163a12dc17fe28cd17e.pdf

*appropriately tailor procurement processes, contracts and delivery models to the objectives of a project.*⁶⁹

Recruitment and retention

The APCC identifies strategies to support recruiting and retaining procurement professionals in this transitional environment. It recommends embedding recruitment and retention strategies into ongoing management activity, career management frameworks and rotational programs, and fast-track talent management programs to support high-performing procurement professionals.⁷⁰ These types of strategies may go some way to addressing the apparent leakage of public sector procurement professionals to the private sector that some public authorities have indicated to the Commission is a current challenge.

It is the Commission's view that SA can do a great deal better in building a professional discipline in public procurement. Elevating procurement to a strategic and high-value function within public authorities and prescribed public authorities is likely to attract and retain high-performing individuals to engage in procurement activity and would also complement the multi-disciplinary procurement team approach. In short, it means building a government procurement profession in South Australia.

There are several aspects that could give effect to this, including: staff rotations; fractioning individual employee's duties between their existing role and the procurement function; and confined restructuring of agency operations. Given the emphasis on high performance in this model, the Commission favours approaches where employees are invited or enticed to be involved and bring their initiative and new ideas to develop and grow the procurement profession.

3.2.5 Engagement with suppliers

3.2.5.1 Market engagement

The Commission explored market engagement in Stage 1, focusing on public authority knowledge of the marketplace and supplier capability; information provided to suppliers during the tender process; and information on future procurement needs of public authorities.⁷¹ The Commission made four recommendations arising from its examination of these issues that have been agreed to by the government. Those recommendations variously covered increased availability of information regarding supplier capability and future government procurement opportunities (2.3, 2.4 and 2.6), and an industry engagement guideline for government buyers encouraging effective market engagement (2.5). The commitments by the government include:

- the development of a revised Meet the Buyer program that will include agency involvement and have specific forums for 'start-up' businesses;

⁶⁹ Deloitte Access Economics (commissioned by Consult Australia), 'Economic benefits of better procurement practices', 2015, p. 59, available at: <https://www2.deloitte.com/au/en/pages/economics/articles/procurement-balancing-act.html>

⁷⁰ Ibid.

⁷¹ South Australian Productivity Commission, *Inquiry into Government Procurement – Stage 1 – Final Report*, pp. 65–75.

- continuing regular 'supplying to government' workshops with interested businesses to improve their understanding of the public sector procurement process. Agencies will be engaged to participate in these workshops;
- creating linkages between the Industry Capability Network and other supplier information;
- developing improved guidance and training for agencies on industry engagement, to encourage effective engagement with suppliers, including providing feedback to suppliers; and
- improving agencies' compliance with the requirement to publish a forward procurement plan.

The Commission has received additional information from business and agencies as part of Stage 2, which is set out below. In addition, the Commission has conducted qualitative analysis of market approaches, including in relation to construction procurement, based on its data holdings, which are explored in this section.

3.2.5.2 What the Commission heard

In response to the Commission's Stage 2 issues paper some of the submissions received offered additional views in relation to market engagement. The AIIA commented on market engagement, proposing new alternative means to access government procurement information:

While a number of education and meet the buyer events and mechanisms already exist, other channels of engagement should also be considered. For instance, informative youtube clips may provide an additional and highly accessible avenue for educating new and incumbent suppliers to government – not just to inform on general principles and available services, but also on any new policies or changes in procurement requirements (such as for instance the economic contribution test). (AIIA submission, p. 6)

And from an innovation and collaboration perspective:

engagement could range from pre-procurement workshops to inform specific tenders, to wider industry-specific dialogue on opportunities to improve outcomes and cater for innovation and technology change for both government and suppliers, an open panel to engage on what works/what doesn't in current ICT procurement and contracting processes, and an open conversation on how to achieve better outcomes for both government and suppliers, as well as the State at large. (AIIA submission, p. 9)

The architecture industry expressed a view on the fairness of market approaches:

There is a perception that some recent consultancy tenders have been structured to achieve predetermined outcomes, with criteria effectively precluding sectors of the prequalified consultant practices. It is recommended that client departments, through DPTI, opt for a selected tender process in these instances, as opposed to an open ROI. Where an open tender process

is required by the Government's procedures or the client department, criteria should be written to enable prequalified local consultant practices to have an equal opportunity to bid for the work. (AIA and ACA submission, p. 5.)

This is generally the result of the requirements for previous experience being limited to projects that exceed the value of projects recently delivered in South Australia. Ensuring that previous project experience requirements can be met through projects delivered recently in South Australia. Project value is not the only measure of capability, with complexity and project type being important considerations. (AIA and ACA submission, p. 6)

This comment was reinforced by Consult Australia:

The selection process could also be structured to prevent keeping bids alive when they have no realistic prospect of success. (Consult Australia submission).

Feedback provided by businesses on SA Tenders also mentioned tender requirements that can exclude SMEs from competing effectively in government tendering processes:

For SME's trying to get considered for government work, there is always a strong criteria for having undertaken that type of work for government. That leads to a Catch 22 situation. If you haven't worked for government, you can't get work for government. (in SA Tender survey 2017)

The Commission has observed this in a small number of projects from the 106 random tenders. In a majority of tender evaluations, the combined weighting of 'experience' and 'capability and capacity of key personnel' is between 25 and 45% of the total score (out of a total non-price criteria weighting of 45 to 55%). For a few projects, 'capability and capacity of key personnel' has been evaluated in relation to the previous project experience of the team (size and complexity of projects); therefore, the score gap appears to be unsurmountable between SMEs and tier 1 businesses.

The Commission will follow up with agencies to better understand the weighting process used in those cases.

Going beyond those specific examples, and to address the concerns raised by businesses, the Commission will seek information on how agencies can achieve better matching between the market approach chosen and the fairness provided to the targeted pool of suppliers to compete for the work. For instance, in those cases where client agencies are after a very specific set of experiences, a selected tender process should be chosen instead of an open tender, avoiding unnecessary costs for less experienced tenderers. If it is not the case, the evaluation panel should set the bar, for each criterion, at a level that can be met by SMEs willing to participate.

DPTI feedback

The Commission asked DPTI for its views and the approaches it uses in relation to market approach for construction procurement.

DPTI advised it has a mature and open relationship with industry and key DPTI officers regularly meet with industry representatives. DPTI advised that balancing state and industry interests is an ongoing challenge. Meeting and managing the expectations of large contractors, SMEs, designers, architects and other professional service providers requires ongoing commitment, particularly regarding value for money and apportionment of risk.

DPTI supports 'Meet the Buyer' events, works closely with the Office of the Industry Advocate and engages with industry bodies to discuss upcoming construction procurement opportunities. DPTI participates in industry forums, including the Civil Contractors Federation SA (CCF), the Australian Construction Industry Forum (ACIF), Master Builders Association (MBA), Consult Australia and the Association of Consulting Architects Australia (ACAA).

The prequalification framework for building and transport infrastructure projects is one of the main initiatives to improve supplier capability for construction procurement. DPTI advises it works closely with suppliers to address prequalification requirements. It reviews the procurement strategy for each procurement and the best method of engaging the market is determined having regard to market conditions, and the value and risk of the procurement.

Where appropriate, construction tenders specifically nominate prequalified supplier categories in line with DPTI's prequalification scheme to encourage prime contractors to engage with local businesses/SMEs who are prequalified. DPTI also indicated it encourages local suppliers to participate in regional construction procurements and participates in regional procurement roadshows. The Commission has not heard from regional stakeholders on those points.

In DPTI's Projects Pipeline Industry Briefings in recent years the minister, chief executive and senior DPTI representatives have provided an overview of the state's upcoming and future capital projects, including proposed delivery models, timeframes and information on tendering opportunities for industry. DPTI indicated that its market analysis and supplier capability is tailored not only to attract the best field but also to ensure that local SMEs get the opportunity to participate.

Other (Lead) Agency feedback

Lead Agencies generally indicated that market analysis and engagement is undertaken by DPTI in relation to their projects. Some Lead Agencies told the Commission that they do their own market analysis, which is passed to DPTI, and do their own engagement through industry forums and meetings with key stakeholders. Lead Agencies support DPTI with industry briefings and managing contractor project-specific supplier events.

The Department for Education indicated it engages and collaborates with other jurisdictions and industry about alternative delivery models. The example cited was a collaboration with Victoria regarding a possible delivery model that offered faster delivery of schoolrooms.

The Department for Health and Wellbeing (DHW) advised it had a network of Professional Services Contractors which helped to identify potential new suppliers and technologies. It also receives direct approaches from suppliers to present their products or services. DHW holds various memberships with organisations and associations such as the Australian Institute of Project Managers (AIPM), Australasian Health Infrastructure Alliance (AHIA),

Australian Health Design Council (AHDC), Institute of Healthcare Engineering (IHEA) and the Green Buildings Council of Australia (GBCA) to understand the market.

Prescribed public authorities' feedback

SA Water advised it keeps the communication channels open with its suppliers through a range of activities (see Figure 3.9). It has a well-considered, structured framework for engaging the market and understanding its capabilities.

Figure 3.9 – SA Water communication with suppliers



Source – Extract from SA Water presentation to the Commission (July 2019)

SA Water has also implemented a supplier relationship management strategy, including:

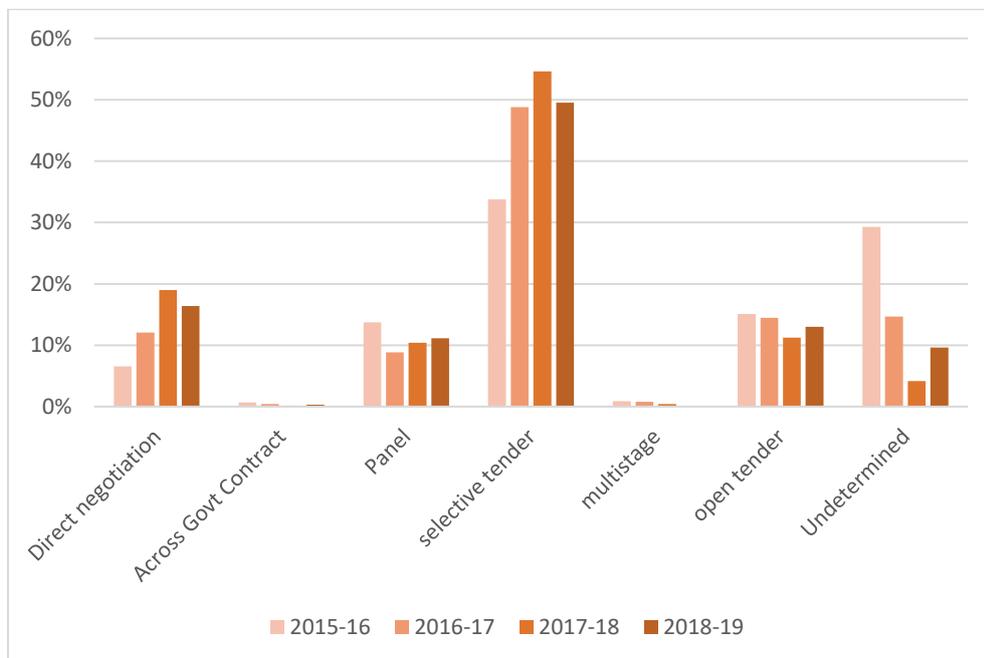
- annually identifying its strategic suppliers;
- recording information on its strategic suppliers, including through profiles, a supplier performance management tool and a contractor management system;
- evaluating its strategic suppliers through performance and risk scorecards (including level of satisfaction and regular financial viability assessments);
- engaging with its strategic suppliers through annual or biannual meetings; and
- reporting on its strategic suppliers through a supplier management dashboard.

3.2.5.3 Observations from the data on market approach

Many comments have been received from business stating how hard it is for new entrants to participate in government procurement. The Commission looked at market approach

information from the database it compiled from ten public authorities' data. The findings are described in this section.

Figure 3.10: Evolution of public authorities' market approach in numbers over time (contracts above \$150k excluding GST)



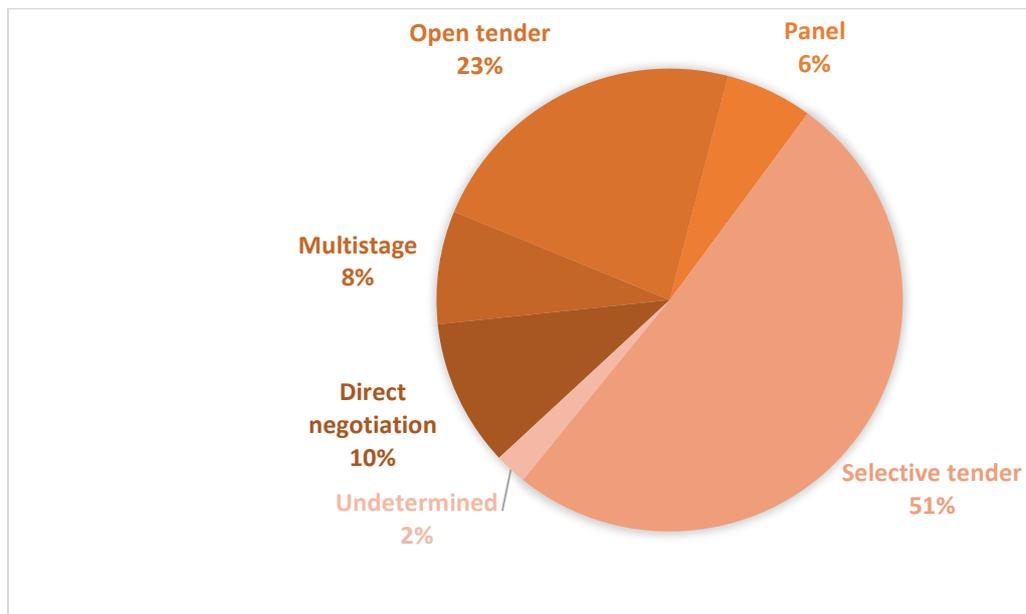
Source: SAPC consolidated database for 2015–18 for Stage 2 terms of reference (construction procurement activities above \$150k excl. GST and total procurement activities of prescribed public authorities)

Direct negotiation is far less prevalent in construction procurement (16 per cent) than for goods and services (47 per cent). The prevalence has more than doubled in the last four years, from seven per cent in 2015–16 to 16 per cent in 2018–19 (see Figure 3.10). For Stage 1 of the inquiry, it was possible to find the reason for the use of negotiation. For construction procurement and for prescribed public authorities, this information is not recorded centrally.

Selective tendering is the most common market approach chosen (53 per cent). It has increased by almost half in the last four years. The Commission however noted, when looking at random tender evaluations, that 'selective tender' is sometimes incorrectly entered in the agency's central database, when the actual market approach conducted has been a 'multistage process' or a selective tender from a 'panel' arrangement.

The percentage of contracts for which no market approach has been specified has also decreased by two-thirds over time.

Figure 3.11: Sum of contract value per market approach in 2017-18



Source: SAPC consolidated database from agencies 2015-18 databases of procurement activities

By value (Figure 3.11), selective tendering is still the predominant method (51 per cent), with open tenders being the second market approach chosen, accounting for 23 per cent of the contract value awarded, while direct negotiation and undetermined market approaches account for 12 per cent of the value of contracts executed.

So, on face value, all potential suppliers currently have access to a minimum of 13 per cent of tenders (sum of open tenders and multistage tenders) which represent 31 per cent of the total value of tenders for 2017–18.

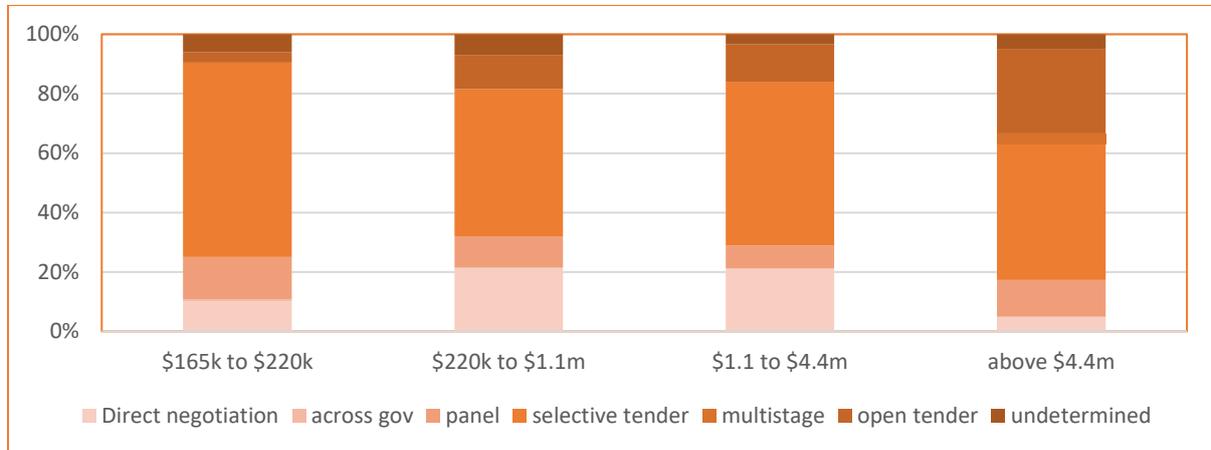
From Figure 3.12, looking in more detail at how those figures change as the value of the contracts increase:

- The percentage of contracts being tendered through an open tender more than doubles, going from 4% for contracts valued under \$220 000, to 12–13% for contracts valued between \$220 000 and \$4 million, to 28% for contracts valued above \$4 million.
- Multistage processes are introduced for contracts above \$4 million (usually an expression of interest followed by a selective tender to the two to four preferred suppliers). This trend allows a competitive process at the start (an even playing field), while having the potential to reduce the cost to tenderers by filtering non-suitable tenderers early.
- The use of direct negotiation decreases (direct negotiation is mostly used for contracts valued under \$4 million).

This evidence suggests the lower the value of the project, the less open/accessible the tender process is, which exacerbates the issue of access to tenders for SMEs who are likely to bid for those lower-value projects. In response to the Commission’s Stage 1 inquiry

recommendations, the government has committed to ensuring at least one local business has the opportunity to submit a tender for procurements between \$220 000 and \$550 000.

Figure 3.12: Use of market approach per value of contract (2017-18 data, incl. of GST)

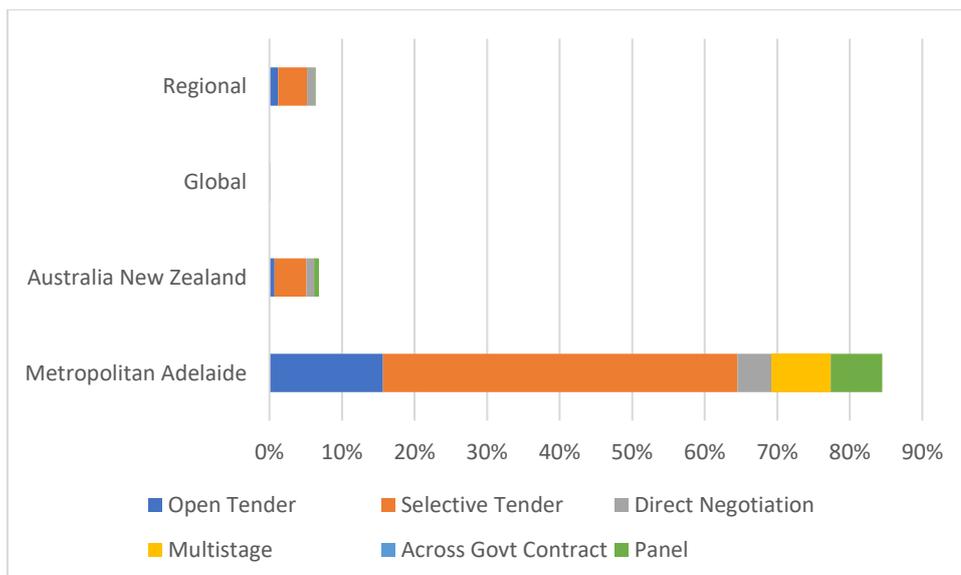


Source: SAPC consolidated database from agencies' 2015-18 databases of procurement activities

It should be noted that it is likely that the use of multistage approaches and panels are under-reported (as observed in a sample of 106 tender evaluations considered by the Commission).

Looking at the share of the value of government construction spend by market approach and supplier location (see Figure 3.13), local suppliers seem to have a much greater share in construction than they do for goods and services (90 per cent versus 73 per cent). This data is surprising and will be followed up with agencies.

Figure 3.13: Share of the value of government work per market approach and supplier location in 2017-18



Source: SAPC consolidated database from agencies 2015-18 databases of procurement activities

3.2.6 Streamlining the procurement process

3.2.6.1 Introduction

Since 1995, government construction procurement has been managed under the *Construction Procurement Policy: Project Implementation Process*, which is the five-step Infrastructure Planning and Delivery Framework, and Treasurer's Instruction No. 17.

The Project Implementation Process applies to all types of prescribed construction projects. The process provides detailed procedures which guide lead agencies through the process of procurement of infrastructure and buildings. It also defines the role of DPTI in the delivery of prescribed construction projects.

For construction projects up to \$1.1 million in value (exclusive of GST), DPTI may accredit agencies in accordance with the Agency Self-Management Approval Assessment Framework for Delivery of Lower Risk Construction Projects (the Accreditation Assessment Framework). It is unclear to the Commission why \$1.1 million was chosen as the threshold: it has not been reviewed recently and appears to be inefficiently low where a public authority has the requisite capability and judgement to undertake its procurement.

Detailed accreditation assessment criteria are provided in the Accreditation Assessment Framework. Approval is primarily given on a project-by-project basis.

Process steps for construction procurement

The lead agency determines the need for an infrastructure project to support existing or additional services and:

- defines the service required;
- identifies strategies to meet service delivery needs;
- decides whether there is a need to upgrade, replace or procure assets;
- sets the quality standards, budget, program and risk management regime required to achieve objectives; and
- decides on the preferred funding and procurement model.

The Lead Agency is responsible for ensuring that the proposed construction project has a business case with demonstrable benefits under the requirements of *Treasurer's Instruction 17: Evaluation of and Approvals to Proceed with Public Sector Initiatives*. At this point, the project is included on an approved government program (with funding) and proceeds to the Project Implementation Process, which is step 5 under the Infrastructure Planning and Delivery Framework, developed and issued by DPTI.

The steps of the Project Implementation Process were set out earlier in this draft report.

3.2.6.2 Agencies' role in the construction process

DPTI

Construction procurement is undertaken by DPTI and by some prescribed authorities. The description of construction procurement here is based on the DPTI process. Prescribed

authorities have indicated that they conform, where appropriate, to relevant government circulars, Treasurer’s Instructions and SPB policies.

Delivering infrastructure construction projects includes planning, procurement, project and facility management, and governance. The procurement phase of construction follows a similar sequence of phases to goods and services procurement, being acquisition planning (including market analysis and pre-market engagement), the market approach, and supplier selection and contract management. Unlike goods and services procurement, there is a phase for management of or transfer of assets.

DPTI divides construction procurement into the distinct streams of building infrastructure and civil infrastructure; facilities management supports both streams.

Building infrastructure

DPTI formalises the roles and responsibilities for the project with Lead Agencies through a service level agreement. DPTI charges Lead Agencies fees set on a pre-agreed sliding scale for the delivery of services of a multi-disciplinary project team. The approved agreement sets out the roles and responsibilities of all parties on a particular procurement. Each agreement is tailored to the project.

The procurement process comprising the acquisition plan (which formalises the various roles and responsibilities for each construction procurement project), market approach, evaluation and supplier selection is undertaken by DPTI. Following selection of the supplier, the project is formally handed from DPTI procurement to the Building Projects division within DPTI, who then contract manage the process.

Civil infrastructure

The framework for procurement process for civil infrastructure has been developed by DPTI and is known as the Project Management Framework (PMF). The Commission has not been provided with further information on this framework but intends to follow up the issue during the consultation phase on the draft report.

For civil construction projects, DPTI is its own client, with the projects managed by the Major Projects division of DPTI. This division works closely with other areas of the department – planning, finance, technical services, asset management, traffic operations, public transport and the Portfolio Management Office (PMO)⁷² – to ensure all approved initiatives align with DPTI’s strategic objectives and optimise benefits.

For projects considered of high value/high risk, the gateway review process is applied (managed by the PMO). Other categories of projects can also adopt the gateway review process in accordance with indicative level of risk, complexity, criticality and delivery.

The gateway review complements internal processes such as the project management framework, business planning, risk management, procurement and acquisition, and contract

⁷² The PMO is an enterprise office that supports and advises DPTI’s executive leaders to make decisions on significant initiatives, and seeks to provide DPTI with consistent and repeatable portfolio, program and project management capabilities that will lower the department’s overall risk profile, increase the overall value realised and decrease the time it takes for capital investment and business (corporate) improvement programs/projects to deliver planned value. The PMO is comprised of DPTI executives and key operational staff.

management. It is a short review of a project prior to key decisions in the project's life cycle. Reviews are undertaken to identify opportunities to improve program or project delivery to ensure the best possible outcome.

Gateway review Process

The gateway review process occurs at six points throughout the course of a program or project's life cycle. Gateway reviews provide the Senior Responsible Officer (SRO) with a view on the current progress of the project and assurance that it can proceed successfully to the next stage.

The gateway review report gives the project a delivery confidence rating and makes recommendations that help provide the project the best chance of success. The gateways are:

- Gate 0 – Initialisation Phase: direction and planned outcomes of the initiative against the wider departmental or whole of government goals or needs.
- Gate 1 – Proving Phase: reviews the preliminary business case, ensuring the project is justified prior to funding.
- Gate 2 – Pre-Delivery Phase: investigates a project's viability and proposed approach prior to approaching the market or developing a final business case for approvals.
- Gate 3 – Procurement Phase: confirms suitability of recommended decision prior to contract award; includes tender documentation, project resourcing, the risk register and the works program.
- Gate 4 – Delivery Phase: ensures suppliers' readiness to commence work and confirms ownership of the project is clearly identified after handover; includes benefits realisation plan, operation and maintenance manuals and budget.
- Gate 5 – Realisation Phase: confirms that benefits set out in the business case are being achieved and that the operational service (or facility) is running as intended. This phase typically occurs 12 months after project handover.

Facilities management: building and civil

The Across Government Facilities Management Arrangements (AGFMA) covers maintenance, management and improvement of government building assets that underpin essential community services. The government entered into a new AGFMA under which full services commenced on 1 July 2015 with the potential to extend to 30 June 2024.

Facilities management (FM) services arrangements include the provision of planned and unplanned maintenance, minor works, small construction works and property services in greater metropolitan Adelaide and regional South Australia. The FM service providers are Spotless Facility Services Pty Ltd and Department of Planning, Transport and Infrastructure – Facilities Services). The FM service providers procure small construction works, minor works and replacement/refurbishment maintenance projects according to the relevant policy and procedures manual established under the contract.

Mandated services must be done under the FM services arrangements for the applicable region. Mandated services are categorised as either planned or unplanned services. Planned mandated services generally comprise services that fall under the following categories:

- preventative maintenance;
- replacement/refurbishment maintenance of value \$5000 (exclusive of GST) or more but less than \$1 million (exclusive of GST); and
- minor works of value \$5000 (exclusive of GST) or more but less than \$150 000 (exclusive of GST).

Unplanned mandated services comprise services under the following categories:

- breakdown maintenance, which includes scheduled attendance breakdown maintenance, of value up to \$20 000 (exclusive of GST); and property services;
- replacement/refurbishment maintenance of value less than \$5000 (exclusive of GST); and
- minor works of value less than \$5000 (exclusive of GST).

Non-mandated services may be carried out under the FM services arrangements by the relevant FM service provider at agencies' discretion. Non-mandated services are categorised as either planned or unplanned services. Unplanned non-mandated services include handyperson maintenance. Planned non-mandated services include:

- small construction works of value \$150 000 (exclusive of GST) or more but less than \$1 million (exclusive of GST). Small construction works may be procured either through the FM services arrangements or through DPTI Project Delivery.
- property services. Agencies are able to add any of the property services to the scope of their FM services over the term of the arrangements.

Responsibility for the procurement process in the FM arrangements is divided between agencies and the service providers (Spotless and DPTI Facilities Services). The process is almost identical to goods and services contracts up to the value of \$33 000, with the difference to the FM process being the thresholds used – \$20 000 and above.

For preventative maintenance and minor works where the value of the contract is estimated as \$20 000 (excl. GST) or with a minimum value of \$5000 (excl. GST), if directed by the agency representative to undertake a competitive quote process, the FM service provider must:

- obtain three quotes with the agency able to nominate subcontractors from whom to request quotes;
- provide the quotes to the agency along with a recommendation for the quote offering the best value for money;
- on approval of the recommended quote by the agency, engage and manage the recommended subcontractor such that works are delivered in line with the quote.

For planned replacement and refurbishment maintenance, breakdown maintenance and planned minor works exceeding \$20 000 in value, a competitive tender process is to be undertaken. The FM service provider must:

- compile the tender documentation, including a detailed specification, approved by the agency representative, of the work to be performed;
- call tenders from a minimum of three subcontractors;
- examine and analyse all tenders received and invite an agency representative to participate in the analysis should they desire;
- recommend to the agency the tender that should be accepted; and
- on approval of the recommended tender by the agency, engage and manage the recommended subcontractor so that work is delivered in line with the accepted bid.

3.2.6.3 Roles in the construction project implementation process

The Lead Agency is primarily responsible for the initial planning, budgeting and approval elements of the building construction project and ultimately accountable for the management and operation of the asset that results. The Lead Agency is the building project sponsor or 'owner' and ensures there is appropriate governance and that the building project meets the requirements of government and agency strategic asset management plans. It is responsible for the provision of government services and consequently defines the extent, quality and location of services.

Department of Treasury and Finance

DTF advises on the budgetary and financial aspects of proposals, including project financial evaluation and business case preparation as outlined in *Treasurer's Instruction 17: Evaluation of and Approvals to Proceed with Public Sector Initiatives*. In accordance with this instruction, all initiatives which need Cabinet approval to proceed must have written advice from DTF on the financial and budgetary aspects of the initiative.

ODASA

The Office for Design and Architecture SA (ODASA) is part of DPTI and is led by the South Australian Government Architect. Its role is to provide leadership and strategic advice on design, architecture and urban design to the government through support for major projects, design review programs and the publication of design guidelines. ODASA applies the broad principles of integrated design to enable, connect and add value through design with a strategic focus. DPTI advises that, where applicable, prior to lodging a submission to the Parliamentary Public Works Committee, they will refer the project brief for review by ODASA.

Public works

The *Parliamentary Committees Act 1991* (the Act) requires that any public work with an estimated value over \$4 million (GST exclusive) must be referred to the Parliamentary Public Works Committee (PWC).

Mandatory referrals to the PWC are undertaken in accordance with the Act, and Department of Premier and Cabinet (DPC) Circular 015: *Procedures for Submissions to Cabinet Seeking the Review of Public Works by the Public Works Committee*. Submissions to the PWC are prepared in accordance with these requirements, which includes seeking acquittals from the following agencies:

- the Department of Treasury and Finance (on economic and financial issues);
- the Crown Solicitor (on legal process);
- the Department for Environment and Water (on environmental sustainability issues).

Submissions between \$4 million (GST exclusive) and \$15 million (GST exclusive) require approval from the relevant minister, prior to referral to the PWC. For submissions over \$15 million (GST exclusive), a minister's intention to refer a proposal to the PWC must first be noted by Cabinet, prior to the referral.

DPTI advise that they have more than 20 active reports with the PWC on which they report quarterly, with further submissions planned to be submitted in the remainder of 2019.

3.2.6.4 Stakeholder feedback

Business stakeholders mentioned reduced costs of tendering to suppliers through better use of prequalification information and the introduction of limits on the length of responses. That said, those stakeholders consider the cost of tendering is an issue for construction procurement processes, particularly for the design aspect of the process.

Stakeholders are concerned project briefs tend to lack relevant detail and can omit significant information. This can significantly increase the risk to the lead consultant preparing the tender. In addition, a lack of resolution regarding the construction procurement methodology at the time of the tender request increases uncertainty.

The AIIA consider a regular review of tender documents should occur to ensure that requested information is pertinent and a level of detail would ensure improvements to the tender system are maintained. Consultancy tender requirements for small projects remain disproportionately onerous as compared to the potential fees for the project.

Some tenders also require submission of information that has already been captured in the prequalification process or which contradicts prequalification requirements, whilst other examples cited included multiple requests for resourcing and financial information, adding significant time to the preparation of the tender without adding useful information, and sometimes not commensurate with the size of the tender.

The introduction of requests for 'early design concepts' within stage two of the tender process in recent tenders also raised some concerns. The AIIA cited a recent example with the Department of Education Capital Works program where the preparation of early design concepts introduced a significant additional cost to the tender process. The real cost of preparing these concepts is in the order of \$100 000, while the compensation offered was about 1/10th of that amount.

The AMCA submission highlighted the following issues:

- the quality of the detail provided on the specification and scope of work is not adequate;
- the contractual obligations and adherence to those obligations are not monitored; and
- the enforcement of reasonable timing to assess tender and contract documents is not monitored and in most cases not adequate to properly consider documentation as part of project scope, project delivery and management of risk assessments.

The AMCA also observed the level of design and the quantity of detail provided at the time of tender to subcontractors has reduced over time.

3.2.6.5 Findings

The Commission has focused on three issues:

- the efficiency of the process;
- the relationship between DPTI and lead agencies for projects; and
- the scope of activities undertaken by agencies and DPTI, including policy thresholds.

Efficiency of the process

Using similar methodology from the Stage 1 inquiry on goods and services, the Commission has attempted to replicate the SPB database for construction procurement. There is no equivalent system-wide methodology for the standardisation, collection and reporting of activity for construction procurement. The Commission has analysed information and tender documents of DPTI, Renewal SA, the SA Housing Authority and SA Water on construction projects greater than \$150 000 (excluding GST).

Timeliness

After analysing and attempting to describe the typical time taken for construction procurement processes, the Commission found that these types of projects vary greatly in scope, levels of competition, evaluation and engagement with the market on design or aspects of the contract.

The time taken for early planning phases of an initiative (problem identification, initiative identification, options development and business case development) is not typically recorded and reported on by the agencies in the Commission's data.

The indicators and benchmarks in construction procurement processes are not commonly done among Australian jurisdictions. A Transport and Infrastructure Council benchmarking report in 2015⁷³ analysed procurement processes from the perspective of timeliness and quantitative and qualitative performance measures (the latter based on industry consultation). The benchmarking analyses the following phases of the procurement process:

- pre-procurement;

⁷³ Transport and Infrastructure Council of Australia, *Infrastructure Benchmarking Report*, 2015.

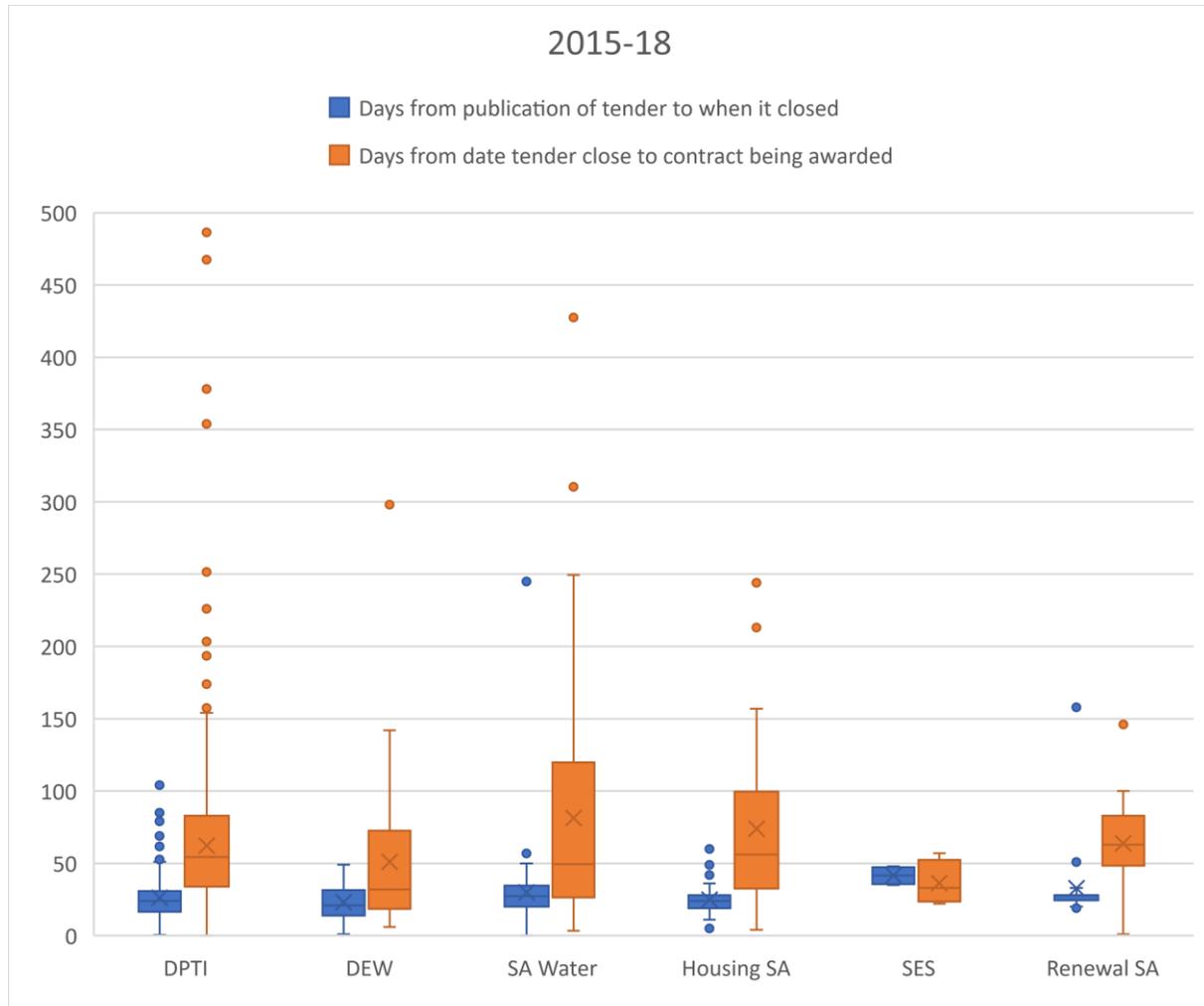
- expression of interest;
- request for proposal; and
- evaluation and contract finalisation

The Commission has attempted to replicate these measures using data generated from construction project databases held by DPTI and selected prescribed authorities.⁷⁴ The data only permit measurement of two phases: average time for projects going to market (covering both expression of interest and request for proposal phases); and time taken for evaluation.

The following timeliness measures are taken from the Transport and Infrastructure Council report. The Commission has attempted to replicate the measures for South Australia in the following table.

⁷⁴ 777 contracts out of 4910 executed between July 2015 and Dec 2018 (16%) had usable data on timeliness (49 administrative errors, where wrong dates were entered, were found out of the original 793 contracts considered (6% of the total usable contracts). When the error was obvious, it was corrected; when it wasn't obvious, the entry was deleted.

Figure 3.14: Average time (in days) provided to suppliers to tender against the time taken by agencies to award the tender, by agency (for contracts executed between 2015 and 2018)

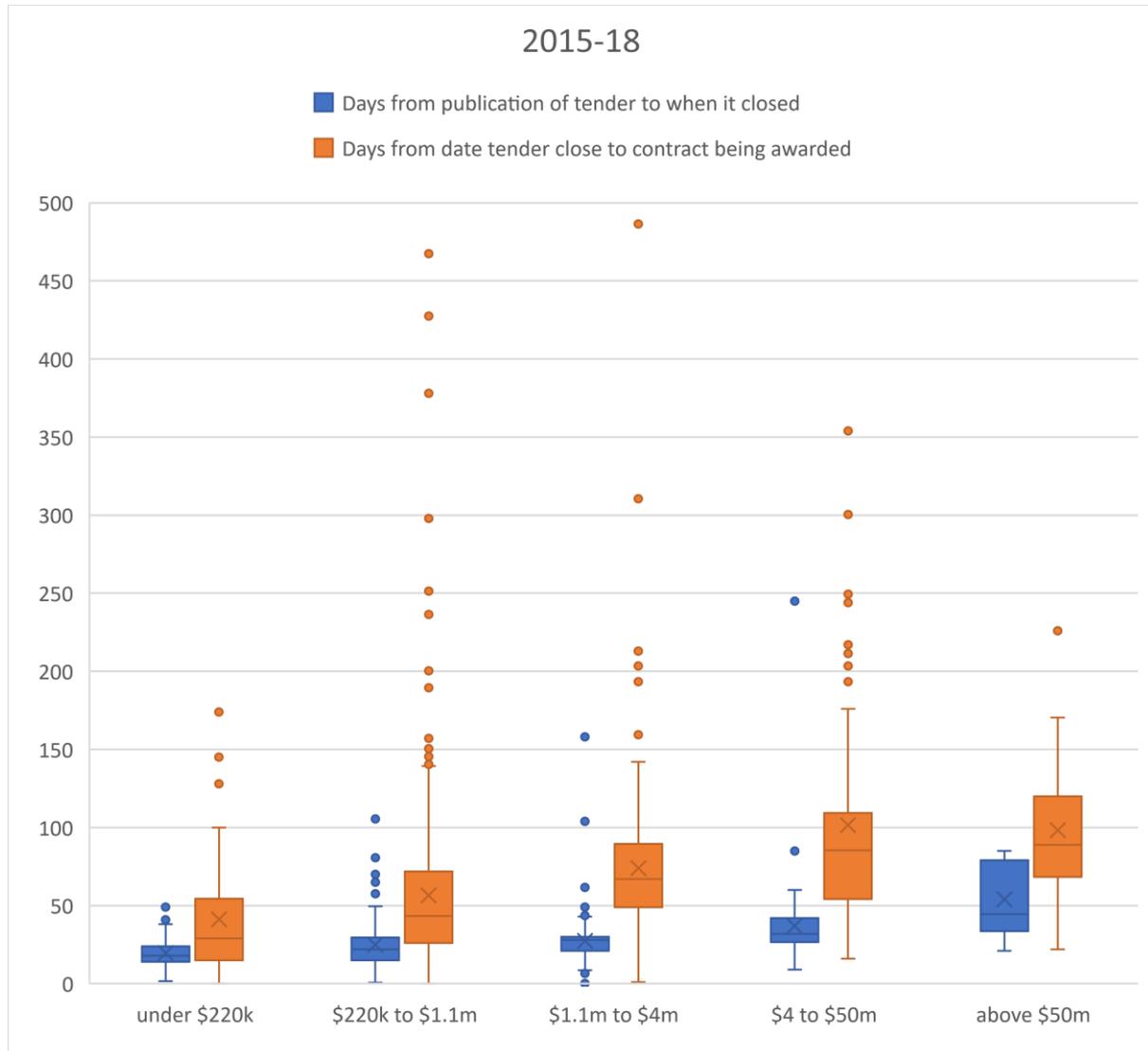


Source: SAPC consolidated database from agencies' 2015–18 databases of procurement activities

The analysis indicates that the average time taken for agencies involved in construction procurement varies significantly across the sector, reflecting the complexity of the projects, individual needs and business objectives along with the efficiency of the process. The outliers highlighted in Figure 3.14 above show that the evaluation period can be protracted.

Further, as shown below in Figure 3.15, the average time taken for evaluation of the contract increases with the value. The analysis shows the small amount of time on average that tender documents are put out to market compared with the average evaluation period. This can be disproportionate for projects approaching \$50 million in value.

Figure 3.15: Average time (in days) provided to suppliers to tender versus the time taken by agencies to award the tender, by value of contract (for contracts executed between 2015 and 2018)



Source: SAPC consolidated database from agencies' 2015–18 databases of procurement activities

Quantitative benchmarks

The National Transport and Infrastructure Council developed the following process benchmarks:

- divergences of planned procurement program from planned timeframes;
- divergences of actual procurement program from planned procurement program;
- expression of interest (EOI) response requirements for information relating to the project solution;
- divergences from the information provided to potential and actual proponents;

- planned addenda for changes or for issue of missing information during the request for proposal (RFP) phase;
- material changes to contract terms or scope during the RFP phase;
- RFP requirements for project plans that exceed the requirements to address material agency risks;
- RFP requirements for designs that represent a material risk to the agency.

The Commission considers that these measures illustrate a gap in the measurement of the efficiency and effectiveness of the tender process in South Australia.

Duplication and potential inefficiencies in the process

The analysis in this section only refers to processes of DPTI for construction procurement. The Commission has not attempted to analyse common features of the process undertaken by prescribed authorities.

The Commission reviewed the process flowcharts for both building infrastructure and civil infrastructure and observes the following.

For building infrastructure:

- Liaison with lead agencies is not explicitly identified in the planning stage of the process or in the development of tender documents.
- Financial approval is sought after tender documents go to market.
- While IPP calculations are identified as an explicit step in the process, sustainability impacts, and regional and social impacts are not identified.

For civil infrastructure:

- Approvals for business cases are not an identified part of the process flowchart (while they may occur in practice).
- References to Cabinet, ministers or the Public Works Committee for significant projects are not included.
- The individual or party that manages the project within DPTI is not identified in the flowchart.
- The IPP steps, sustainability impacts, regional and social impacts are not identified in the process.
- Scope and technical requirements are finalised after the acquisition plan is complete.

Several layers of governance are included in civil infrastructure projects, depending on the complexity, risk and dollar value. As indicated earlier in this chapter, there are gateway reviews and PMO oversight from a broader DPTI perspective. Internal stakeholder engagement, buy-in and input are used at all stages of the planning, procurement and delivery phases, which may involve collaboration across multiple divisions of DPTI.

It is not uncommon to have steering committees set up for the procurement phase as well as the delivery phase that include senior executives from the department to provide advice and guidance. There is also a Major Projects Review Panel that has responsibility for oversight of projects in the procurement phase as well as those in the delivery stage.

High-level organisational information provided by DPTI indicates significant sections and divisions of the department are involved at the various stages of the process. While the processes may be well established and within the department, the Commission found tracking outcomes, decisions and information flow within the department not easy to understand. The Commission will engage DPTI on these issues.

Lead agency–DPTI relationship

The Project Implementation Process provides a framework for how lead agencies and DPTI work together in the delivery of building and civil infrastructure and minor works. The Commission has received feedback from both DPTI and lead agencies as clients to DPTI on the outcomes of the process and areas for reform.

DPTI view

DPTI reports that the two issues that cause sub-optimal outcomes from its perspective are incomplete project briefs and changes in scope of the project during the design phase.

Incomplete project brief

If the lead agency has not been able to, for whatever reason, provide a project brief that is resolved, DPTI is, for the most part, unable to proceed to market to engage with architects to commence the project. Where timeframes are tight, this can lead to significant delays to a program. DPTI believes it is spending an increasing amount of time assisting agencies to develop fit-for-purpose project briefs.

Scope change

If in the design phase of a project the lead agency changes the scope of a project, there will be impacts on the program as well as additional costs to be charged by the design team. If the scope change occurs during the construction phase, these impacts can be even greater. Waiting for the design to be complete, prior to lead agency review, is often a cause of delay and design rework that may involve additional design fees.

Engaging local suppliers

PIRSA's experience is there are opportunities to improve the management of small projects that have short delivery timeframes or that complement a larger project. For these projects PIRSA prefers to engage directly with pre-qualified tradespersons, as the projects mainly occur in the regions. Direct engagement by PIRSA is the preferred method of regional schools as they can avoid lengthy delays while the requests are being channelled centrally through the Adelaide office. PIRSA reports that there are normally cost savings associated with dealing in this manner.

Guidance from DPTI on process

DCS considers the guidance and policy materials provided by DPTI and DPC could be improved for projects valued between \$150 000 and \$1 million (GST exclusive). More detailed procedures, guidance and processes for these projects would ensure higher compliance and better procurement outcomes. Both DHS and DE support current guidance material to cover all forms of procurement.

The guidance on roles and responsibility can be unclear when both agencies are involved in the procurement process. An agency had to seek self-management approval for a process that was essentially procuring a service. However, the nature of the service was judged a construction process by DPTI and hence required approval for accreditation. Partial approval was given for the agency to manage the contract and for DPTI to manage the procurement process. As a result, the agency now manages the procurement process, with DPTI only providing final approvals. In this example, there appears to be little value added from DPTI and timely outcomes are compromised.

Scope of activities undertaken and policy thresholds

Construction projects with a total value exceeding \$150 000 (exclusive of GST) must follow the established policy framework (the PIP). In addition, the across-government contract to maintain or add to government assets, AGFMA, compels agencies to use the arrangements for maintenance and minor works. For construction projects up to \$1.1 million in value, DPTI may accredit agencies in accordance with the Accreditation Assessment Framework.

The issues identified by agencies relate to the scope of activities that might be undertaken by the agencies themselves rather than through the process established under the PIP or through across-government contracts. Agencies argue in some cases that the capability exists or with some element of reform have the potential to exist to manage smaller capital works programs within their agency and that the project outcomes would be optimised. This is particularly relevant for specialised or service-related requirements where the agency may be better placed to manage the project.

Management of facilities contract

DHS has noted positively, on aspects of the Across Government Facilities Management contract specifically, their experience of the repair, breakdown and maintenance aspects of the contract. With respect to project management of minor works, DPTI's insistence that it contract manage these processes seems to the Commission difficult to justify.

Prior to the introduction of the AGFMA, agencies were accredited to undertake projects up to the value of \$1 million (exclusive of GST). Under the terms of the AGFMA contract, there are mandated activities that must be undertaken by the contracted service provider. For some agencies, such as DHS, these mandated activities were the core activities for which they were accredited but now are no longer able to do, as it would breach the terms of the AGFMA. In DHS's view, they question the service provider fees that have no demonstrated additional value. This impacts on price, quality and whole-of-life costs of assets. DHS's capability to deliver these types of projects seems evident as both DHW and DE approached DHS to conduct works on their behalf.

Centralisation effects on subject expertise

DHW believes that the understanding of healthcare-specific requirements within DPTI has weakened over time. In 2015, DPTI moved toward 'lump sum'/'guaranteed maximum price' as the preferred delivery model, which DHW contends reduced collaboration and flexibility and focused project outcomes on 'cost' rather than 'best value'. In recent times, DPTI has moved toward contract models based on interstate experiences (such as on civil/road projects) which are not, in the department's opinion, appropriate for the healthcare sector where collaboration, consultation, stakeholder management and flexibility is required.

DHW has provided examples where the focus on a 'single point of contact' within DPTI for DHW to liaise with and transfer project-specific knowledge has resulted in miscommunication of information and delays in the process for tender, evaluation, approval and contract award.

DEW has reported that, in other instances, delays of weeks to several months have occurred in achieving self-management for projects and procurements where DEW has clearly demonstrated experience and expertise.

3.2.6.6 Conclusions and draft recommendation

Efficiency of the process

Infrastructure Australia recently published an audit of Australia's infrastructure challenges and opportunities over the next 15 years.⁷⁵ The key messages are:

- Changing and growing demand, and a mounting maintenance backlog, mean a new wave of reform and investment is necessary to ensure quality of life and economic productivity are enhanced over the next 15 years. By 2034, Australia's population is projected to grow to 31.4 million, adding to infrastructure demand.
- Users are often not at the centre of infrastructure planning and decision making for Australia's future; however communities are increasingly demanding greater transparency and service choice.
- Constant and rapid change is creating challenges for planning, delivery and operation of infrastructure. Growing social, economic and environmental interdependencies have added both complexity and opportunity to the planning, delivery and operation of infrastructure.

With respect to procurement processes, the audit found the overall volume and scale of infrastructure construction has created a heated, stretched construction market and reduced competition for projects. (The limited competition was identified by several stakeholders in South Australia and Victoria.) High-risk projects are not achieving a desired level of competition during procurement. This may result in delivery being delayed or delivered by a higher-risk, lower-skilled contractor.

Truncated bidding timelines, unnecessary documentation requirements and under-resourced government project teams have resulted in poor procurement and delivery outcomes. This

⁷⁵ Infrastructure Australia, *An Assessment of Australia's Future Infrastructure Needs: The Australian Infrastructure Audit 2019*.

results in higher levels of risk and uncertainty being priced into tenders. These costs are ultimately carried by the users through poor quality services or additional costs, or met through government reimbursements.

Some jurisdictions have responded to the emerging infrastructure trends by developing policy frameworks to support processes and procedures in delivering on outcomes.

NSW Government 10-point commitment to the construction sector

The NSW Government's Action Plan: ten-point commitment to the construction sector released in June 2018 was developed to support the government's infrastructure objectives through improved procurement outcomes. The Action Plan adopts a broader, longer term view about the need to drive quality, innovation and cost effectiveness by

- fostering a thriving and sustainable construction sector;
- reducing industry's costs and 'down time' by making government procurement processes more efficient.

In respect of making the procurement process more efficient, the key features of the Action Plan are to:

- use early market engagement to elicit industry's views on the best choice of procurement model for each major project, and (where appropriate) for works within that project, drawing on good practice in NSW and other jurisdictions;
- move away from a reliance on fixed-price, lump-sum procurement methods, and be open to collaborative contracting models like alliancing;
- adopt expedited engagement processes like early contractor involvement (ECI) where a project's risk profile justifies it and where it saves time and resources without sacrificing value for money;
- develop in partnership with industry, and then publish, simple guidelines which document 'best practice' for each of the main procurement methods, and the circumstances in which each method is likely to be preferred;
- 'close the loop' with potential bidders once market soundings for major projects have been undertaken, including through an interactive session prior to the finalisation of tender documentation, so that bidders can test and understand the rationale for procurement decisions. Ensure that, once awarded, contracts are managed by both parties in a professional and mutually respectful fashion.
- use inception workshops to establish strong behavioural alignment and shared objectives between the parties soon after contract award.

Victoria's public construction framework

Victoria adopted a public construction framework which took effect from 1 July 2018, aimed at enabling:

- simpler and easier industry participation – this refers to greater standardisation of procurement processes across government including contracts and the supplier register;
- time and cost savings when preparing bids – the practice of agencies only seeking information once with greater use of pre-qualification and staged tenders where appropriate;
- a stronger focus on project objectives, rather than the administration of tenders, with greater alignment to evaluation criteria;
- fair, transparent and openly competitive tender processes with clearer requirements for probity and support for greater interaction with industry during tenders; and
- greater transparency of upcoming procurement opportunities and improved dialogue with industry participants.

South Australia lacks these initiatives. In South Australia, SA Water found that the streamlining processes, especially in the front end with early involvement of contractors, assist in identifying critical issues central to delivery and whole-of-life costs of procurement.

The Commission has found that the focus of DPTI on process efficiency and effectiveness benchmarks is not evident, with little or no data collection or benchmarking activity occurring. The information not collected relates to:

- outcomes from procurement planning, establishment of the business case and engagement with suppliers on the design aspect of projects;
- timeliness of the procurement process; and
- outcomes of the procurement process in terms of meeting original scope.

Given the significance of community expectations and the quantum of infrastructure requirements the state has in the future, demonstrating and executing efficient processes are important to support the delivery of capital works programs and meet demands of the community.

Draft recommendation 3.3

In order to better track performance in construction procurement, the Commission proposes that DPTI develop benchmarking for construction procurement processes to compare performance across matters such as:

- outcomes from procurement planning, establishment of the business case and engagement with suppliers on the design aspect of projects;
- timeliness of the procurement process; and
- outcomes of the procurement process in terms of meeting the original scope.

The Commission observed some gaps in the DPTI process flowcharts provided to staff for use on procurement projects and sees merit in addressing them. It will follow up with DPTI on this matter.

DPTI – Lead Agency relationship

The centralisation of the construction procurement process has resulted in expertise being concentrated in one agency. This a logical approach given the size of the state and the need to achieve a critical mass of expertise. The obverse of this design, in concert with the amount of public works that the government undertakes, could make it difficult for DPTI to administer the volume of work. The Commission has not been able to verify this as yet.

In addition, time delays, lack of understanding of agency requirements and the extent of tender documentation relative to the value of the procurement have been reported by agencies to have impacted on the effectiveness of the process. These delays for instance have materialised in delays to engage maintenance service providers in regions through a centrally administered (Adelaide-based) facilities services contract.

Agencies commended DPTI's expertise on larger projects as invaluable, while noting that capability was scarce. One possible solution is to stratify the application of the project implementation process: the expertise that DPTI have cultured and established in addition to industry ties and experience over a considerable amount of time is more suited to larger projects. In effect, the policy framework supporting construction procurement needs to better balance what DPTI can manage effectively and the delivery requirements of other agencies, particularly for smaller and specialised construction projects.

This will be considered in the Commission's final report in terms of the future scope of the procurement system and the associated roles and responsibilities that agencies will have under a future system.

Scope of activities and thresholds

Some public authorities consider the current threshold of \$150 000 (exclusive of GST) is too low to undertake infrastructure projects that it might otherwise be able to undertake. In some instances, the crowding out of agency independence and capability to perform this work by the AGFMA contract has been an unintended consequence of the arrangements.

The reforms some agencies seek relate to both maintenance and minor works up to a threshold value in excess of what departments can currently be accredited for, which is \$1.1 million. This would give agencies the necessary autonomy to manage their requirements for small-scale works without the need for an additional administrative process. Such a reform would also enable agencies to deliver directly more of their low-risk, low-cost projects, reduce delays in the process, and promote a more effective and concerted management of whole-of-life costs of assets. Agencies contend that, particularly for minor works, whole-of-life cost considerations are not as prominent as they otherwise should be in determining the scope of projects.

This reform would necessarily come with additional responsibilities for agencies such as maintaining asset registers and being responsible for future maintenance and replacement.

The Commission has not formed a view yet of what an appropriate threshold may be and will undertake further consultation with public authorities on the notion of higher thresholds and greater scope to undertake activities. Consultation would also include looking at the impacts of such a reform on the flow of service fees between departments and fees external to the government sector.

In addition, the Commission will investigate further the arrangements of the AGFMA to determine the feasibility of redrawing the contract to enable agencies greater autonomy to conduct construction procurement processes.

3.3 End piece

The following is an extract from the 2018 South Australian Auditor-General's report:

DPTI closed the procurement modernisation project in February 2018, having completed most of its intended changes. Responsibility for the remaining items was transferred to DPTI's Procurement and Contract Management Directorate.

DPTI has now implemented:

- *a single executive accountable for all procurement and contract management activity across DPTI*
- *a new procurement and contracting structure*
- *a defined category management framework*
- *strategies for actively engaging with industry and suppliers*
- *spend analytics, opportunity assessment and analysis for potential savings, and active monitoring of savings and benefits*
- *a centralised structure for procurement and contract management*
- *a training and development program, capability framework and feedback opportunities.*

The following actions were incomplete:

- *developing a suite of effective procurement policies (see below)*
- *implementing IT systems for procurement processes, supplier relationship management and contract lifecycle management*
- *establishing an online catalogue and work flow process for goods and services procurement.*

Now that DPTI has largely reformed its procurement and contract management processes, it must also update its large volume of documented policies and procedures. As at July 2018, of DPTI's:

- *six policies, one needs review and three were pending approval*

- *95 procedures, 66 need review and 20 were either under review or pending approval*
- *242 templates, 228 need review and nine were either under review or pending approval.*

DPTI advised us that it expects to complete its review of policies and procedures by 30 June 2019.

The comments in the Auditor-General's report are generally consistent with the Commission's review of DPTI procurement processes to date. Two findings are particularly relevant.

The first is that DPTI has clearly made a number of improvements to its procurement function, including a restructure that delineated more sharply the building and civil engineering streams of procurement. This was evident in the Commission's meeting with DPTI personnel and comments from public authorities and external stakeholders.

The second is that DPTI has work to do in modernising its information systems, including the information recorded and, importantly, documenting its procurement processes. The Commission observes that the thresholds that govern the use of DPTI's various processes appear very low. Some have clearly not been adjusted from some time, which increases red tape and limits discretion in projects that in earlier times would have been subject to less strict process requirements.

For example, since 1995, government construction procurement over \$150 000 has been managed under a policy umbrella approved by the Government of South Australia – *Construction Procurement Policy: Project Implementation Process*, the 5-Step Infrastructure Planning and Delivery Framework and Treasurer's Instruction No. 17. Effectively, this requires public authorities to work with DPTI on all major and minor construction projects unless they are accredited by DPTI to manage the individual projects on their own.

The Commission agrees with the logic of utilising the (scarce) expertise of DPTI for construction, especially for larger/more complex projects. That said, the Commission sees merit in appropriately qualified and capable public authorities managing minor projects on their own. This has the benefit of closer interaction between the client business unit and the procurement process under the overall accountability of a single chief executive who is accountable for both the outcome and quality of the procurement activity.

There are two further benefits to this option. Importantly it would free up resources in DPTI to focus more effort on larger and more complex projects. External stakeholders and public authorities have expressed a concern that DPTI's resources are stretched thin. This has also been confirmed by DPTI.

The state has projected a significant increase in infrastructure spending over the forward estimates and other infrastructure groups have indicated that it will be necessary to maintain a higher level of infrastructure spending to meet growing population requirements. The Commission considers it would be prudent to consider options that ensure DPTI's existing scarce expertise is used in the most effective manner and its critical mass is strengthened, especially given South Australia's size compared to the major states.

The Commission will explore with DPTI and other public authorities a potential adjustment to this threshold between the release of its draft report and the submission of its final report. Other thresholds also appear low and old have been discussed in the preceding sections of this chapter. The Commission intends to investigate updating the policies or thresholds as part of the final report.

The *Construction Procurement Policy: Project Implementation Process* is intended to govern all construction projects over \$150 000 (excluding GST). DPTI has told the Commission that it uses a slightly different process to manage civil engineering projects. The Commission has not yet seen documentation of the alternative process. The Commission intends to look at this in more detail before finalising its recommendations.

The Commission observes that organisations make choices about the balance between formal documentation and the use of custom, practice and culture to ensure sound process and good outcomes. Less weight on formality increases the reliance on expertise and experience largely embodied in staff: an important corollary is that such organisations are more fragile and their performance in areas that rely on this embodied expertise is more vulnerable to the loss of key staff. This circumstance is exacerbated where there is insufficient ongoing investment in capability and succession.

Another issue is the apparent use of different complex formulas in the tender process. In its review of tender documents, the Commission observed that DPTI uses a number of different formulas to score tenders. It is not always clear why the particular formula is chosen, but it is clear that the choice of formula has a material impact on the final evaluation.

For example, the Commission rescored a civil engineering project using one of the formulas used for the building side of the department. In this case, a different supplier would have obtained a higher score for this particular tender. The Commission acknowledges that buildings and civil engineering projects are quite different but, as stated earlier, the rationale for choosing the formula in the documents that the Commission reviewed to date is unclear.

The Commission is not aware of any impacts of these apparently inconsistent approaches and will follow up with DPTI.

As is evident from the above comments, the Commission has not progressed its understanding sufficiently to form definitive conclusions at this stage. The following is a summary of items the Commission intends to follow up with DPTI before finalising its report:

- DPTI's strategic approach to value in procurement;
- the strategic use of different formulae in tender evaluation;
- the application of risk management principles in practice;
- how subcontractor feedback is/will be addressed;
- the development and use of contract management plans;
- how lessons learned feedback is incorporated in future procurements;
- the strategic use of different formulae in tender evaluation;
- the difference between the civil infrastructure and building management processes;

- procurement process documentation; and
- DPTI's view of appropriate procurement metrics.

Nonetheless, it is evident from consultation that there are options to improve the effectiveness of DPTI's own procurement and the services that it provides to other agencies.

4. Other procurement issues

This chapter considers three issues that are common to procurement for both prescribed public authorities and construction and were subject to the same consultation process as the preceding two chapters.

4.1 Metrics, reporting and performance

A recurring theme throughout the inquiry has been the lack of data and information to provide evidence on trends in the procurement system, to support monitoring of performance and to identify areas for improvement. The Commission has heard this point from both stakeholders and public authorities.

The whole-of-government reporting of outcomes and collection of information by agencies is inadequate. This situation reflects the limitations on information that is collected, limitations of IT systems, as well as the low levels of accountability in procurement spending (for both goods and services and construction procurement).

The Commission notes that information and data collection capability vary widely across public authorities. Some public authorities, such as SA Health, have developed relatively sophisticated ICT arrangements for central procurement management, while others have minimal ICT capability for managing the procurement process. This partly reflects the absence of an across-government ICT digital strategy for procurement. As a result, public authority ICT capabilities and resources may or may not incorporate functionality that is suitable for the procurement processes.

4.1.1 Agency information

The Commission requested public authorities to provide a summary of the measurement regimes and reporting arrangements used for construction procurement processes. The information request related to measuring the different phases of the procurement process, value for money, contract outcomes and other broader outcomes such as IPP. Other than at the individual project level, public authorities did not provide examples of reporting on outcomes used either internally or externally for the purposes of demonstrating outcomes or activity from the procurement process.

In terms of systems to support collection and reporting of information, there are varying levels of capability across the public sector with considerable amounts of recent reform and activity. The Department of Health and Wellbeing utilises the Procurement and Contract Management System for category management and financial workflows of procurement projects. The Departments of Energy and Mines (DEM), Innovation and Skills (DIS), Child Protection (DCP) and Education (DE) have recently implemented reporting to support governance, business controls and improvement, enabling:

- analysis across contracts;
- analysis and management of financials by service type, contract, key performance indicator (KPI) or service provider;
- forecasting of payments and future financial commitments;

- monitoring spend against contracts, which can be viewed at a panel, contract or work order level; and
- exportable contract, contract manager and service provider information.

As DPTI is a central agency in the construction procurement process, it was asked to provide a copy of the information held in its database on projects undertaken by the government for both building and civil infrastructure. This information covers building infrastructure projects across the sector.

In examining the database, the Commission found that limited information regarding the procurement process or outcomes of categories of projects is collected or reported. For example, DPTI have advised that they do not typically record and report on the time taken for steps in the early planning phases of an initiative (problem identification, initiative identification, options development and business case development).

All public authorities that undertake construction procurement have indicated that they disclose contracts, in accordance with PC027, on the SA Tenders website. Public authorities advised that, in all but a very small number of cases, contracts that should have been disclosed were disclosed.

DPTI, DEW and SAPOL publish their forward work plans for construction procurement. DPTI publishes its workplan on a rolling four-year basis, while DEW and SAPOL publish their forward workplan for construction projects as part of the workplan submitted to the SPB (on a rolling three-year basis).

4.1.2 Findings

In Stage 1 of the procurement inquiry, the Commission found that reporting of goods and services procurement activity and performance in South Australia was of considerably less quality and description than that published in other jurisdictions. The South Australian Government accepted the Commission’s recommendation to develop a reporting regime for improved procurement metrics for goods and services for completion by February 2020.

This section brings together the issue for all government procurement.

4.1.2.1 Procurement activity measures

The Commission’s analysis of reporting methods and outputs across the sector has focused on both what is generated internally by public authorities and what is reported for public consumption. The Commission sought examples of reporting for goods and services procurement and construction procurement across four categories:

- procurement process;
- capability;
- continuous improvement; and
- outcomes.

Public authorities generate reports on goods and services procurement in:

- total purchasing expenditure across the sector;

- median time taken for a procurement process (above contract value of \$220 000);
- location of supplier;
- type of engagement with the market (sector-wide data);
- contracting activity by department;
- number of acquisition plans examined by the SPB;
- supplier complaints against public authorities; and
- disclosure of contracts on the SA Tenders website.

These reports relate to the key objectives of the procurement framework established by the *State Procurement Act 2004*: fairness and transparency, ethical dealing and value for money. Fairness and ethical dealing are reported on to some extent through timeliness and supplier complaints; sector-wide data on expenditure and contracting activity provide some description of the scope of activities. Almost all of the reporting that occurs is done at whole-of-government level (apart from contracting activity). This does not allow for or encourage agencies to account for their contribution to overall results. The gaps in the reporting regime as they relate to the procurement framework are:

- value for money: information on value for money is not included, demonstrating lack on information on financial and non-financial outcomes or holistic reporting of contract management;
- capability of staff to undertake their roles and responsibilities;
- compliance with SPB guidelines; and
- efficiency and effectiveness of organisations in supporting procurement functions including supplier engagement and tools and guidance for procurement staff.

The analysis of the current reporting regime covers both goods and services and construction procurement. While the SPB framework elicits some level of public reporting on goods and services, no such public reporting occurs for construction procurement apart from the public disclosure of contracts. The absence of across-sector reporting on construction procurement, covering the activities of public and prescribed authorities, is probably linked to the exemption of construction procurement activity under the SP Act.

Construction procurement projects' description, budget and timelines are reported through budget and financial reporting processes of public authorities; however, they relate to the finances of the project, not the effectiveness of the procurement process or the related outcomes.

Examples in other jurisdictions sighted by the Commission include dashboards of information which can be interrogated and cross-tabulated for expenditure and contracting activities across government. New South Wales collects for internal purposes information on:

- supplier (supplier groupings – sectors or categories used by government);
- categories of purchasing;

- locality of supplier; and
- business type or size.

Western Australia publishes annual expenditure by region, department and by commodity and services along with annual contracting activity data by department.

The Queensland Government has initiated a reform for agencies to develop a procurement plan (or strategy) on an annual basis. The plan includes areas of expected expenditure by category and by key projects as well as key corporate metrics for the agency including capability development. The plan is updated quarterly to allow for recent project planning or emerging requirements and is intended to reflect current priorities to better inform the supplier market. The planning process is linked to budget planning and represents the agency's current intent for its procurement activities.

4.1.2.2 Capability measures

The Commission has engaged extensively with SA Water on their capability development framework as it seems to be a good model for ensuring a high-performance organisation in purchasing goods and services. The SA Water Capability Development Program is designed for use by all business units in the organisation with a focus on ease of use and engagement with a high degree of structure and coordination. The key features of the capability development program at SA Water pertinent to metrics and reporting are:

- gap analysis of procurement teams and business units where procurement is a key strategic activity;
- prioritising and planning the key needs for development intervention; and
- tracking and reviewing impacts of intervention.

In terms of metrics to indicate how the capability program is progressing, SA Water:

- assesses procurement capability at points in time for key competencies;
- reviews performance and contribution to key departmental objectives; and
- identifies and tracks the amount of training provided or qualifications undertaken and key competencies addressed by each.

4.1.2.3 Continuous improvement

SA Water has developed a continuous improvement process that reviews their internal quality management system at regular intervals. A documented and comprehensive internal quality audit of the business operations is conducted according to an established program. These reviews are aimed at verifying that the quality activities proceed according to plan and to determine the effectiveness of business units.

The governance arrangements ensure that the assurance reviews are to be carefully considered by the Procurement Leadership Group of SA Water and documented as part of the review process. Relevant data and statistical information are collected on the relevant processes and services to demonstrate the suitability and effectiveness of the business unit.

This data is used to evaluate where continual improvements of the effectiveness of the business unit can be made.

The Victorian Government has continuous improvement metrics as part of its complexity and capability framework. The framework requires:

- monitoring and management of procurement performance;
- external benchmarking and gap analysis; and
- compliance monitoring and reporting on procurement governance for:
 - roles and responsibilities;
 - delegations;
 - risk management;
 - probity; and
 - compliance with procurement strategies.

The VGPB annual reports include for each mandated organisation the capability scorecard at a universal level, accounting for all factors including continuous improvement, rather than publishing scores against each metric.

4.1.2.4 Outcome measures

The Commission has analysed the use of data to describe financial outcomes and non-financial outcomes across the public sector.

In terms of financial outcomes, SA Water has developed a benefit recording process and database as part of its category management framework. The financial benefits, from both sourcing and contract management processes, are captured, monitored and reported by SA Water's Procurement Team. This process includes forecasting and tracking benefits that have been defined within Category Management Plans to deliver benefit to customers.

In terms of non-financial outcomes, the Industry Participation Policy is the most embedded government objective in the procurement process. Since 2015–16, the Office of the Industry Advocate has been collecting information on construction procurement expenditure and all expenditure from prescribed public authorities. The information includes the type of industry participation plan that applies, the economic contribution test being scored (metropolitan, regional or tailored), the score of the winning supplier and the total estimated value of the contract. The information is used by the Industry Advocate to track compliance with the objectives of the Industry Participation Policy and as a basis for engaging with businesses on procurement opportunities in government.

The South Australian Government has stated policy goals and objectives for economic growth in a sustainable and socially responsible way. The relationship of procurement to these objectives is contained to varying degrees in SPB guidelines and policies. The requirement to undertake sustainability impact assessment is mandated for all contracts above \$4 million (exclusive of GST). While there are considerations and requirements for broader government objectives, there are no measures to quantify the contribution of

procurement to these objectives. As such, there are no whole-of-government procurement-related objectives for innovation, environmental impacts and social impacts.

4.1.3 Working conclusions and draft recommendations

4.1.3.1 Reporting

The greatest source of value, and indeed the main purpose of the reporting, is the strategic use of information for improving business performance and demonstrating accountability of public authorities. A striking aspect of the analysis to date has been the low use of reporting to demonstrate accountability of outcomes. This implies a low level of strategic importance attached to the procurement function.

The Commission notes that there are processes and projects currently occurring that will improve the quality and availability of data and the capacity of the system to collect and report on procurement (e.g. reform to the SA Tenders website, introduction of a single business identified and agency rollout of contract management and workflow systems).

While these processes are acknowledged, the Commission emphasises the need for coordination and central strategic oversight of these reforms and similar processes in the future. This will be important to:

- ensure as much uniformity as possible in the administrative data supporting the reports;
- ensure consistency in the methodology for collating and analysing the data;
- develop standards of reporting and benchmarks for agencies and whole of government to publish performance; and
- promote development of information and performance benchmarking at agency level to meet, where relevant, agency needs.

Two key messages for the case for change are, first, reporting on a procurement framework must account for all procurement activity undertaken by the public sector and currently this is not the case. Second, that the information is used to support better outcomes: more capable organisations; more efficient procurement processes; better engagement by suppliers and improved outcomes for business of supplying to government; and a more strategic approach to the basket of goods purchased by agencies to drive better value for money.

Draft recommendation 4.1

In order to strengthen the South Australian Government's capacity to understand, analyse and improve whole-of-government procurement in line with its support for Recommendation 2.7 of the Commission's final report into Stage 1, the Commission proposes that the reform of the reporting requirements and the related short-term actions previously approved in relation to goods and services be extended to cover construction procurement.

4.1.3.2 Measurement

In order to undertake the reporting described in the previous section, information will need to be collected in a form that can be retrieved and analysed by public authorities. The conclusions here outline the metrics required of a procurement system to demonstrate the efficiency and effectiveness of and accountability for expenditure of public monies in purchasing goods and services. The Commission outlines below the elements of the measurement framework required to demonstrate that these outcomes have been met and the elements of this framework that South Australia does and does not currently have.

The measurement framework is based in part on best practice examples found by the Commission and in part on the findings of the inquiry to date. The framework is for application to both goods services as well as construction procurement.

Procurement activity

Expenditure and contracting activity

The Commission considers that summary information on procurement activity in South Australia does not occur to the level required to demonstrate where and how public expenditure on goods and services occurs. The benefits of better information collection and use on expenditure relate to:

- using information on suppliers to manage procurement strategies and expenditures, particularly for key suppliers in the industry and the nature of supply chain for key projects;
- creating an efficient process for generating reports for decision makers and to meet agency and whole-of-government reporting requirements, particularly on whole-of-government outcomes;
- determining the proportion of procurement spend under contract and where opportunities lie for disaggregation or aggregation of expenditure; and
- the future basis for determining categories of expenditure aligned to key corporate and government objectives.

The Commission acknowledges that to collect and utilise this type of information in the future at the level required will necessitate an investment of resources by the government; however, the Commission considers the benefits exceed the costs, especially if the information is used to target ongoing continuous improvement and benchmarking.

In terms of key government and agency contracts, currently only whole-of-government expenditure on key contracts is collected; however no usage (volume) or pricing data is collected at a whole-of-government level. The consolidated expenditure is not based on a sophisticated collection mechanism and does not track contract leakage (or expenditure related to the commodity or service through a supplier not part of the panel arrangements).

Supplier relationship in contracting with government

Currently, no data is collected on the outcomes of pre-qualified businesses (in terms of contracts won); neither is data collected on the number of tenders related to particular

business capabilities for which subsets of pre-qualified suppliers apply. This gap in data collection, which can be reported on by category of expenditure, business size and by industry, needs to be addressed to ensure that a large proportion of pre-qualified businesses are not competing for small amounts of procurement contracts and to ensure a better understanding of the capabilities of the supplier market.

The Commission has found limitations in levels of oversight and reporting in construction procurement of tracking of expenditure and stages of work throughout construction projects, particularly tracking subcontractors engaged and payments to contractors. Further, the identification of suppliers performing individual pieces of work at the project level is a responsibility of project managers, usually an external contractor to government. This lack of line of sight does not allow for a holistic picture of the project structure in terms of coordinating stages of work and milestones but also in terms of supplier management. This increases risks for government of not paying contractors on time or providing small business with opportunities to tender for business.

Procurement strategy

In Stage 1 of the inquiry, the Commission concluded that the governance arrangements do not promote forward planning or strategic oversight in the procurement system and the lack of information on future opportunities is a symptom of the lack of strategic oversight.

The Commission recommended that in order to strengthen the capacity of SA businesses, especially SMEs, to compete in government procurement opportunities, each agency should be required to meet its obligation by:

- publishing a complete forward procurement program setting intentions and probable timing in the coming 12-month horizon on a moving basis;
- publishing a complete list of current contracts with planned intentions of extension or market approach on a 12-month moving basis.

The government has accepted this recommendation.

Timeliness

The procurement system currently has only one measure reported at an across-government level. This is timeliness of the procurement process, reported as the median time taken to complete the procurement process from sign-off of the acquisition plan through to contract award. South Australia is the only jurisdiction to report on this measure. Whilst the Commission understands the reservations regarding publishing nominal timeliness metrics, it is recommended that agencies report on whether they have met the expected timeframes and, where overruns have occurred, whether time to undertake the process has gone beyond an acceptable margin of time (this margin would necessarily be higher for complex projects).

Acquisition planning

Another aspect of the tender process not adequately captured in terms of measurement relates to the effectiveness of the acquisition planning process. Currently, only acquisition planning that involves the SPB is recorded in South Australia. This does not provide an

indicator of the appropriateness of the market approach or the extent and accuracy of the market research on the project.

The Commission considers that variations to the scope of projects and reason recorded to identify common causes can assist with continuous improvement in the planning for procurement process.

Further, the Commission considers that the clarity of communication of requirements to suppliers is also weakly measured and that sampling of responses to tenders should occur to provide an assessment of whether the supplier understood and addressed the requirements adequately. This sampling process can be built into the annual auditing process of agencies.

Contract management and risk management

With respect to contract management, the Commission found that the tracking of contracts within agencies, particularly renewal or expiry dates and outcomes, the tracking of variations to contracts and the reasons for variations occur sporadically and in an uncoordinated manner within agencies and across the government sector.

In terms of risk management, the reporting within agencies on common risks, outcomes of risk treatment when risks materialise and where the responsibility for risk lies has been found to be inadequate. The failure to track risks by types of procurement, by types of contract and across an agency’s expenditure profile does not allow for improvements in how the organisation treats risks and may also lead to poor or ill-informed decision making and process reform.

To enable better treatment of risks and assessment of risk management processes, the Commission recommends that information be collected and utilised by agencies on:

- the owner of the risk by business size for key strategic or high-risk projects; and
- outcome of risk treatment by contract type where the risk materialised.

Table 4.1: Draft measurement matrix for procurement activity

Criteria	What to report/measure	Benefits	Across government	Agency level	Data currently collected
Expenditure on goods and services	Expenditure by: <ul style="list-style-type: none"> ➤ supplier or supplier groups ➤ commodities or service groups (categories) ➤ locality of supplier ➤ business size 	<ul style="list-style-type: none"> ➤ improved supplier management ➤ efficiency in reporting ➤ procurement planning ➤ category management 	×	×	Some data is collected on suppliers and categories in a small number of agencies. All agencies collect some form of supplier location data.
<i>Across government</i>	<ul style="list-style-type: none"> ➤ Whole-of-government or 	<ul style="list-style-type: none"> ➤ Greater information for market on key 	×	×	Totals of data for most but not all

Criteria	What to report/measure	Benefits	Across government	Agency level	Data currently collected
<i>and agency panels</i>	<ul style="list-style-type: none"> whole-of-agency expenditure ➤ contract volumes and pricing ➤ contract leakage⁷⁶ ➤ outcomes ➤ number of contracts won by pre-qualified suppliers for each contract by service area/commodity 	<ul style="list-style-type: none"> government contracts ➤ better information for agencies to support use and strategy for common purchasing ➤ greater transparency and effectiveness in use of panel contracts and better matching of supplier capabilities to organisation need 			contracts is collected but not published. Agency information and usage data not available
Contracting activity	<ul style="list-style-type: none"> ➤ Contracting activity by department, by category and commodity 	<ul style="list-style-type: none"> ➤ Efficiency in reporting ➤ procurement planning ➤ category management 	×	×	Yes for contracting activity. However, up until 2017–18, commodity data collected by SPB. Category management approach not used currently
Procurement strategy	<ul style="list-style-type: none"> ➤ Development and regular update of planned procurement projects 	<ul style="list-style-type: none"> ➤ Publishes list of future procurement projects 	×	×	Yes. Value of information can be improved.
Procurement activity					
<i>Timeliness</i>	<ul style="list-style-type: none"> ➤ The time taken for agencies to process tenders relative to published timeframe 	<ul style="list-style-type: none"> ➤ Accountability for service standards of agencies for low-risk tender processes 		×	Median time taken is published. Published service standards or time expected for process not mandatory.
<i>Acquisition planning</i>	<ul style="list-style-type: none"> ➤ Variations to plans ➤ instances of mis-specification of tender documents 	<ul style="list-style-type: none"> ➤ Helps identify common causes in process and improve capability in specifications and market research 		×	Not collected currently

⁷⁶ Expenditure related to the commodity or service through a supplier not part of the panel arrangements.

Criteria	What to report/measure	Benefits	Across government	Agency level	Data currently collected
<i>Contract management</i>	<ul style="list-style-type: none"> ➤ Supplier performance ➤ tracking of contract renewal dates ➤ tracking of variations of contract and reasons for variation 	<ul style="list-style-type: none"> ➤ Improves contract management performance and performance of suppliers. 		×	Tracking of contract renewals is piecemeal across agencies. Reasons for variations and tracking not done currently.
<i>Risk management</i>	<ul style="list-style-type: none"> ➤ Owner of risk by key projects ➤ outcome of risk treatment where risk materialised 	<ul style="list-style-type: none"> ➤ Better treatment of risk and improved risk management processes 		×	Not collected currently

Source: Office of the SA Productivity Commission

Capability

With respect to metrics and reporting of procurement capability, the Commission acknowledges current reforms occurring across the state government:

- Single business identifier – establishing a platform to enable agencies to retain information about business for service provision and transactions and for business to be able to maintain and update information with government. The process will enable streamlining of process for procurement
- Tenders SA Website reform – improvements to reporting capability, data classification and functionality to better progress elements of the tender process
- Installation across a selection of government agencies of contract management and tender process workflow systems.

The reporting functionality and output across the South Australian Government is not currently adequate in generating common outputs and metrics. The Commission has identified in the previous section what it considers to be whole-of-government metrics, noting much of what agencies are required to collect and report on will be particular to their purchasing responsibilities.

Beside system capability, the other key aspect of the ability of an organisation to function effectively is the capability of its people, which is covered elsewhere in this draft report. The desired metrics to demonstrate processes in place to ensure adequate capability development as well as reporting on current levels of agency capabilities will be discussed here.

Current levels of agency capability

In Stage 1 of the inquiry, the Commission found that data or information on human resource procurement capability is not collected nor reported as it is not considered to be a strategic priority. The Commission has found in its requests of agencies that information on numbers of staff engaged in procurement activities cannot be precisely determined. Although the SPB has a working list of procurement and contract management staff from public authority heads of procurement, capability development participants and other sources, this list is not derived from a common methodology or strict measurement regime.

Accurate information on the numbers, skills, education and experience of procurement staff is an essential foundation for development of the capability of the cohort of procurement professionals. Further investigation and request of agencies by the Commission indicates that the numbers of full-time procurement staff can be large or small depending on how it is defined. To enhance procurement staff development and capability development of organisations, capture and generation of information at agency level needs to improve markedly. At a basic functional level, information needs to be collected and utilised:

- on position descriptions for roles where procurement is a part of their responsibilities with an assessment on whether the procurement role is basic, intermediate or advanced level for each type of officer (the Commission suggests the key categories are decision-maker, manager and officers);
- the skill levels and experience of current staff in relation to key procurement competencies and the requirement of the organisation;
- the level of training requirements across business units and the organisation related to procurement competencies;
- integration of performance measures of procurement staff with key corporate objectives and procurement strategy KPIs.

Metrics on procurement staff development

Apart from those developed by SA Water, the Commission has not encountered metrics on procurement staff development or been made aware of the existence of these metrics in public authorities or prescribed authorities. Metrics that will be required are:

- baselines of capability assessments for procurement staff. This is essential for future assessment of not only how staff are performing but also the type and levels of staff development required.
- performance reviews to quantify future training requirements and identify areas of staff training or qualifications;
- quantum of training undertaken and quantum of staff with professional accreditation. This provides the agency with stock and flow of training requirements and training interventions required.

Table 4.2: Draft measurement matrix for procurement capability

Criteria	What to report/measure	Benefits	Across government	Agency level	Data currently collected
Current levels of agency staff capability					
<i>Position descriptions</i>	➤ Stocktake of procurement staff by decision maker, manager and officer level	➤ Supports gap analysis and recruitment		×	No
<i>Key competencies</i>	➤ Stocktake of key competencies for procurement roles based on skill/ experience by business unit	➤ Supports gap analysis and identifies training requirements		×	No
<i>Training requirements</i>	➤ Benchmarking of agency staff that meet minimum requirements for each competency	➤ Supports capability development and can be integrated into performance development		×	No
<i>Performance development</i>	➤ Gap analysis and training requirements and support for key corporate objectives			×	No
Procurement capability development					
<i>Assessment of capability</i>	➤ Establish baseline for future assessment	Supports continuous improvement in capability		×	No
<i>Review of performance</i>	<ul style="list-style-type: none"> ➤ Identifies areas for intervention ➤ Reviews achievement of corporate objectives 	<ul style="list-style-type: none"> ➤ Identifies future training requirements ➤ Identifies areas of corporate performance where capability can support 		×	No
<i>Training and qualifications</i>	➤ Quantum of training undertaken and quantum of staff with professional accreditation	Provides agency with stock and flow of training requirements and interventions		×	No

Source: Office of the SA Productivity Commission

Continuous improvement

The objectives of indicators for continuous improvement are to assess the extent to which government agencies have processes to support and monitor their performance and to formulate and implement improvement plans. This requires among other things the availability of information systems, a capacity for analysis, feedback mechanisms and planning capacity for implementation of improvements. These improvements are designed

to support efficient and effective procurement processes to address shortcomings where required and to maintain high organisational standards when they have been achieved.

It is very important that responsibilities are clearly assigned and are being performed to enable measurement of organisational capacity and measurement of progress in improving capacity over time.

The two key groups which provide measurement and feedback of procurement processes and performance are the two participants inherently involved in the system – suppliers and agency procurement staff. Regular feedback from both suppliers and agency staff on how the system is performing and feedback on how reforms are progressing is critical in measuring performance and making the necessary reforms in the future.

Agencies need to demonstrate that information strategy and training capacity exists to provide training, advice and assistance to develop the capacity of government and private sector participants to understand the rules and regulations and how they should be implemented. The purpose is to assess the existence and quality of advisory services on procurement matters for government agencies and the public at large.

A well-functioning system should provide for assessment or verification of advisory services or help desks for public or private sector parties where they can get advice on application and interpretation of policy and rules. The Commission recommends that instances of assistance provided to business units within agencies on interpretation of procurement policy and rules should be recorded by central procurement units to track improvements in agency understanding across all business units. Further, common instances should be tracked and addressed through internal guidance material provided to staff.

Guidance materials, policies and tools need to be tracked from when they have last been updated. Reporting should state whether they have lapsed, and they have addressed all requirements identified by staff. Government agencies are also to record that new staff have received the appropriate level of induction relevant to their procurement responsibilities and capacities.

The Commission recommends that queries on the tender process from potential suppliers, rather than specific responses or project-related matters, should be recorded by government agencies to track supplier understanding of procurement processes and rules.

The Commission has reviewed the survey of suppliers conducted by SPB and has concluded that the survey is overly long, can be subject to bias from respondents and does not allow for analysis of key outcomes. The Commission recommends that the engagement is reconstituted to steer away from the outcomes of the tender process itself and to elicit more meaningful feedback from suppliers on:

- areas of tender processes that can be improved;
- dialogue on the specifications and government requirements of tenders; and
- reflections on key aspects of evaluation.

The measurement of outcomes of supplier engagement and identifying opportunities for improvement are key components of ensuring that procurement processes and outcomes remain relevant and up to date.

Table 4.3: Draft measurement matrix for continuous improvement

Criteria	What to report/measure	Benefits	Across government	Agency level	Data currently collected
Benchmarking of performance		Enables comparison across the sector, with previous performance and with similar organisations	×	×	No
Organisational capability					
<i>Guidance, tools and policies</i>	Proportion of documents up to date (or lapsed) and proportion assessed as relevant by staff	Ensures staff knowledge is up to date and that guidance is keeping pace with business needs		×	No
<i>Induction for new staff</i>	Proportion of staff receiving appropriate level of induction	Ensures staff receive requisite information sources and procedural documents		×	No
Supplier engagement	Tender process seminars offered and attendance	Facilitates building of supplier capacity in understanding state government processes		×	No
Supplier feedback	<ul style="list-style-type: none"> ➤ Survey on key aspects of tender process ➤ Number of queries on tender process and tracking of common issues 	Provides indication of how agencies plan and execute processes, complexity of tender documents and contracting issues		×	Yes, SPB survey. However, this is overly long and needs to be focused.
Compliance monitoring and reporting	Staff use of established policies and tools (or alternatively instances where process not followed)	Ensures staff demonstrate knowledge and use of agency procurement processes		×	No

Source: Office of the SA Productivity Commission

Outcomes

One of the Commission’s findings in this inquiry has been the system’s inability to demonstrate the contribution of procurement to broader government objectives: competition and participation, involvement of SMEs in the procurement process, sustainable procurement, innovation and the proportion of government procurement supporting better social outcomes.

The draft matrix below outlines a suite of possible measures for each criterion to best demonstrate procurement contribution to outcomes.

The Commission considers that the amount of interest, on average, of suppliers in tender processes is an important indicator to monitor and to try and influence. The level of interest as determined by the number of bids gives an indication of the intensity of competition and may provide further information about types of firms applying. The same firms or same types of firms and reliance of local firms on government contracts will provide an evidence based to engage with suppliers.

Public authorities have expressed the difficult nature of influencing let alone measuring procurement’s contribution to innovation outcomes. A possible way of encouraging and measuring innovative outcomes is to monitor and measure the number of approaches to suppliers or from suppliers outside the normal procurement process that progress to a pilot concept or co-design with the public authority. This will enable a comparison across periods and between public authorities of the intensity of innovation outcomes involving procurement.

For sustainable procurement, the SPB framework provides for the assessment of impacts of procurement proposals on measures such as emissions, recycling and energy costs. These measures need to be quantified and reported on where impacts are assessed as relevant. In addition, where the evaluation criteria of a procurement project relate to sustainable procurement not only as a stated objective but also forming critical elements of supplier decisions, then these projects should be counted (and similarly for social procurement objectives).

Table 4.4: Draft measurement matrix for government and procurement related outcomes

Criteria	What to report/measure	Benefits	Across government	Agency level	Data collected currently
Competition and participation	Average number of bidders per tender (possible variables by industry, business size and by complexity)	Enables measurement of extent and interest in tendering as well as competitive nature of individual industries	×	×	No
Sustainable procurement	Number of tenders pursuing environmental objectives in addition to primary objective	Quantifies extent to which sustainable outcomes are being considered in tender processes	×	×	No
	Impacts on environment by key assessment metrics: <ul style="list-style-type: none"> ➤ energy costs ➤ use of recycled materials ➤ emissions 	Enables whole-of-government quantification of environmental impacts.			No
Innovation	Proportion of pre-market approaches that progress to purchasing or proof of concept	Enables assessment of level of innovation facilitated by agencies.		×	No

Social procurement	Number of tenders pursuing social objectives in addition to primary objective	Quantifies extent to which social outcomes are being considered in tender processes	×	×	No
---------------------------	---	---	---	---	----

Source: Office of the SA Productivity Commission

The Commission has not yet formed a final view on the data required to support the reporting regime that is required to improve accountability and improvement in public authority purchasing. The Commission has provided the measurement matrix in draft form to elicit feedback and comment from public authorities and stakeholders on:

- the extent of the indicators suggested and whether there is scope for adding to what is drafted here;
- the practicality of the indicators here and the extent to which they will provide for comparison, standard methodology for collection and reporting;
- the application across the public sector to collecting data on these objectives.

The Commission will follow up with agencies on this matter in the coming weeks.

It is proposed that agencies will measure and report on procurement benefits in accordance with whole-of government procurement performance principles issued by the Office of the Chief Advisor – Procurement SA. Implementation of the reporting framework would be overseen centrally by the Chief Procurement Officer to ensure best practice and meaningful reporting of performance utilising a standard methodology.

The Commission also proposes that the establishment of the measurement and reporting framework be initiated by baselining of agency and across-government performance, based on available information to provide a reference point for future measurement of progress.

4.2 Innovation

4.2.1 Introduction

The terms of reference of this inquiry include considering examples of contemporary procurement policies and practices from interstate, overseas and the private sector and their effectiveness in promoting innovation. This section addresses both construction procurement and procurement of goods and services.

Public procurement is generally considered an instrument for fostering innovation to deliver new or improved functionality in government procurement and by providing reference sites as a customer for innovative businesses. The use of public procurement to stimulate innovation is either incorporated within, or subordinate to, the primary function of government procurement, namely to perform public services at the best whole-of-life cost.

The policy dilemma sharpens when a public authority, in making its choice of what to buy, seeks innovation either by demanding goods and services that do not yet exist or by developing outcome criteria that encourage innovative solutions.

Promoting innovation can be incorporated into a policy framework with four categories:

- framework conditions such as rules and regulations governing procurement processes;
- identifying, specifying and signalling needs and outcomes;
- organisational capabilities of public authorities; and
- incentivising innovative solutions.

The Commission has considered the interaction of innovation goals and public procurement through two lenses of the framework. First, the use of enabling administrative processes and policies to support public procurement outcomes when procuring innovative goods and services and, second, using public policy instruments to support innovation by suppliers.

4.2.1.1 South Australian procurement system design for promoting innovation

Construction procurement

DPTI guidance material for building infrastructure discusses innovation in the context of shared risk contracts being part of the contractor risk and reward system.

DPTI offers reward for contractor performance related to innovation where the objective is to encourage contractors to adopt a proactive culture on the lookout for continuous improvement. DPTI offers reward for excellence in the management of construction contingency or for achievement of on-time completion.

The guidance material states: 'some of the risk and reward initiatives have proved to be right in principle but very difficult to administer in practice. There needs to be a balance of new initiative opportunities with appropriate rather than unwieldy administration'.⁷⁷

DPTI guidance material for building construction includes a schedule of delivery models and selection factors including the presence of innovation in design and construction and the level of innovation desired. There is no further guidance on the relative merits of different delivery models from an innovation perspective.

Goods and services

Agencies dealing with innovative proposals must comply with the SPB policy on probity and ethical behaviour, as well as other government policies, guidelines and codes to govern ethical behaviour and to prevent fraud and corruption.

Currently there is limited guidance for public authorities on supporting innovation and evaluating innovative proposals in the suite of policy/guidance documents issued by the SPB. Innovation and IP do not have a dedicated policy or guideline and are not common themes in other guidance material. Procurement officers in public authorities use, when the situation requires, the South Australian Government Intellectual Property Policy which, in relation to consulting, states that:

- Agencies must ensure all contracts and other legal documents with third parties effectively address IP. This is generally taken to mean the state owns the IP.

⁷⁷ DPTI, *Understanding Building Construction Procurement*, January 2012, pp. 7-8.

- Ownership of IP should be specifically addressed whenever it may be generated or acquired (e.g. under terms of employment or other contractual arrangements).
- If the agency will not hold ownership of the IP, access and reuse of that IP should be specifically addressed to maximise public value. This can act as a further barrier to innovative businesses, particularly SMEs for whom IP may be their principal asset.

Stakeholder views and the innovation processes in practice

In Stage 1 of the inquiry, stakeholders indicated that the application of the state's IP policy can have an adverse effect on innovation outcomes. These views come from business stakeholders (mainly ICT projects and other innovative products or services) that have successfully competed outside South Australia, but found winning business inside the state more difficult.

These businesses observe public authorities insist that the state should own all IP developed, and see this as a barrier to doing business, particularly where the state has no capability to exploit it. This position on IP not only discourages innovative businesses from competing for South Australian Government tenders, but also acts as a barrier to business development in the state.

Supplier feedback to Business SA also indicated frustration about the general requirements for IP transfer in state government contracts that were disincentives to innovation and questioned why the government necessarily had to own businesses' IP (Business SA submission).

Requirements for IP ownership by the government were seen as major barriers – in some cases show stoppers – to supplying innovative goods and services to government.

Business stakeholders said they would not share IP with public authorities without strong safeguards to prevent their IP being given to competitors in the tender disclosure process or through future procurements.

The AIIA (Australian Information Industry Association) relayed views of their membership that innovation in procurement policies of government can be enhanced by:

- ensuring contracts allow for emerging and incremental technology improvements and innovations as well as emerging products and services during the contract term, without the need for an additional procurement process;
- creating a mechanism for innovation activities (such as proof of concept initiatives) and allowing for development or technology evaluation as part of the contract;
- providing suppliers with the problem to be solved, rather than a prescriptive solution to enable suppliers to innovate to an outcome; and
- providing platforms for engagement with industry, informing the market on government expectations, and the government of what is available from the market.

AMCA SA commented innovation in procurement requires a precise definition and description of objectives and implementation. AMCA SA stated innovative tenders need to ensure:

- the level of design and documentation can be understood and responded to meaningfully by suppliers where goods and services have characteristics not widely used in the market place;
- the specifications elicit responses from various specialist tenderers to enable clear assessment of what is required and the application of special design, products, performance, efficiency, operational costs and whole-of-life considerations;
- the scope is open enough to allow suppliers to interpret the government's requirements.

Innovation policy in South Australia

The Office of the Chief Entrepreneur has recently published the SA Government's Future Industries Exchange for Entrepreneurship Strategy, which supports local businesses to improve their capacity to innovate and commercially develop proposals.

The strategy recommends the adoption of smart procurement policies to source more innovative solutions from entrepreneurs and early stage businesses. The elements of the Smart Procurement Policy are:

- Public authorities are to take account of the objectives of the policy in their own purchasing strategies and procedures.
- A single sourcing procurement methodology will be developed for innovative start-ups and SMEs to develop and grow through securing opportunities for procurements valued up to \$550 000.
- The private sector will be encouraged and incentivised to collaborate and co-invest with government to deliver on stated government objectives.
- A series and schedule of Hackathons and 'Meet the Buyer' or supply chain events will be developed to connect start-ups with potential public and private customers.

The policy would take effect through the SPB's policies and guidelines.

Procurement policy in innovation in other states

In Stage 1 of the inquiry, the Commission concluded the current guidance and engagement model was unsatisfactory, essentially reducing the intended relationship on IP to a contractual level, excluding a relationship from which public authorities can derive high levels of value. The state's current engagement model does not provide for:

- identifying the most effective means of engagement;
- navigating the different engagement processes throughout the procurement cycle;
- mitigating the risks that arise from engagement with industry such as giving feedback and discussions around the use of IP;
- tailored guidance for particular industries, such as ICT, which is a source of higher-complexity industry engagement; and

- measuring the outcomes of engagement and identifying opportunities for improvement

The government accepted the Commission's recommendation in Stage 1 for a government supplier engagement planning process for use by agencies as well as recommendations to improve access to tender opportunities.

For Stage 2 of the inquiry, the Commission reviewed innovation systems and processes to support public procurement among other jurisdictions in Australia. The Commission observes in South Australia that:

- The guidance and practice on early engagement with suppliers to elicit innovative proposals and how to organise agency processes to support innovative processes is inadequate for use by public authorities.
- The guidance and policy documents supporting treatment of IP issues with suppliers is not adequate for use by public authorities.

4.2.2 Findings

The issues from other jurisdictions fall into two broad groups:

- innovation in procurement and design of intellectual property
- the use of public policy instruments.

4.2.2.1 Innovation in procurement and intellectual property policy design

The Victorian Government provides guidance for their procurement staff on encouraging and facilitating innovation in procurement. The guidance covers four action areas⁷⁸:

- organisational alignment
 - identifying organisational programs, deliverables and key procurement categories. A key feature of this element is determining which areas of spend can be dedicated to or are feasible for innovation related purchases through agency procurement plans.
 - developing contract management strategies to identify categories of procurement that lend themselves to flexibility in supplier engagement
 - developing the agency supplier engagement plan.

early market engagement Through carrying out regular market sector scanning in concert with business associations. (This type of approach is formalised in Queensland through the use of Category Councils.)

Early supplier engagement, Providing suppliers with sufficient time to scope and respond to procurement requirements, incorporating innovation into value for money calculations, devising multiple stages to the market approach and structuring

⁷⁸ Victoria Department of Treasury and Finance – Innovation and the Procurement Process – Procurement Guide, October 2012.

specifications on an outcomes-basis supported by steps such as delineating core and non-core elements to enable suppliers to propose alternate solutions;

innovation support activities. These can include pilot projects, risk sharing or inducements and rewards.

The Australian Government issues, for use by all *Public Service Act* entities, a statement of IP principles that provides a broad policy framework for IP management by Commonwealth departments. The statement of principles is supported by extensive guidance material including⁷⁹: a manual; model contract clauses for ICT contracts, and related explanatory material; and guidelines on licensing public sector information for government departments.

The guidance material covers:

- managing IP across the stages of the procurement process:
 - incorporating the preferred IP position of the department into relevant market documentation or contracts;
 - managing IP during the life of the contract;
 - managing IP upon termination or expiry of the contract;
- instruction on conducting an IP needs analysis and the advantages and disadvantages of types of IP/ownership rights;
- types of arrangements that give rise to IP issues; and
- identifying government needs for IP, taking account of value for money considerations and broader government objectives such as sustainable sourcing or support for social enterprise.

The principles and guidance material enable departments in the Australian Government to develop individual IP management frameworks that reflect their own needs and purposes.

The New South Wales Government has developed comprehensive guidelines on management of IP⁸⁰ and the Queensland Government has developed IP principles to provide a high-level policy guide for public sector agencies in managing IP.⁸¹

This contrasts with the information provided through the South Australian DPC Policy on IP which provides little practical guidance for officers in managing IP of suppliers in the procurement process. The inclusion of IP is not a mandatory requirement in the procurement process.

The issue generally arises where public authorities are purchasing a product or service that is designed wholly for use of the public authority or when suppliers in providing a good or service want to protect their IP applied during the project. It is the intent of the state's policy that only the instances where the entirety of the product and all capital developed are wholly for the use of a public authority where IP transfers to the government. In such

⁷⁹ Australian Government, Intellectual Property Manual, June 2018, p. 10.

⁸⁰ New South Wales Government, Intellectual Property Management Framework for the NSW Public Sector, Premier's Department, 2005.

⁸¹ Queensland Government, Queensland Public Sector Intellectual Property Principles, January 2013.

circumstances it is reasonable to consider IP as a part of the contractual arrangements, without accepting the point that the expectations of suppliers should always be met. There are alternatives to state ownership that should be considered and adopted where appropriate.

The Commission previously observed the lack of data, information and details on how innovation is promoted in South Australia and the low level of importance attached to efforts in promoting innovation.

4.2.2.2 The use of public policy instruments to support innovation by suppliers

Most jurisdictions now seek to encourage innovation through procurement, with a focus on outcomes rather than through prescriptive tender processes. The intensity of effort in employing policy instruments to support innovation differs across jurisdictions in practice.

With respect to activities supporting innovation, interstate and overseas experience and practice indicate that instruments used to identify, specify and signal needs as well as incentivising innovative solutions include:

- pre-commercial procurement of R&D to develop and demonstrate solutions, for example the SBIR (Small Business Innovation Research) Program;
- innovation programs to bring suppliers and users together, such as innovation partnerships, category councils, meet the buyers (or other similar events);
- calls for tender requiring innovation with guaranteed levels of purchasing or certification of innovation, which can be a feature of some proof of concept programs; and
- insurance guarantees.

The Victorian Innovation and Procurement Process / Guide details innovation activities such as pilot projects, cost sharing and longer-term contracts for innovative products, sharing of elements of risk not normally apportioned to particular parties and licensing arrangements. The Department of Agriculture and Fisheries, in Queensland, for example, developed new varieties of fruits and vegetables, and then licensed them for distribution and commercialisation

The relative merits of program type have been highlighted in evaluations of programs, such as the SBIR in the US. A key feature of these policies is to move beyond the statement of objective, which is usually couched as promoting innovation to organising in agencies function and form to be innovative.

An overwhelming focus on value for money considerations, and concerns about risk minimisation, in public sector procurement can stymie innovative solutions to public problems.⁸²

The Commission notes such schemes also accept a higher level of functional risk in generating better goods, services and infrastructure, while structuring the risk management effectively. In particular, compared with mainstream procurement such schemes presume a

⁸² *Australia's Economic Future: An Agenda for Growth (June 2016)*, CEDA, p. 18.

higher level of failure as part of the overall price in developing innovative outcomes that deliver significant net benefits to the state.

Acknowledging that 'responsibility for innovation resides with business and not government' but that 'government can act as a catalyst for change', CEDA has recommended funding SME innovation through an exploration of research and development focused public procurement programs like the US Small Business Innovation Research (SBIR) program.⁸³

The choice of activities usually included inducements awards, pilots – identification, specification and signalling of needs or incentivising innovative solutions.

Queensland

The Queensland government's SBIR program is based on the US and UK counterparts. It releases innovation challenges and funds the development of innovative solutions through a staged procurement process. The five stages see challenges issued to the market, proposals assessed, successful propositions funded (for up to six months) for feasibility. Feasible solutions are funded for up to 12 months for proof of concept.

Successful applicants retain all IP they develop within the SBIR program, and have the potential to secure a government lead customer for a tried and tested product which is ready to attract further investment.⁸⁴

The *Testing Within Government* program borrows from the SBIR principles. This program supports ICT SMEs 'to improve the positioning of their products by working collaboratively with Queensland Government on a number of business problems'. Successful applicants are funded for a 12-week program, at the end of which products are showcased to government and industry representatives 'improving the potential to access broader commercial opportunities in Queensland, Australia and internationally'.⁸⁵

The Queensland government has accepted the premise that 'Adopting less prescriptive, outcome-based approaches where appropriate, can support increased market innovation'. The recently released *Using an Outcome-Based Procurement Approach Guide* issued by the Queensland Office of the Chief Advisor – Procurement sets out what an outcome-based specification is, when it is suitable to be used, and evaluation and reporting guidance. It includes a 'readiness assessment' which supports agencies to determine if an outcome-based approach is appropriate for a specific procurement.⁸⁶ The outcome-based approach is underpinned by the Queensland Procurement Policy.⁸⁷

The Queensland Department of Housing and Public Works has indicated innovative ways of engaging with business are encouraged. Practices supporting co-design (within appropriate

⁸³ Ibid, p. 13.

⁸⁴ Small Business Innovation Research, Advance Queensland, Queensland Government, accessed at <https://advance.qld.gov.au/entrepreneurs-and-startups-industry-small-business/small-business-innovation-research> on 7 March 2019

⁸⁵ Advance Queensland, Testing Within Government, accessed at <https://advance.qld.gov.au/entrepreneurs-and-startups-small-business/testing-within-government> on 8 March 2019.

⁸⁶ Using an outcome-based procurement approach - Office Of The Chief Advisor – Procurement, accessed from <http://www.hpw.qld.gov.au/SiteCollectionDocuments/UsingOutcomebasedProcurementApproach.pdf>, 8 February 2019, p. 4.

⁸⁷ *Queensland Procurement Policy* 2018, Principle 4.3.

probity settings); and systems development in consultation with service providers that will assist procuring agencies to identify service providers with accreditations and policies in place that support government policy outcomes are being explored.

Queensland has recently introduced SparkPlug, which provides opportunities for innovative suppliers in particular focus areas (e.g. emergency services; drone technology; artificial intelligence) to pitch directly to relevant government decision makers. Although there is no funding attached to this program, it is intended to help build both connections and capability for both start-ups and government participants, and ultimately lead to small scale trials, pilots or other contracts.

New South Wales

The NSW Government has drawn on the underpinning principles of the Small Business Innovation Research (SBIR) model in its Procurement Innovation Stream, including:

allows procurement-accredited agencies to directly engage an SME on short term contracts valued up to \$1 million and to do proof-of-concept testing or outcomes-based trials. The test or trial should be designed to demonstrate the feasibility of a good and/or service to solve a specific problem or improve government service delivery.

Agencies can then award a contract following a successful test or trial, subject to procurement rules. SMEs retain ownership and can potentially derive ongoing value from their innovative products and IP.⁸⁸

4.2.3 The Commission's view

4.2.3.1 South Australia's innovation policy

The Commission has heard from stakeholders, particularly in the construction sector, and public authorities that the desire and the readiness to engage using more open and collaborative procurement processes designed to meet the governments needs is strong in appropriate circumstances. That is a noteworthy qualification.

During both stages of the inquiry, the Commission has not been presented with quantitative information that enables easy assessment of the extent of innovation in procurement processes and outcomes. Based on the evidence received from stakeholders and public authorities:

- In construction procurement, the spectrum of delivery models in theory allows, to varying extents, innovative design and contractual arrangements for delivering on that design and broader objectives of projects. In practice, preferences for relationships between contractors and government and the advantages offered by particular types of models appear to override consideration of innovation and design. This may be dictated by government considerations of budget, availability of key Tier

⁸⁸ NSW Government Small and Medium Enterprise and Regional Procurement Policy, accessed at <https://procurepoint.nsw.gov.au/policy-and-reform/goods-and-services-procurement-policies/nsw-government-small-and-medium-enterprise> on 18 February 2019, p. 10.

1 contractors and timing (scheduling the delivery of projects related to service provision or political considerations).

- In goods and services procurement, while the guidance on innovation is more comprehensive and explicit than construction procurement, the size of private suppliers and the focus of public authorities on delivering financial savings in their purchasing are said to cause public authorities to be reluctant to encourage and select innovative solutions. The use of preferred suppliers and negotiation with one or a small number of suppliers reduces competition and the potential for innovative products to meet business requirements.
- Low importance attached to strategic planning drives a reticence to engage with suppliers at critical parts of the planning process and reduces collaboration with suppliers throughout the contract management process. From the Commission's observations of tender documents and purchase recommendations from agencies, these concerns appear to result in the choice of more expensive bids that have in-built insurance against risk of project failure.
- Innovation is treated by public authorities as an administrative exercise, rather than as a tool to enable public authorities to meet their purchasing objectives. To support this conclusion, engagement with public authorities by the Commission has revealed very few examples of innovation in procurement. Public authorities and businesses do not find common understanding in terms of the application, use and development of innovative products and services.
- There is evidence, for both goods and services and construction procurement that probably significant value is being missed in terms of what the market has to offer and what public authorities are willing to take up. The Commission has heard this from business stakeholders particularly in ICT who have found it difficult to win government business in South Australia but not in other states and in the construction sector where the focus on price and timeframes reduces the likelihood of innovation in design.

The current procurement frameworks for construction and goods and services, in design and in practice, do not systematically enable collaboration and commercial partnership on proposals for purchasing goods and services with innovative characteristics. The underlying causes seem to be:

- Innovation often occurs during the market approach phase rather than at project design. Project design is where most of the benefits can be realised.
- A lack of understanding of the impact of procurement specification and procession on innovation. The purchase of emerging products by government can provide a reference site that materially increases the prospects of the successful company of making sales elsewhere.
- The absence of processes applied within agencies across the public sector to identify opportunities for innovative solutions coupled with poor market engagement.

The Chief Entrepreneur and the Industry Advocate have argued for the Smart Procurement Policy to become part of the government's entrepreneurship and innovation policies and programs. The Smart Procurement Policy would ensure that local businesses would have better opportunities to participate in trials and pilots of their products and to gain more widespread acceptance of their innovative products by South Australian government agencies.

The Commission notes no evaluation mechanism is proposed, which is undesirable.

The Commission broadly agrees with the views of the Chief Entrepreneur that the policy environment supporting innovative ideas of local business can be improved by:

- Enabling innovative proposals to operate within the accepted framework of procurement policies and guidelines of single source procurement from suppliers identified as having innovative products or services – essentially a 2-stage framework.
- Providing agencies to take the risks inherent in procuring innovative products, including the approach to helping businesses developing their IP.
- Simplifying procedures to support innovative tendering that focus more on capability and capacity of the proposal rather than capturing administrative information which does not enable effective evaluation.
- Has incentives and reduced barriers to business and public authorities to collaborating on a greater scale on future purchasing requirements (including goods and services and construction), consistent with probity. Such programs or incentives can occur through category management plans, meet the buyer type events and more extensive supply chain management.

Draft recommendation 4.2

To encourage innovative procurement offerings in government procurement, the Commission recommends that policy and practice be amended to make express provision for:

- innovative proposals to operate within the accepted framework of procurement policies and guidelines of single source procurement from suppliers identified as having innovative products or services – essentially a two-stage framework.
- agencies to accept and manage the inherent risks involved in procuring innovative products, including the approach to helping businesses developing their IP.
- procedures to support innovative tendering that focus on capability and capacity of the proposal rather than capturing administrative information which does not enable effective evaluation.
- flexibility for both business and public authorities to collaborate on a greater scale on future purchasing requirements (including goods and services and construction). Such programs or incentives can occur through, for example,

category management plans, meet the buyer events and more extensive supply chain management.

- increased attention by public sector authorities to identifying areas that would benefit from innovative purchase practices.

The Commission notes that a more capable procurement profession capable of higher discretionary judgement would underpin efforts to stimulate innovation. The professional capability issue is discussed in more detail in Section 3.2.4.

4.2.3.2 Intellectual property guidance material

The Commission considers the current guidance and policies on managing IP in procurement are inadequate specifically in relation to providing certainty and confidence for suppliers or procurement officers. This situation has led to a reluctance on the part of suppliers to engage with government or to approach government with their product, particularly SME's. It has also led to the risk averse nature of procurement processes overstating and overriding the possible benefits. This calls for much greater flexibility for IP contract provisions in government contracts and clear guidance for procurement staff.

The benefits of redressing this situation are that:

- Officers in public authorities would have authoritative information in engaging with suppliers on IP issues;
- Suppliers would have complete transparency on how their IP will be handled in specific situations.

Draft recommendation 4.3

In order to reduce the impediment to innovation and improvement that aspects of current contracting arrangements may impose, Commission proposes that a clearer, set of arrangements be put in place by:

- developing and publishing improved guidance on the state government Intellectual Property policy to provide a wide range of examples of particular types of procurement and the state's position on ownership of IP;
- including in the guidance contained in the state government intellectual property policy guidance on the relative merits and instructive case studies for construction procurement outlining the factors for various delivery models and greater flexibility in contract provisions; and
- providing guidance on managing IP covering needs analysis, managing IP through the procurement process and model clauses and contracts that address matters raised by stakeholders.

5. SA Industry Participation Policy for construction and prescribed public authorities

The terms of reference for this inquiry direct the Commission to evaluate the effectiveness of the SA Industry Participation Policy (SAIPP), ‘...in particular the IPP’s impact on:

- a. Competition between firms, including those from interstate and overseas;
- b. Prices and value for money of goods and services procured over time; and
- c. Broader economic effects such as the growth of local industry and employment.’

The Stage 1 report addressed this task from a goods and services perspective. This chapter specifically addresses the interaction between industry participation and construction procurement by public authorities and prescribed public authorities (PPAs). The evidence is drawn from consultation, submissions and data provided by those authorities.

The use of government procurement to contribute to stronger local employment, sourcing, investment, upskilling and other social outcomes, is looked at in the context of maintaining:

- the competitiveness of South Australian businesses;
- administrative simplicity;
- value for money;
- capable suppliers (i.e. those that can supply goods, services and capital that are fit-for-purpose for government needs); and
- compliance with all relevant legal requirements.

This chapter sets out the operation and impact of the SAIPP for construction projects and analyses implementation issues raised by businesses, public authorities and PPAs.

5.1 Overview and application of the SAIPP to construction projects

The Industry Advocate role was established in 2013 to help businesses based in South Australia take advantage of opportunities from the South Australian Government’s procurement, infrastructure projects and grant funding activities. The *Industry Advocate Act 2017* commenced on 1 January 2018. It establishes the Industry Advocate as a statutory position with specific functions and powers to further the objectives of the SAIPP. The policy aims to ensure South Australian businesses are given a full, fair and reasonable opportunity to compete for government contracts.

A comprehensive overview of the functioning of the SAIPP was provided in Stage 1 of the inquiry. Since then, machinery of government changes transferred the responsibility of the SAIPP from the Department of Innovation and Skills (DIS) and the Minister for Innovation and Skills to the Department of Treasury and Finance (DTF) and the Treasurer.

The policy development and application of the SAIPP now falls under DTF, with DIS continuing to look after the systems supporting the scoring of Economic Contribution Tests

(ECT) and Industry Participation Plans (IP Plans), through an agreement between the Chief Executives of DTF and DIS. The advocacy, compliance and annual reporting functions remain with the Office of the Industry Advocate (OIA).

The SAIPP is implemented by:

- The OIA which:
 - checks if the project is within scope of SAIPP;
 - assists the client authority and reviews the draft acquisition plan for projects above \$4 million (\$1 million in regions);
 - reviews and negotiates IP Plans and tailored IP Plans;
 - maintains the scoring system (currently done through DIS); and
 - responds to queries from suppliers or authorities.
- The Industry Advocate who:
 - advocates for the SAIPP;
 - builds the capacity of local businesses to tender for Government work;
 - receives and investigates complaints about the SAIPP and makes recommendations to resolve them; and
 - monitors compliance by authorities and suppliers with the SAIPP, including the issuing of directions to suppliers and reporting on non-compliance to the minister. This activity commenced at the beginning of 2018 and will be reported on for the first time in October 2019.
- Public authorities that:
 - determine whether to increase the minimum weighting (through an expanded economic opportunity assessment);
 - test the data provided by suppliers;
 - include the ECT or IP Plans scores in their tender evaluations;
 - report to both the OIA and SPB on scores for the winners of their tenders; and
 - include IP Plans commitments as contractual requirements for relevant projects.
- Suppliers that are responsible for completing ECT and IP Plans and reporting their performance against commitments in IP Plans on labour force metrics.

For construction specific issues, the Industry Advocate engages with businesses directly and through the Industry Advocate's 'Building and Construction Industry Advisory Panel'. This panel provides input into the development of new initiatives by the Industry Advocate and feedback on the delivery of the SAIPP objectives.

Construction projects, like goods and services, fall under three categories according to value:

- Between \$33 000 and \$4 million (or \$1 million in the regions): tenderers are required to provide an Economic Contribution Test (ECT) and above \$220 000, the client agency must give a minimum weighting of 15 per cent to the ECT score in the tender evaluation. The Commission notes that the Government has agreed to adjust the thresholds for the ECT which will impact on the construction thresholds referred to here⁸⁹.
- Between \$4 million and \$50 million: tenderers are required to provide an Industry Participation Plan (IP Plan) and the client agency must give a minimum weighting of 15 per cent to the IP Plan score when evaluating the tender.
- Above \$50 million (major infrastructure or major construction projects): tenderers are required to develop, with the OIA, a tailored IP Plan that considers the economic development objectives of the Government.

If a program of interlinked small infrastructure projects is funded by government or if the project is in a priority area of focus, a tailored IP Plan may also be developed from inception.

In addition, for projects triggering an IP Plan and involving the purchase of structural and reinforcing steel, a minimum 20 per cent weighting will be applied, and the steel used will have to meet the requirements of the relevant Australian Standards.

The scoring of ECT or IP Plans for construction projects includes consideration of:

- For ECT:
 - percentage of labour hours in SA (expressed either in hours, in value or in percentage) and in the region (if regional ECT), from the supplier and its subcontractors;
 - participation of aboriginal business (yes / no); and
 - level of SA contribution to the supply chain of goods provided (from manufacture to supply, in percentage of the value of goods provided).
- For IP Plans:
 - local supply of labour and sourcing for each item of the project (expressed in value and economic descriptor for SA and regions: from nil to very strong);
 - use of aboriginal business (yes / no);
 - use of SA existing and new apprentices and trainees (yes / no);
 - level of SA contribution to the supply chain of goods provided (tick the box from manufacture to supply);

⁸⁹ SAPC Stage 1 Procurement Inquiry Report, recommendation 3.4 to lift the ECT threshold to \$500,000 excluding GST.

- investment, located or to be located permanently in South Australia, in plant, machinery and equipment required to deliver the contract (tick the box in the following ranges: up to \$50 000, \$50 000 to \$200 000, \$200 000 to \$400 000, \$400 000 to \$1 million and above \$1 million); and
 - investment in SA research and development (R&D) or use of SA intellectual property (yes / no).
- For tailored IP Plans, in addition to the IP Plans criteria:
- employment and subcontracting opportunities specific to the building and roads construction sectors;
 - implementation of the Steel Policy;
 - delivery of the Skilling South Australia Procurement Guidelines (15 per cent of the labour force hours need to be performed by trainees and apprentices and other nominated groups including cadets, long-term unemployed, people with barriers to employment, aboriginal jobseekers and graduates); and
 - any other criteria which could be leveraged to generate employment outside the contract for South Australia.

In regions established as economic participation regions, the weighting is increased to a minimum of 20 per cent.

5.2 Evidence of the impact of the SAIPP

This section considers the evidence on the effectiveness of the SAIPP as it relates to the scope of the Commission's Stage 2 inquiry including:

- the information from submissions, meetings and interviews with businesses and agencies collected by the Commission as part of the Stage 2 inquiry;
- the Commission's analysis of the databases maintained by public authorities on construction contracting activity between 2015-18;
- the Commission's analysis of a random sample of 106 construction tender evaluations.

5.2.1 From submissions received by the Commission

As indicated in the Stage 1 final report, most business associations and external stakeholders support the intent of the SAIPP. Some positive comments have been recorded:

'Our members have seen the benefits of the industry participation focused on creating opportunities for local business, including building and construction' (AMCA submission)

'We see the impact (of the Industry Participation Policy) as positive' (O'Connor submission).

However, many stakeholders told the Commission they perceive there has been a limited impact as a result of the SAIPP:

- they have not seen much or any demonstrable effects from the policy;
- it is too easy to get a high score, therefore defeating the purpose of differentiating bids based on local participation;
- there is no preference provided to SA based businesses

'...award[ing] such projects to interstate companies who may pass the Industry Participation Policy though their employment of SA based workers does nothing for the long-term success or indeed survival of SA based sub-contracts' (Specialist Contractors SA submission);

- *'The other state governments have a support local policy and follow through with it. The State Govt' have a policy but do the opposite and encourage interstate companies to win work and take the overheads / margins and profit money back interstate. It has been happening for a long time and that money could have underpinned the state'* (quote in Ready to Tender research project 2019⁹⁰).

This has been corroborated by several public authorities who have indicated that national constructors tend to perform very well from an SAIPP perspective as they usually have a presence in SA and employ a strong local team. However, one national firm questioned the assertion that interstate or national firms are favoured under the SAIPP, citing instances where it has been unsuccessful in competition against local businesses.

Some of the comments also reflect a limited awareness of South Australia's obligations under free trade agreements, including the Australia and New Zealand Government Procurement Agreement (ANZGPA), that do not permit preferences for local suppliers but do allow an emphasis on capital investment, labour, supply chain opportunities and the associated economic contribution to the state.

In that sense, the objectives of the SAIPP, which is not to favour local businesses, but to encourage the use of local labour, local goods and services, and investment in SA, are met.

In the database consolidated by the Commission on the construction spend for four government agencies, and on procurement including goods and services for five PPAs:

- a total of nine per cent of contracts for the period 2015 to 2018 (four per cent for 2017-18) were scored for ECT/IP Plans;
- two per cent of contracts were reported exempt from the use of ECT/IP Plans for the period 2015 to 2018 (1.2 per cent in 2017-18);
- the other 89 per cent of contracts did not report on ECT/IP Plans;
- two agencies out of seven reported on ECT and IP Plans: SA Water (for 15 per cent of contracts) and DEW (for 100 per cent of contracts); and

⁹⁰ OIA, 2019. Ready to Tender research presentation, Action Market Research & Hudson Howells:
<https://industryadvocate.sa.gov.au/wp-content/uploads/2019/08/Ready-To-Tender-Research-Presentation.pdf>

- scores were supposed to be recorded out of 15; however, some of the scores found (22, 66, 80, 130, 50/70) suggest that scores have a different denominator. Consequently, the Commission considers those scores not to be comparable.

Table 5.1: Number and value (GST excl.) of contracts reported by agency since 2015 (the values for SES and DCS were hidden as they represented less than 3 contracts per cell)

Agency	No. 2015-16	Value 2015-16 (\$'000)	No. 2016-17	Value 2016-17 (\$'000)	No. 2017-18	Value 2017-18 (\$'000)	No. Jul-Dec 18	Value Jul-Dec 18 (\$'000)	Total No. 2015-19	Total Value 2015-19 (\$'000)
DPTI for DPTI	75	1,356,439	92	297,287	60	735,441	23	192,193	250	2,581,358
DPTI for Education	18	20,861	38	128,259	150	189,955	15	11,210	221	350,286
DPTI for Health	14	229,602	5	26,569	19	47,857	4	1,163	42	305,192
DPTI for others	28	60,693	14	70,902	21	94,625	3	20,711	66	246,930
Total DPTI	135	1,667,595	149	523,017	250	1,067,878	45	225,277	579	3,483,766
SA WATER	726	266,792	780	334,411	837	566,937	632	556,763	2,975	1,724,904
Renewal SA	107	40,776	92	41,389	178	213,261	96	142,999	473	438,424
SA Housing	52	11,719	82	125,150	76	76,680	105	112,500	315	326,049
RTWSA	66	5,184	47	15,636	82	18,891	62	19,799	257	59,510
Forestry	66	8,232	84	19,620	37	5,314	22	3,437	209	36,603
DEW	9	7,111	14	8,593	12	15,880	5	2,913	40	34,497
SES / DCS										
TOTAL	1,164	2,009,724	1,249	1,069,875	1,483	1,967,858	967	1,063,687	4,863	6,111,145

Source: SAPC consolidated database from agencies 2015-18 databases of procurement activities

The database collected by the OIA in 2017-18 does not have entries from Forestry SA. It includes Adelaide Venue Management Corporation, Defence SA, DHS, the Motor Accident Commission and the SACE Board.

The data collected by OIA contains significant differences to the Commission’s data. Some examples are provided below for 2017-18, for all contracts above \$150 000 (excl. GST):

Table 5.2: OIA and SAPC data comparison

Agency	OIA database No. of contracts	OIA database Value of contracts (\$'000)	SAPC database No. of contracts	SAPC database Value of contracts (\$'000)
DPTI	296	1,259,251	250	1,067,878
SA WATER	139	296,417	346	534,541

Source: OIA database and SAPC consolidated data base from agencies 2015-18 databases of procurement activities.

The reasons are not clear at this point, although generally the OIA data collected on ECT and IP Plan scores is of better quality than the data that was provided to the Commission:

- all agencies approached by the OIA reported on ECT and IP Plans with actual scores or exemptions to the SAIPP;
- overall, scores or exemptions to the SAIPP were recorded for 96 per cent of contracts for the period 2017-18 (compared to five per cent in the Commission’s database). This suggests that the process for collecting SAIPP information may be disconnected from procurement information in the public authority;
- 37 per cent of contracts were reported exempt from the use of ECT/IP Plans for the period 2017-18 (1.2 per cent in the Commission’s database); and
- scores were supposed to be recorded out of 15, however some of the scores found (16, 28, 73, 142, 10/10, 15/20, etc.) suggest that scores have a different denominator. Consequently, the Commission considers those scores not to be comparable.

The differences between the data sets will be investigated during the consultation process following publication of this draft report.

5.2.1.1 Impact on the selection of suppliers

In the database consolidated by the Commission, the records relating to ECT and IP Plans scores correlate to the winning bidder. There is no information readily available on the runner up or the other bidders. In the absence of information on other bidders, it is difficult to assess the impact of the SAIPP on the selection of a supplier.

5.2.1.2 Impact on local participation and competition

The type of data collected by agencies on the location of the winning supplier varies considerably (see. Table 5.3).

Table 5.3: Information on supplier location collected by public agencies in 2015-18

Agency	Information recorded centrally	Result
SA Water	Address of the office of the supplier undertaking the work	72% SA, 28% Interstate
DPTI	Based on SPB categories: metropolitan Adelaide, regional South Australia, ANZ, Overseas, considering location of business and location where most of the employment activity will occur	DPTI: 71% metro, 26% region, 3% ANZ
Return to Work SA	Local, Interstate, National, Global	67% SA, 9% Interstate, 15% National, 10% Global
Forestry SA, SA Housing Trust, Renewal SA, DEW	No data	

Source: SAPC consolidated database from agencies 2015-18 databases of procurement activities

The figures received from DPTI (97 per cent of contracts going to South Australian suppliers) are inconsistent with the feedback received from local businesses that many contracts go to interstate suppliers. The figures received from SA Water and Return to Work SA (around 70 per cent of contracts going to South Australian suppliers) are also quite different to DPTI's. The Commission will investigate further the definition used by those agencies to determine the location of a supplier.

The Commission has noted, in a few cases, that the tender assessment is based on a fraction of the total contract value (often corresponding to the managing contractor fee). The Commission will investigate the percentage of contract values that is actually influenced by public authorities (as opposed to the percentage of contract value that is controlled by the managing contractor once contracted by government).

From the entries available (78 per cent of the full database), the location of suppliers has not changed much over time (see Figure 5.1 and Table 5.4).

Figure 5.1: Evolution of the spread of number of contracts per supplier location (for SA Water and RTWSA, regional suppliers have been included in the metropolitan category)

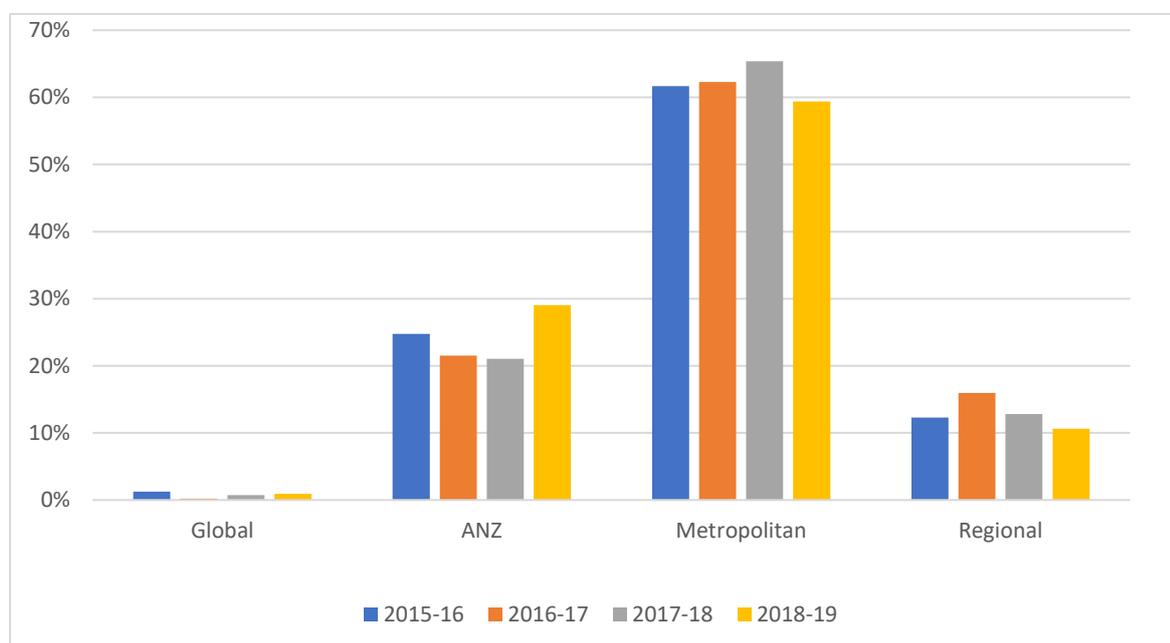


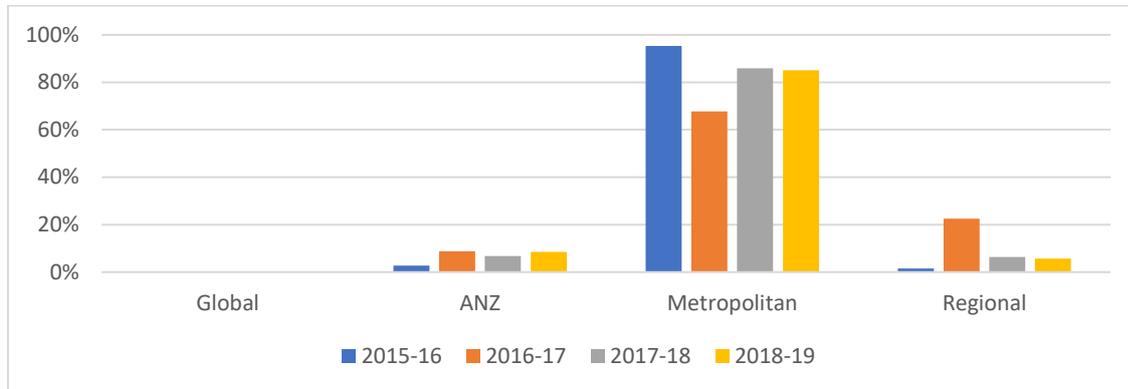
Table 5.4: Location of supplies by year

	Global	ANZ	Metropolitan	Regional
2015-16	1.3%	25.0 %	62.3 %	11.4 %
2016-17	0.2 %	21.8 %	62.8 %	15.1 %
2017-18	0.8 %	21.3%	65.7 %	12.3%
2018-19	0.9 %	29.2 %	59.4 %	10.4 %

Source: SAPC consolidated database from agencies 2015-18 databases of procurement activities

There has been an eight per cent loss of numbers of contracts attributed to South Australian suppliers between 2017-18 and 2018-19, and an equivalent gain of contracts attributed to interstate suppliers. However, this does not translate to a change in the overall value of contracts (see Figure 5.2).

Figure 5.2: Evolution of the value of contracts per supplier location (noting that for SA Water and RTWSA, regional suppliers have been lumped in the metropolitan category)



Source: SAPC consolidated database from agencies 2015-18 databases of procurement activities

In terms of interest from suppliers and competition, the number of quotes received for competitive tenders does increase (see Figure 5.3), in proportion, with the value of the contract.

Figure 5.3 indicates there are a few occurrences, for contracts above \$4 million, where between five and ten quotes were received. For those contracts, the financial and productivity costs of tendering for the unsuccessful bidders can be significant, particularly when multiplied by the number of unsuccessful tenderers. Businesses have indicated repeatedly that a multistage process is more appropriate, as it means that so that only two or three preferred suppliers are exposed to more costly information requests. A few businesses have even suggested that, where the client agency is confident that the preferred supplier can deliver the work, only that supplier should incur significant tender costs (e.g. design).

Figure 5.3: Number of quotes received per value of contracts (2015-18)



Source: SAPC consolidated database from agencies 2015-18 databases of procurement activities

Looking at the average number of quotes that contracts attract over time (see figure 5.4), there has been a reduction in the volume of high value contracts over time. This is either by

design: less quotes requested in order to limit the impact on unsuccessful businesses; or by better assessment, by suppliers, of the value of tendering/chances of winning; or by a lesser pool of competitors. This appears to be a more efficient outcome.

Figure 5.4: Average number of quotes received per contract between 2015–16 and 2018–19



Source: SAPC consolidated database from agencies 2015-18 databases of procurement activities

The topic of efficient tendering was highlighted by Consult Australia in their submission:

...we ask that clients respect and consider the cost imposed on businesses through their approaches. An example of this was a recent Renewal SA tender. The tender required a detailed response, to which 20 responses were received. In this scenario, the option of shortlisting prior to requesting a detailed response would have had the potential to help save time and costs to both client and industry.

For those contracts valued less than \$220 000 the average number of quotes received has more than doubled over the last four years, indicating a higher level of competition in that value category.

The evolution of labour hours committed to South Australia would also provide a good indication of the impact of the SAIPP if this information were available. The Office of the Industry Advocate has advised the Commission that it is presently undertaking a project to recover historic data from physical files and will update the Commission when it is available.

5.2.2 From the random sample of 106 tenders

As noted in the Stage 1 report on the procurement of goods and services, the Commission’s task of evaluating the SAIPP for the procurement of construction work is complicated by the absence of appropriate system-wide data.

Purchase recommendations provide detailed information on the tendering process and the technical aspect of selecting a supplier over others. They also include the detailed evaluation and scoring of ECT and IP Plans.

5.2.2.1 Method

In order to access detailed information about the implementation of the SAIPP, the Commission asked 12 government agencies and four PPAs (on the basis of their capital project spend) for a random sample of their tender assessments of competitive tenders covering construction projects above \$150 000 (GST excl.) that were executed since January 2018 (when the *Industry Participation Act 2017* came into operation). A larger sample was asked of DPTI in order to represent both the civil projects undertaken by DPTI on its own account and the construction projects delivered by DPTI on behalf of other agencies.

Out of the 12 government agencies, ten had executed less than five construction contracts in 2018, as they conduct most or all their construction projects through DPTI. Therefore, only two agencies were in a position to provide the Commission with more than five tender evaluations.

All four relevant PPAs were able to participate in this project.

The final sample obtained consists of 106 tenders from the six public authorities with the largest expenditure on construction procurement, comprising two government agencies and four PPAs (see Table 5.5).

Providing this information was, for some agencies, a significant task. Their cooperation in providing this information is greatly appreciated.

Table 5.5: Overview of sample of tenders requested and received by SAPC

	Asked	Received	Reason	Single quote	Final number
DPTI (for DPTI)	10	14		1	13
DPTI (on behalf of others)	30	31		1	30
DEW	10	10		1	9
SAFECOM	10	0	Too few		
DCS	10	0	Too few		
Health	10	0	Through DPTI		
Education	10	0	Through DPTI		
DPC	10	0	Through DPTI		
AGD	10	0	Through DPTI		
CAA	10	0	Through DPTI		
SAPOL	10	0	Through DPTI		
DCP	10	0	Through DPTI		
DTF (for PPP)	10	0	None in 2018		
SA Water					
	15	18		0	18
Housing					
	15	17		1	16
Renewal					
	15	15		1	14
AVM					
	15	8	All contracts	2	6
TOTAL	210	113		7	106

Source: SAPC consolidated database from agencies 2015-18 databases of procurement activities

5.2.2.2 Results

Representativeness of the sample

The sample covers \$770 million of construction procurement purchases.

The share of contracts between PPAs and public authorities is about 50/50, both in number and value. DPTI’s contribution to these figures is for:

- DPTI’s own construction procurement expenditure (mostly civil work), corresponding to \$364 million (compared to about \$735 million contracted in 2017-18); and
- DPTI’s work as agent for other departments’ building projects, corresponding to \$24 million (compared to about \$332 million contracted in 2017-18).

In terms of value of contracts, there is a good representation of low, medium and high value contracts (see Table 5.6).

Table 5.6: Distribution of sample of tenders by value range

Value of contract	%
below \$220k	22%
\$220k-\$4m	57%
above \$4m	21%

Source: SAPC 106 random tenders

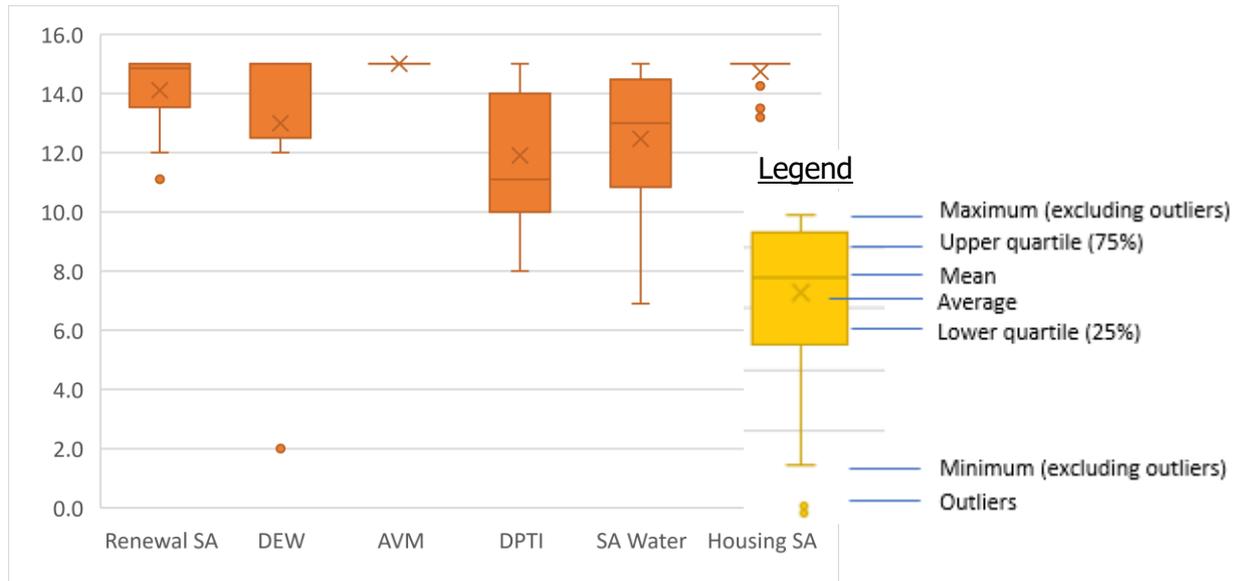
For most agencies, the sample represents 30 per cent to 90 per cent of the value of contracts undertaken by them. It is noted that, for the projects undertaken by DPTI on behalf of other public authorities, the sample covers mostly construction services (lead Professional Services Contractor and cost managers), which represents just over 5 per cent of the value of contracts undertaken. The full value of those contracts is, of course, much larger (\$332 million). Apart for this category, the Commission is satisfied with the size and quality of the sample obtained.

Several administrative errors were identified while going through the sample. For example, ECT or IP Plan scores incorrectly reported from the scoring sheet to the evaluation matrix in seven per cent cases. The Commission corrected errors when they were detected.

Impact on selection of a supplier

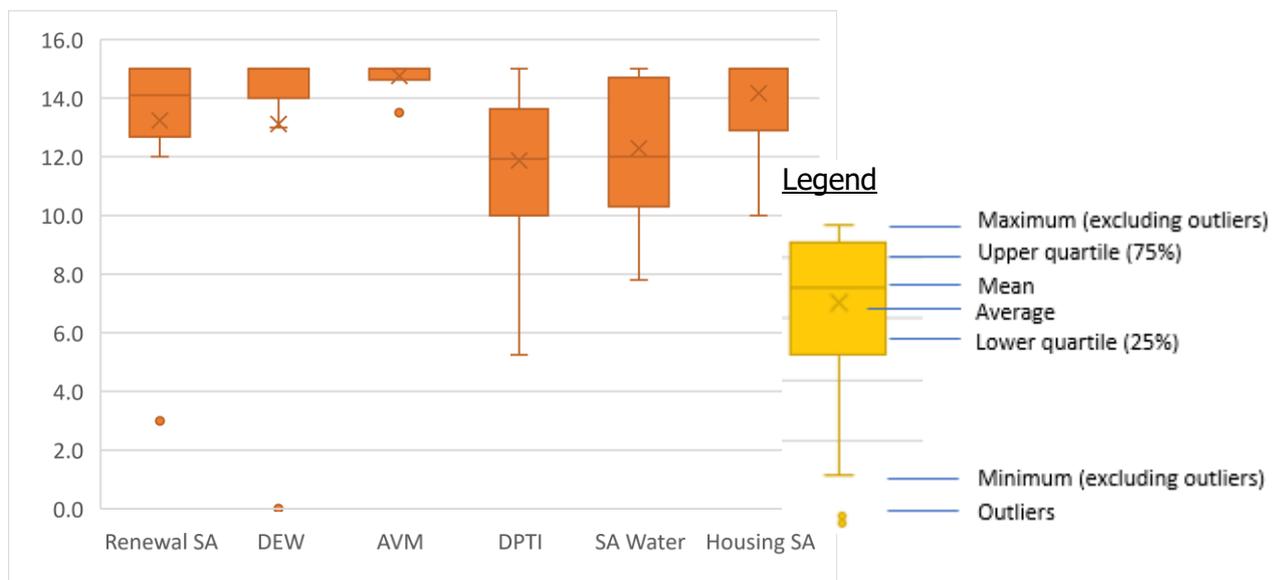
In 78 per cent of cases, the difference in ECT or IP Plan scores between the winner and runner up was less than two points (out of 15). 45 per cent of tenders had identical scores for winners and runners-up (see Figure 5.5.a and 5.5.b).

Figure 5.5.a: Distribution of ECT/IP Plan scores of the winner by agency



Source: SAPC 106 random tenders

Figure 5.5.b: Distribution of ECT/IP Plan scores of the runner-up by agency



Source: SAPC 106 random tenders

Figure 5.5.a and 5.5.b also show that scores are in general very high in the construction field, with little variability (as opposed to the procurement of goods and services). This is consistent with the comments from stakeholders that businesses seriously consider the SAIPP scoring.

In two tenders of the sample, the ECT or IP Plan scores changed the outcome and resulted in the highest scored suppliers winning the tender in one case and being placed on a panel in the other.

It should be noted that, for a further 40 per cent of cases (see Table 5.7), if the ECT or IP Plan score had been different between the winner and the runner-up, then that, in itself, would have been sufficient to affect a change in the outcome of the tender.

Table 5.7: Tenders for which a difference in ECT or IP Plan scores would have changed the outcome

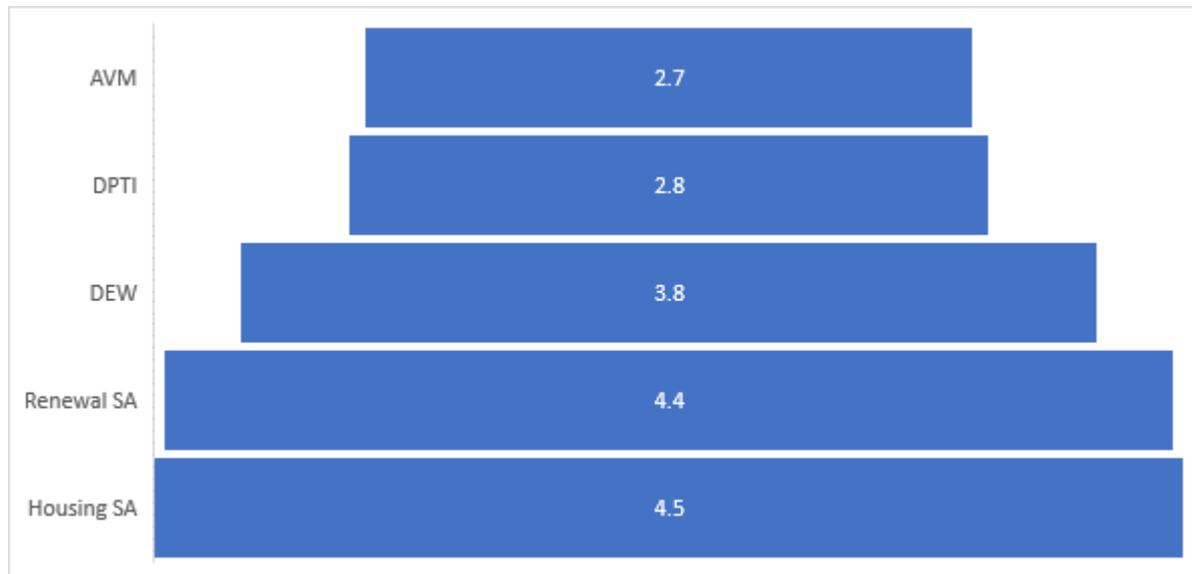
Agency	Number of contracts	Percentage of contracts
AVMC	4	67%
DPTI	18	47%
Housing SA	10	67%
Renewal SA	2	15%
SA Water	4	27%

Source: SAPC 106 random tender evaluations

Impact on competition

The average number of quotes received per agency, for open tenders, vary between agencies (see figure 5.6).

Figure 5.6: Average number of bids received per agency for open tenders



Source: SAPC 106 random tender evaluations

On the whole, they indicate that there are competitive pressures at play.

Impact on local jobs

In order to obtain additional information from Stage 1, the Commission in Stage 2 recorded the number of labour hours that tenderers committed to in their bid. Unfortunately, this data is hard to use for analytical purposes. In a majority of cases, the number of total labour hours for a tender varies significantly between bidders (up to five times the number of hours

for the exact same job or task: e.g. bidder 1, ECT score of 15, labour hours in SA: 7,500 hours – bidder 2, ECT score of 15, labour hours in SA: 1,600 hours. The ECT or IP Plan score measures the percentage of total labour hours committed in South Australia. In many circumstances, the bidder that had a higher score had a lower number of labour hours committed to South Australia, but a higher percentage (e.g. bidder 1, ECT score of 13.5, labour hours in SA: 850 hours – bidder 2, ECT score of 12.8, labour hours in SA: 3000 hours). This matter will be raised with public authorities in progressing the final report.

On average, bidders commit to 96 per cent of local labour, with no distinction between the winner and the runner up.

Out of \$127,142,614 contracted value, 593,769 hours of labour were committed to South Australia, and the average standardised ECT/IP Plan score was 13.7 out of 15.

5.3 Issues raised regarding the SAIPP

Few comments have been made in writing to the Commission about the SAIPP during Stage 2 of the inquiry, however the topic has been raised several times through direct consultation, hence the relatively low level of submission references in this section.

5.3.1 Scoring

A few individual businesses have reported low ECT scores despite being South Australian and using 100 per cent South Australian suppliers. The lack of transparency of the scoring system makes it difficult for businesses to understand where their effort has the most impact.

Stakeholders have also reported the absence of consideration given to the back-office expenditure of local firms in the scoring of ECT or IP Plans: those expenses (general administration, accounting, communication, legal advice, accommodation, consumables, top executives salaries etc) directly contribute to the South Australian economy but are not currently considered in the scoring methodology.

Public authorities have also reported a number of cases where the ECT or IP Plans returned an unusual score, triggering a review, and subsequent change of the score. This suggests that market knowledge within public authorities is very important to verify the scoring, therefore ensuring that SAIPP achieves the correct outcome. This also suggests that the current scoring is subject to different interpretation by the tenderer.

By going through hundreds of ECT and IP Plans, the Commission noticed a few elements of the scoring methodology that do not seem to appropriately reflect the effort committed to by a supplier:

- for employment of Apprentices and Trainees, investment in R&D and Intellectual Property and Aboriginal participation, the questions only ask for a 'yes/no' response;
- for investment in plant, equipment, office and warehousing, amortisation can be considered. It is likely that many businesses don't know this and miss out on scoring points;

- for labour and sourcing, the reference to an economic benefit descriptor (very strong, strong, positive etc) is not straightforward. A matrix is provided for the assessment however it could be made simpler by self-calculating out of the information filled in by the tenderer; and
- 'physical presence in South Australia' is asked (tick the box between head office, branch, warehouse and other), however it is not taken into account in the scoring.

The scoring could better reflect the investment of the supplier in those categories, noting it could make the IPP more complex to score and it would change the formula again, making it difficult to compare scores over time. The Commission also suggests the capacity of interstate and national businesses to include SA businesses in their business supply chains is a potentially important benefit to the State and could be included in the ECT and IPP model.

Information request 5.1

The Commission seek views, evidence and advice on the current scoring of ECT and IP Plans in relation to construction projects regarding how it could better reflect the economic contribution made by suppliers to South Australia, including strengthening South Australian businesses by including them in the value chain of interstate and national businesses and the contribution of services providers.

5.3.2 Weighting and thresholds

A few businesses indicated that applying thresholds for indigenous employment or regional development requirements, based on construction value, is not the best way to meet these objectives. The requirement for quotas of employment for indigenous persons is also seen as very difficult by some stakeholders, who advised it is not always possible to reach those quotas, despite considerable efforts. The fines that apply when plan commitments are not met are seen as unhelpful.

Public authorities' views on the ECT threshold varied, going from supportive to the view that the \$33 000 ECT threshold is too low, does not impact outcomes, creates red tape for low value contracts and should be increased to \$220 000 or \$550 000. The difference comes from the market approach chosen by those authorities: where the strategy is to source work locally, the impact of SAIPP is not seen. Where the work is highly specialised and requires going out of South Australia for solution, the SAIPP is seen as an impediment.

In Stage 1, the Government supported the Commission's recommendation to lift the minimum threshold for which ECT is required to \$550 000 (GST inclusive), and that agencies will determine whether to integrate ECT requirements into their assessment criteria for tenders between \$220 000 and \$550 000 (GST inclusive). The Government's response indicates this measure will be implemented by 31 October 2019.⁹¹

⁹¹ SA Government's response to the SAPC inquiry into government procurement – Stage 1: https://dpc.sa.gov.au/data/assets/pdf_file/0009/109845/SAGov-Response-Procurement-Inquiry-2019.pdf

5.3.2.1 Impact of tender evaluation formulas on the actual weighting of ECT/IP Plans scores

From the 106 random tenders collected by the Commission, in 16 cases the formula used to score the tenderers might be distorting the weightings. A couple of examples are provided below:

- Price had a 70 per cent weight, non-price criteria had a 30 per cent weight, IP Plan score had a 20 per cent weight, adding to 120 per cent and therefore diluting the actual weight of each factor. In this case the actual weight was 16.7 per cent (20/120).
- Formula was: $(IP\ Plan\ weight \times (1 - IP\ Plan\ score / Max\ IP\ Plan\ score) \times price + price) \times (price\ weight + non\ price\ weight \times highest\ weighted\ score / non\ price\ weighted\ score)$. In this formula, it is not easily to determine if the IP Plan has maintained its original weighting.

For the SAIPP to realise its objectives, the Commission considers that the formula used by agencies to score the different criteria should maintain the integrity of the weightings identified for each criterion.

5.3.3 Compliance

5.3.3.1 Participants' views

Stakeholders consider oversight at contract management level is inadequate and can compromise the objectives of SAIPP:

Non-compliance on capital works projects tends to be the result of product or system substitution. In contracts where the construction contractor is responsible for delivery within strict time and cost parameters but is permitted to achieve these parameters by reviewing construction methodology and materials selections without oversight by the client. (AIA submission).

5.3.3.2 SAPC's views

The OIA data on compliance has not yet been released. The Commission will give further consideration to the compliance of suppliers with their industry participation plan when that information becomes available, assuming it is available in sufficient time.

That said, the Commission sample provides useful information. From the 106 random tenders, 95 per cent of the tender evaluations reported the ECT or IP Plan scores for the winning bid, with 90 per cent reporting the ECT or IP Plan scores for the runner up. The Commission concludes there is a high level of compliance with SAIPP in the construction industry. This finding indicates a higher level of compliance for construction than for goods and services procurement (77 per cent) in Stage 1.

For contracts under \$220,000 (the threshold under which agencies are not required to give a minimum weighting of 15 per cent to the ECT score), all agencies applied the 15 per cent weighting. This suggests that SAIPP is incorporated well in the tender evaluation process.

However, from the viewpoint of reporting and performance analysis, much improvement is needed in the way public authorities record the ECT/IP Plan scores in their central database (e.g. providing a score rather than a comment, recording the denominator or using a common denominator, systematically recording ECT/IP Plan scores).

5.3.4 Administrative cost

Business stakeholders report that the administration associated with the SAIPP does add some cost (scoring for tender and reporting during contracts). They also state that frequent changes to procurement policies (including the SAIPP) are frustrating and time consuming to stay on top of, which is particularly difficult for SMEs.

5.3.5 Delays

Some agencies indicated that the scoring of IP Plans, or the involvement of OIA in the market approach, sometimes delayed the tender evaluation process. In those cases, there was no added value from that process.

5.4. How to include broader impact (regional considerations, innovation, productivity, competition)

5.4.1 Participants' views

5.4.1.1 More focus on disadvantaged groups

Stakeholders have reported that broad social goals (support for disadvantaged groups like aboriginal employment) are important and need to remain an objective of the procurement process. Stakeholders also submit that the policy needs to ensure that it supports those local businesses that are capable, competitive in the market, and sustainable.

5.4.1.2 More focus on training of local suppliers

It was commonly expressed in meetings with SMEs and in submissions that more needs to be done in the ECT and IP Plan to encourage upskilling of local businesses by the bigger interstate or overseas businesses winning contracts in South Australia:

Economic contribution in relation to consultancy tenders should capture the level of professional engagement and development provided to South Australian practitioners as well as the number of local practitioners involved in the team. South Australian consultants should have the opportunity to learn new skills and develop expertise through partnerships with interstate or overseas practitioners where this is deemed necessary. This will enable South Australian practice to build capacity and to retain experienced staff in South Australia. (AIA submission).

5.4.1.3 More focus on consultancy services

The Australian Institute of Architects (AIA) indicated in their submissions that 'SAIPP in the construction sector are currently focused on procurement of goods and contractor services'. They would like to see '...an increased application of IPP to procurement of consultancy services'.

5.4.1.4 More focus on graduates

Consult Australia indicates in their submission that *'at present contracts over \$50 million do not include the further nominated groups of a) Cadets, or b) Graduates...'*, even though the SAIPP nominates those groups. Also, under \$50 million, there is no *'...incentive for the Head Contractor and Subcontractors to engage tertiary qualified graduates... to allow the internal permanent transfer of highly experienced and skilled professionals from other Australian states or international offices to live and work in SA'*, and there is no support for *'...innovation programs that bring and retain national and international knowledge to SA on significant infrastructure programs or projects'*.

5.4.1.5 Higher impact in large tender

Stakeholders reported that broad government objectives are easier to implement for large projects and can have very large beneficial impacts when the objectives are clear, and the project is led by the client public authority. Some successful examples have been quoted, like the skills program during the build of the Women's prison and the North Hub for aboriginal and displaced automotive workers participation in the Northern Connector project.

5.5. Summary and conclusions

The Commission's analysis of the use of the SAIPP and ECT by the PPAs broadly confirms the conclusions in stage 1 relating to procurement of goods and services. The South Australian Government has accepted the Commission's recommendations on those matters.⁹²

The Commission's further findings on the SAIPP relating to construction and PPAs are:

- There are clear deficiencies in the information recorded by agencies regarding their application of the SAIPP, and in some cases, some deficiencies in practice, particularly the weighting. The Commission notes the OIA has work in progress that has the capacity to at least partially address these issues through better information and exercising the Industry Advocate's authority to seek improvement
- The SAIPP appears to be well-established in tendering for the State's construction work and for PPAs, notwithstanding the inconsistencies in application (refer section 5.3.3.2). . It is not surprising from that perspective that stakeholders observe that it does not make a difference in selection given the apparent fact that the ECT/IP Plan scores appear to rarely have made the difference between the winning bid and runner up. The Commission also notes in some cases the expectations by business of the policy do not reflect national and international agreements that bind all participating parties on matters of industry preference and local content
- There is a case for reconsidering the ECT and IP Plan scoring in light of comments made by stakeholders regarding the treatment of construction professionals and consulting groups (such as architects)

⁹² SA Government's response to the SAPC inquiry into government procurement – Stage 1: https://dpc.sa.gov.au/_data/assets/pdf_file/0009/109845/SAGov-Response-Procurement-Inquiry-2019.pdf

- There is also a lack of consistency, between bidders, of the absolute numbers of employment for a particular project
- In addition, the Commission considers the policy should also give consideration to the recognising or including the value generated to local businesses who form part of the supply chains of interstate and national businesses as part of the economic benefit to South Australia. This is a further extension of the Commission's view that SAIPP has a role to play in increasing the numbers of match fit businesses in the state.

As noted at various points in this chapter, that the Commission will complete its analysis of the information it has assembled and will follow up with agencies on some apparent anomalies with respect to the SAIPP.

6. A better system architecture

The Government's response to the Final Report for Stage 1 of this inquiry accepted 28 of the Commission's 30 recommendations in full and accepted the remaining two in part. As a whole, the recommendations called for:

- a strategic plan for raising the capability of the South Australian Government's procurement professionals;
- reforming the reporting requirements for government authorities to central procurement to provide the metrics for understanding and analysing whole-of-government procurement;
- streamlining procurement, including adopting the principle that generally procurement decisions should only be authorised once; and
- actions for improving contract management, increasing knowledge of the marketplace, and providing clearer guidance in key areas such as achieving value for money.

From this starting point and incorporating the Commission's assessment of the procurement system's current architecture, this Chapter sets out three options for architecture that, in the Commission's view, would enable government to better drive a whole-of-government procurement system with authority, accountability and human resources.

The Chapter is organised as follows:

- Section 6.1 summarises the Commission's assessment of the current arrangements for procurement;
- Section 6.2 proposes principles for a better architecture;
- Section 6.3 sets out three options for further development and provides an initial assessment of each option;
- Section 6.4 sets out the Commission's view on incorporating government procurement of construction, goods and services and prescribed public authorities; and
- Section 6.5 provides an initial view of implementation issues.

6.1 The current architecture

In the Commission's view, while South Australia's current procurement arrangements are reasonably well managed given their systems, data and capability limitations, the state could do significantly better. A more fit-for-purpose system architecture is needed to hunt more value from its procurement spend, including achieving the state government's non-economic objectives.

The realised benefits can contribute to:

- savings to be deployed to other purposes including health, education or debt reduction;

- better achieving the State's non-financial objectives that are judged to be relevant to procurement, including skilling, indigenous employment and environmental objectives;
- cutting red tape burdens on businesses and not-for-profits; and
- closing the gap between the best or very good Australian performance and that of South Australia

The Commission does acknowledge that there are some areas of very good procurement practice marked by a strategic use of the procurement function, sufficient resources of qualified professionals, effective monitoring of contracts, organisation around market segments and a clear expectation of the financial savings to be achieved (in addition to meeting non-economic objectives). That said, and having now considered construction procurement and prescribed public authorities in addition to goods and services procurement in Stage 1, the Commission considers the existing whole of government architecture (the combination of structure and organisation) for South Australian government procurement is inadequate. The Commission's specific concerns include that the State's procurement function is fragmented into several streams that have limited relationship with each other, lacks a consistent set of principles, pays insufficient attention to human capability, and has a framework of thresholds for goods and services and construction that have not been recently reviewed or challenged.

Box 6.1 Fragmented Architecture

As summarised previously, South Australia has three separate procurement streams which are: public authorities subject to the *State Procurement Act 2004*; construction expenditure over \$150 000 which is managed by DPTI; and public authorities that are prescribed through regulations under the *State Procurement Act 2004* (the prescription effectively exempts the public authorities from the requirements of the SP Act as well as PC028). It is also worth noting that the prescribed public authorities all operate independently. By allowing procurement to be managed by varying methods across government, the State's purchasing power is diluted and there is little opportunity to determine if it is possible to extract additional benefits from its procurement spend as access to whole of system data is difficult and there is little capacity to analyse the data if it was collected. [need some brief stats on the number of people working in the central procurement unit].

Moreover, at a whole of government level, the current architecture

- lacks focus on, and the energy to drive for, whole of system benefits;
- suffers from poor availability of data to monitor and improve whole of system performance; and
- has limited capability to manage procurement strategically.

The lack of focus on whole of system goals and benefits cannot be emphasized enough. Government agencies and their chief executives are focused on their agency's key goals and while those goals generally support the government's overall objectives, they do not always focus on broader government goals like sustainable development unless they are directly relevant to the agency function and its goals. The silo focus of the public authority can lead to missed opportunities to progress broader government goals.

For example, in Victoria, an emphasis was placed on increasing the social benefits associated with procurement of professional services with an emphasis on increasing the indirect community benefits generated through the procurement process. As an example, law firms were asked to report on the number of pro-bono hours they provided within the State. This encouraged law firms to increase the number of pro-bono hours the firms supported throughout the year and, given the level of competition for government tenders, there was no noticeable impact on the price of those services. The size of the government's procurement spend and its impact on the state economy has the moral suasion to influence private firms behaviours to support the government's broader objectives. However, it needs to manage that spend in a strategic manner that aligns with the State's broader goals.

Box 6.2 Inadequate System-level Data

Stage 2 of the procurement inquiry has confirmed the finding of Stage 1 that there is a lack of useable data available to support strategic management of the state's procurement spend or even that of most agencies. The data requested from the prescribed public authorities and DPTI took an extended amount of time and effort for most agencies to extract. Further, the data provided to the Commission had a number of limitations and took a significant amount of time to assemble and organise into a useable format. The limitations related to the different types of data collected and the consistency in recording the data that was collected (this is discussed in more detail in chapter 4). With a few exceptions, it seems quite clear that the data is not regularly used as a strategic management tool but is probably viewed as an administrative task.

In the Commission's view, having regard to the evidence from public authorities and consultations with business stakeholders and public authorities, there is good reason to believe that significant value is being eroded in the stages of:

- managing the procurement spend strategically;
- developing the right definition of the procurement requirement;
- utilising the right approach to market; and
- contract management.

In short, overall the current system unnecessarily leaks value, notwithstanding some pockets of generally good practice.

Consequently, the Commission considers that South Australia will benefit from better system architecture to focus and energise efforts across the state's procurement to:

- realise value at all stages; and
- implement evidence and data-based strategic improvements to the State's procurement system.

Box 6.3 Lack of Strategic Capability

There are two aspects to this issue. First, there is no single procurement framework. There are two large systems (public authorities and construction) and several big and small prescribed public authorities that are currently managed independently. While there are some sound reasons for organising the expenditure and skilled resources into different streams, in the Commission's view, this separation limits the capacity for some cross-cutting benefits such as a common set of procurement principles or optimising the value from a supplier that serves prescribed public authorities, construction and goods and services.

The State Procurement Board oversees procurement for public authorities covered by the SP Act and provides a point of accountability for those public authorities, but as indicated in the Stage 1 report, its focus is largely on compliance and process. DPTI manages construction expenditure in accordance with the PIP policy which was approved by Cabinet, but there is no external reporting on the performance of its procurement activities or the value generated by its spend. The individual prescribed public authorities have their own governance arrangements, but again there is no external reporting on outcomes and with one exception, there does not seem to be a strong focus on procurement as a strategic management tool.

Second, there is currently very limited capacity in the State to manage procurement centrally. The number of procurement professionals with suitable experience and qualifications compared to the total spend is very low and is being eroded as agencies address savings targets. This is reflected in the common concern from businesses that there are few qualified personnel available to interact with during the tender process. Most agencies also indicate that it is difficult to recruit and retain suitable professionals. At present, even if existing resources were combined and empowered, it would be difficult to progress a strategic management agenda.

In the Commission's view, having regard to the evidence from agencies and consultations, a key need is a much stronger central procurement group to drive whole of government procurement based on five foundational elements:

- sufficient seniority, accountability and authority for the function to shape and implement reforms and improvements to the procurement system over several years. Importantly, this includes the capacity to engage with authority at the highest levels of agencies;
- whole-of-government performance monitoring and data analytics, underpinned by robust and relevant whole-of-government performance information;

- the capability to undertake strategic analysis, and exercise professional judgement in identifying and pursuing whole-of-government improvement initiatives authorised by the government;
- assistance to agencies, notably those for whom procurement may not be a mainstream part of their role; and
- capability development for the government's procurement professional cadre.

This would affect the current accountability framework for Chief Executives in respect of procurement in the agencies, which would need to be amended to reflect the emphasis of procurement as strategic management function and whole of government objectives.

A move in this direction is consistent with other states which have focused on improving data collection, developing analytic tools for analysing procurement data and developing capability frameworks for procurement functions and personnel. The primary aim is to extract the maximum value for the total procurement spend. The most common vehicle to achieve that goal is a single broad-based framework that is governed by principles, good practice and holding chief executives accountable for maximising the value of each agency's procurement task.

Central procurement functions in other states also facilitate the performance of agencies in part by improving the data collection process and providing analytic tools for better spend analytics.

6.2 Principles for better system architecture

The Commission notes there are several considerations in identifying options for a more fit-for-purpose central procurement body. It proposes five principles at this point. In addition, there are very practical considerations of implementation. An initial view of them is provided in Section 6.5.

The Commission is guided by the overriding consideration that 'form follows function', that is the design needs to be fit-for-purpose in enabling the central procurement body to do the work mentioned above.

The principles comprise:

- optimising value;
- simplicity;
- appropriately devolved accountability;
- clear authority; and
- capability.

6.2.1.1 Optimising value

The system should aim to deliver increasing value from government procurement, year by year. To do that, it needs the capacity to identify and assess opportunities across government. This requires the acquisition of data and the development of tools to assess

opportunities. It also involves the capacity and authority to progress and obtain approvals for these proposals.

Further, given the size of the procurement spend and its impact on the state’s economy, it is important that the aggregate spend align with the state’s goals to grow the economy and address other non-economic goals.

The overriding principle for evaluating tenders for the provision of goods and services to government should be value for money. However, the application of this concept is not currently well defined, and the Stage 1 report suggested that better guidance needed to be available to ensure that staff understand how to apply value to money in the procurement process. This is particularly relevant for the non-monetary aspect of value for money.

Part of optimising value might include a whole of government category management data base and spend analytic tools that are available to all public authorities as well as the central secretariat.

The Commission sees merit in establishing a benefit target for the State’s procurement spend. This will clarify the intent of the reforms, focus the pursuit of value and maintain discipline in the system. The most common target seems to be 5% of total spend based on the Commission’s review of existing literature and practice in other jurisdictions. It is also used to monitor benefits in parts of the South Australian government.

The following example on developing and setting targets for deriving benefits from procurement spending is provided by SA Water. It shows how SA Water tracks and measures the benefits resulting from managing its procurement spend in a strategic manner. As is evident from the Table 6.1, SA Water believes it has exceeded the notional 5% benefit target in each year.

Table 6.1: SA Water procurement benefits as a percentage of total procurement spend

Financial year	Total benefits \$m	Purchasing result benefits \$m	Purchasing performance benefits \$m	Total spend \$m	Benefits on total spend %
2015/16	\$32.36m	\$18.45m	\$13.91m	\$378.66m	8.55%
	\$26.36m	\$10.34m	\$16.02m	\$409.11m	6.44%
2017/18	\$86.04m	\$54.57m	\$31.47m	\$544.15m	15.81%
	\$83.28m	\$59.91m	\$23.43m	\$745.94m	11.17%

Source: SA Water

The benefit target is more encompassing than hard dollar savings and can be thought of in three categories.

- **financial savings** which should be defined as a reduction in spend or cost from experience;
- **cost avoidance** which is the reduction from the expected cost of that good or service in the future; and

- **additional benefit** which is the additional benefit not planned for but delivered as part of the contract.

6.2.1.2 Simplicity

It is important that the final design of the procurement framework eliminate unnecessary processes, checking, and shared accountability which reduces focus and breeds unnecessary red tape. The Commission acknowledges that public authorities are responsible for the prudent expenditure of public funds and, as such, it is necessary that the framework have some safeguards to ensure that public funds are used in an effective and efficient manner, but it is also important that each step of the process add value.

An overly complex system discourages participants from maximising the value of the State's procurement spend and will encourage them to focus on process rather than outcomes. This is one of the issues in the current procurement regime with low thresholds and multiple approval points. The initial focus should be on making the procurement decision that delivers best value. Once that decision is made, each check point should be a constructive step toward delivering the result that adds value to the process.

A simpler system will encourage procurement professionals to utilise their judgement and expertise to maximise the value of the procurement spend rather than making sure all aspects of the process are covered.

6.2.1.3 Appropriately devolved accountability

While there may be some theoretical benefit to controlling the system centrally, the Commission does not believe it is practical to manage the entire government procurement expenditure centrally. South Australia's total annual spend exceeds \$11 billion and is spread across numerous agencies that deliver a range of different goods and services (including construction). To ensure these goods and services are delivered in a timely and effective manner, it is necessary to devolve the responsibility for procuring to the agencies accountable for the spend. Requiring a central group or multiple central groups to approve all procurements will only create bottlenecks that will either unnecessarily slow the process or reduce the focus on achieving better value owing to a lack of time available to evaluate proposals.

The different categories or streams of procurement need to be considered in the design and management of the system. For example, construction is often treated separately in other jurisdictions. The Commission leans towards a unified system based on principles with the flexibility to manage streams of specialisation differently. This would allow the recruitment and training of professionals with the skills necessary to manage different types of procurement while still applying the same basic principles to each category or stream.

With devolved accountability comes performance measurement. The Commission sees merit in strengthening the accountability in public authorities and linking demonstrated excellence to career progression in the procurement profession in the South Australian public sector.

Being accountable also requires reporting on the performance both at the whole of government and public authority levels. This involves setting clear whole of government objectives, targets and measures and reporting against that framework.

6.2.1.4 Clear authority

Appropriately devolved accountability needs to be matched by appropriate authority to act. While it may seem obvious the agency's Minister and Chief Executive are accountable for the organisation's procurement spend, the current system builds in some decision points that dilute the accountability of those positions. As recommended in the Stage 1 report, the principle that the spend is only authorised once should be applied with the focus shifting to the Minister, Chief Executive and public authority being accountable for executing the proposal. The Commission notes the government has accepted the Commission's recommendation on this point. It would be appropriate for this to apply across the board for government procurement.

6.2.1.5 Capability

The people undertaking procurement on behalf of government need to be suitably qualified for the task they are undertaking. An improved system includes a strong, strategic focus on building and recruiting professional capacity across government. This would include developing professional standards for procurement staff, investing in capability development and an active approach to managing talent and external recruitment.

6.3 Three discussion options

This section sets out three options for further development and consultation. They are:

- **Option A - optimising existing architecture** without changing the legislation and role of the State Procurement Board
- **Option B - strengthened State Procurement Board underpinned by an amended State Procurement Act** with legislative underpinning for a centralised, comprehensive role for the SPB. The changes would incorporate the five foundations set out in Section 6.1
- **Option C - Procurement SA** a new body to replace the SPB, with a strong mandate for a centralised, comprehensive role. The changes would incorporate the five foundations set out in Section 6.1.

There are several elements in each option that will require an additional investment to capture the potential value associated with better management of its procurement spend. All three options require an as yet unquantified investment in people and technology.

It is clear from the Commission's research that suitably qualified individuals are in high demand and, as a result, compensation will need to be competitive with market conditions. In addition, given the shortage of suitable qualified procurement staff, the investment will entail contracting in some of these services in the short-run and addressing the supply issues by developing its own staff through suitable training. Investing in staff development will mitigate the current supply shortage over time.

There will need to be an investment in technology that will allow the collection and analysis of procurement data. This does not require an investment in a complex or expensive IT solution. It does require an agreement to collect and categorise data effectively so that it can be consolidated in a central data base that its capable of being used for the required

analysis. As some agencies already have category management systems, it may be possible to adopt or adapt the existing technology to meet the broader government's needs.

6.3.1 Option A: Optimising within current arrangements

In this option, the State Procurement Board in its current form is the central procurement body, without making any change to the State Procurement Act including thresholds and the exclusion of construction spending above \$150 000 (excluding GST) and prescribed authorities.

This arrangement has some limited advantages, including minimal implementation issues and continuity.

A key consideration is whether the government prefers the central procurement body to identify and drive system-level improvement opportunities and whole of system capability or whether it prefers goods and services and construction to be managed as separately. The State Procurement Act in its current form limits the expanded roles of capability development, of whole-of-government performance analysis and improvement to goods and services procurement. It may be possible to expand the SPB remit by regulation or other means, but the Commission has not investigated this point.

This option would require the SPB and its secretariat to lift its contribution from a largely administrative focus to purposefully adding value to and improving the whole of government procurement of goods and services. This would be a significant change requiring the development of a high-performance team.

This work would include dedicating more staff time to procurement and contract management, identifying the procurement related outcomes for executive staff including Chief Executives and advising the Commissioner for Public Service Employment and Ministers on incorporating these elements into performance agreements.

Overall, while this option has the potential to add value, the shortcomings are significant, and it falls short of the potential from adopting the five foundation elements the Commission considers fundamental. In particular, a part-time Board is a weak vehicle for engaging Chief Executives as equals.

It also does not address the issue of simplifying the system from the supplier's perspective. Suppliers would still likely deal with different systems and expectations when submitting tenders to different agencies.

6.3.2 Option B: A strengthened SPB underpinned by a whole-of-government SP Act

This option assumes that the optimisation identified in Option 1 occurs. It also assumes that as many of the performance issues identified in the system as possible are addressed using the existing SPB structure.

The *State Procurement Act 2004* objects and functions are quite broad and could be used to manage a broader procurement system. By changing the SP Regulation 2005, it would be possible to include prescribed authorities and construction expenditure in the SPB governance structure.

The SPB Policy Framework could also be amended to allow public authorities to manage their own procurement by amending the tier system to establish appropriate thresholds and relying on the accreditation process to ensure public authorities are capable.

The composition of the SPB and its secretariat would also need to be addressed. The professional capability and range of skills in the secretariat would need to be lifted and expanded to deliver the outcomes expected of the revitalised Board. Broadening the scope of procurement to include construction and specialised areas, would require a commensurate addition in the SPB of members with the appropriate skills to help set directions and standards for these areas.

Hence, it may be possible to give effect to most of the changes that are required to help the procurement system generate the maximum benefit possible with adjustments to the existing governance arrangement. However, the continued existence of the Board would make the cultural change required more difficult compared with a clean break to a new organisation. A revitalised and refocused Board will carry the baggage of the existing the SPB system which may discourage public authorities from taking greater ownership of their procurement spending and processes.

A further consideration is there are, in the Commission's view, more appropriate organisational forms to drive system improvement than a Board reporting to the Minister and interacting with agency Chief Executives. In particular, a Board is not the best vehicle for the first foundation the Commission considers essential – namely sufficient seniority, accountability and gravitas to shape and implement reforms over time and to engage with authority at the highest levels of agencies. The Commission regards the Board as an unwieldy model for that purpose, and a part-time Board even more so.

The Commission considers Option B is a significantly more capable approach than Option A.

6.3.3 Option C: Create Procurement SA and repeal the SP Act

Option C would eliminate the SPB and the SP Act and create a new central procurement body that the Commission refers to as Procurement SA.

It would be led – full-time – by the equivalent of a Chief Executive and would be established to support and improve the whole of government procurement framework. The Chief Executive would be responsible for developing proposals that maximise the benefits of procurement spending, supporting public authorities in the development and training of staff and ensuring that the overall principles are implemented within public authorities. This last point will require the Chief Executive to engage with other Chief Executives on non-compliance issues and, if necessary, elevate issues that require Ministerial involvement.

This option has all the potential of Option B in terms of whole-of-government improvement.

It would place procurement on an equal footing as other strategic functions of government with its own Minister, Chief Executive and strategic management group. This is a superior arrangement to a part-time Board for engaging with CEs on driving whole of government improvements. This option is also generally be consistent with the direction in most other jurisdictions.

The discontinuous shift from the SP Board to Procurement SA would help address the cultural issues associated with an old system and old name.

The level of resources required in the strategic management group would be very similar to that of the secretariat in option B and would depend on the scope of the roles given to the central procurement body

The development of Option C (and also Option B) would need to consider how to incorporate and manage the Government’s other social, economic objectives and capabilities that play a role in procurement. The most obvious area is the SAIPP, but there are others including social inclusion, sustainable development, apprenticeship, etc.

This is the Commission’s preferred option at this stage.

Table 6.2: Commission’s consideration of the models

	Option A: Optimising existing arrangements	Option B: Developing a single framework using enhanced legislation to create a strong SPB	Option C: Create Procurement SA and repeal the SP Act
Description	Builds on the recommendation identified in the Stage 1 report and focuses on utilising the existing system in a better manner. It assumes the policy framework and its associated processes are maintained. It also assumes no changes to existing regulations	This option assumes that the optimisation identified in Option 1 also occurs. It also assumes that the performance issues identified are addressed using the existing SPB structure by amending its framework and regulations.	This option assumes that the performance issues are addressed through the repeal of the SP Act and the creation of Procurement SA. The proposed changes are the same only it relies on implementation through an executive-led agency rather than by a legislated Board.
Criteria			
Creating value	Would increase the value created by increasing effort and capability but still does not optimise owing to system limitations	Would increase the level of benefits captured through a single system, better data analytics and increased accountability for public authorities	Best potential to maximise value through consistent principles and holding agencies accountable for maximising value
Simplicity	The changes would be minimal but not simple from the perspective of suppliers as there	There would only be one system in place and the number of	There would only be one system in place and the number of

	Option A: Optimising existing arrangements	Option B: Developing a single framework using enhanced legislation to create a strong SPB	Option C: Create Procurement SA and repeal the SP Act
	would still be multiple systems	approvals would decrease.	approvals would decrease
Appropriate devolution	Previous delegations would remain and the incentives for public authorities to manage procurement spending more strategically would not change	Public authorities would be accountable for their own procurement spend. The strengthened SPB would drive system improvements.	Public authorities would be accountable for their own procurement spend. Procurement SA would drive system improvements.
Clear accountability	Does not change the multiple accountabilities in the current system	While the intent is to make agencies accountable for their own procurement spend and the outcomes, the continued existence of the SPB might distract from that process.	There is a new central procurement agency, its new responsibilities would be easier to communicate.
Capacity	Would build some capacity but limited by the multiples systems and differences between agencies	Would build some capacity, but deemphasises the role of agencies	Relies on building capacity in both agencies and the central procurement unit

Source: Office of the SA Productivity Commission

The Commission is looking for feedback and views on issues and merits of these three options. It intends to develop them further (or superior alternatives) in the coming weeks and months.

6.4 Incorporating construction and goods and services

The focus of the options discussed above is the whole of government procurement function. All the options identified above rely on the strengthening of the procurement function in government agencies as well. To increase the benefits generated through procurement spending, the procurement function needs to be treated and developed as a strategic management function. This will require developing agency capacity for those agencies that have a large focus on procurement in the delivery of their public services and developing support for those agencies that do not undertake a significant amount of procurement.

The Commission sees merit in incorporating all the elements of government procurement covered in Parts 1 and 2 of this inquiry – goods and services, construction and the prescribed authorities – within an encompassing procurement framework with common

principles and purpose, including a unifying focus on high professional capability. Within that whole of government framework, the Commission is persuaded that some clear specialisation and streams would be necessary.

Importantly, the Commission considers that construction procurement is a distinct, specialised stream with two subdivisions of engineering and building. The Commission's current views on possible actions to improve construction procurement are set out in Chapter 3, particularly in relation to revising the thresholds and to devolving to agencies from DPTI of accountability for low complexity construction.

In addition, in bringing the current prescribed public authorities within this whole of government framework, the Commission considers it would be essential to define the criteria by which these public authorities would have a separate status. For example, The Commission considers there are unlikely to be any net benefits to imposing additional process, policy and practice requirements on SA Water, which is generally very professionally run, with strong links to the market, a focus on measuring and achieving benefits and a strategic approach to the procurement function amongst other desirable attributes. The Commission also accepts the requirement for agile and swift procurement for prescribed public authorities whose business requires those attributes.

That said, the importance benefit of Options B and C in taking a whole of government focus is that it enables the central procurement function to see, and if necessary, act, across the whole of government.

6.5 Implementation and other issues

The preceding discussion has necessarily been at a high level in order to convey the thrust of the options.

Each option has a range of implementation issues that also depend on other decisions including:

- Costs, including with staged implementation
- The scope of the central procurement unit's functions
- The priority areas for improvement, including the largest agencies in terms of procurement spend
- Locating the procurement talent needed to deliver the central body's mission
- Defining and applying the concept of earned autonomy.

The Commission will explore these matters further and any other material matters raised by stakeholders in the coming weeks to finalise its recommendations.

Appendices

Appendix 1: List of submissions for the Government Procurement Inquiry Stage 1 issues paper

Number	Organisation name
1	<u>Adept Technology</u>
2	<u>Air Conditioning and Mechanical Contractors' Association of SA (AMCASA)</u>
3	<u>Antony Thus</u>
4	<u>Associated Newsagents Co-operative (SA) Ltd</u>
5	<u>Australian Industry Group (AiGroup)</u>
6	<u>Australian Institute of Architects and Association of Consulting Architects</u>
7	<u>Australian Medical Association SA</u>
8	<u>Australian Medical Placements</u>
9	<u>Baptist Care</u>
10	<u>Bus and Coach Association SA</u>
11	<u>Business SA</u>
12	<u>CARA</u>
13	<u>City of Victor Harbor</u>
14	<u>Colin Fullerton</u>
15	<u>Consult Australia</u>
16	<u>COTA SA</u>
17	<u>Department for Industry and Skills</u>
18	<u>Don Dunstan Foundation - includes Attachments 1 to 3</u> <u>Don Dunstan Foundation - includes Attachments 4 to 5</u>
19	<u>Engineers Australia</u>

Number	Organisation name
20	<u>Green Industries SA (GISA)</u>
21	<u>Industry Advocate and Office of the South Australian Chief Entrepreneur</u>
22	<u>Leunig Advisory</u>
23	<u>Life Without Barriers (LWB)</u>
24	<u>Liz Higgins</u>
25	<u>Mark Parnell MLC</u>
26	<u>Mike Ford</u>
27	<u>Motor Trades Association of South Australia (MTA SA)</u>
28	<u>Office of the Industry Advocate</u>
29	<u>Paul Rogers</u>
30	<u>Restaurant and Catering Industry Association</u>
31	<u>Royal Flying Doctor Service (RFDS)</u>
32	<u>Small Business Commissioner South Australia</u>
33	<u>Social Change Headquarters</u>
34	<u>South Australian Council of Social Service (SACOSS)</u>
35	<u>South Australian Council of Social Service - Supplementary</u>
36	<u>South Australian Country Womens Association Association (SACWA)</u>
37	<u>Tindo Solar</u>
38	<u>Uniting Country SA Ltd</u>
39	<u>Uniting Country SA Ltd - Supplementary</u>
40	<u>Volunteering SA & NT</u>
41	<u>Wildcatch Fisheries SA</u>
42	<u>Your Nursing Agency Pty Ltd</u>

Appendix 2: List of submissions for the Government Procurement Inquiry Stage 1 draft report

Number	Organisation name
1	<u>Akina Foundation</u>
2	<u>ANCOL SA</u>
3	<u>Business SA</u>
4	<u>Buyability</u>
5	<u>Community Capacity Builders</u>
6	<u>Office of the Industry Advocate - Submission 1</u>
7	<u>Office of the Industry Advocate - Submission 2</u>
8	<u>Paul Rogers</u>
9	<u>SACOSS</u>
10	<u>Small Business Commissioner</u>
11	<u>Social Change Headquarters</u>
12	<u>Social Traders</u>
13	<u>The Stretton Centre</u>
14	<u>VendorPanel</u>
15	<u>Wicked Lab</u>

Appendix 3: List of submissions for the Government Procurement Inquiry Stage 2 issues paper

Number	Organisation name
1	<u>AIIA.pdf</u>
2	<u>AMCA SA</u>
3	<u>Business SA</u>
4	<u>Consult Australia</u>
5	<u>O'Connors</u>
6	<u>SA Chapter of the Australian Institute of Architects and the Association of Consulting Architects</u>
7	<u>SACES</u>
8	<u>Small Business Commissioner</u>
9	<u>Specialist Contractors SA</u>
10	<u>Top Right Medical</u>