



Dynamic Strategic Sourcing

THE OFFICE OF FEDERAL PROCUREMENT POLICY (OFPP)

issued guidance in May 2005 regarding the importance of implementing strategic sourcing across the federal government. They define strategic sourcing as “the *collaborative* and *structured* process of critically analyzing an organization’s spending and using this information to make business decisions about acquiring commodities and services more effectively and efficiently.”

Strategic sourcing implementation has been sporadic at best, with many agencies still struggling to figure out how to implement it without breaking existing procurement processes. This continues even though the Office of Management and Budget (OMB) has made strategic sourcing a priority. Federal agencies were directed to develop plans and pick three areas for implementation, but the reviews on their efforts so far are mixed. This lack of widespread implementation is due in large part to the enormous workload required, and the significant downside impacts of traditional strategic sourcing methods.

Note that the Office of Federal Procurement Policy (OFPP) does not define strategic sourcing as limiting government purchases to a small number of vendors, but rather the goal is said to be a more effective and efficient form of purchasing. With respect to commercial items an agency buys on a regular basis, conventional wisdom has led agencies to implement a strategic sourcing program by limiting the number of vendors and by offering exclusivity of contract as a means of aggregating volume in return for lower prices. This approach can be optimal for buying high-priced commodities on an agency-wide scale, as has been done by GSA through the SmartBuy program for software purchases, by the U.S. Air Force under its enterprise IT commodity council approach, and by several other agencies. However, this approach requires considerable resources and can often have significant downside effects.

Nevertheless, government efforts to implement strategic sourcing to date have generally taken the approach of selecting one or several large vendors for a given commodity and sending all purchases through those select vendors. While this has usually had the effect of lowering prices in the short term, it remains to be seen whether those agencies will see the long-term benefits they desire. Static captive relationships with vendors over time tend to see prices drift upward as the agency becomes reliant on those vendors, and vendors find new options for enhancing revenue through that contract under a “buy in, get well” approach. Moreover, static contract pricing typically incorporates inflation-based price

increases over time, while the market price for many commodity type items, especially information technology commodities, tends to decrease over time.

The approach described is more of a “limited sourcing” than a strategic sourcing process, since it relies on long-term vendor exclusivity and limitation of customer options to obtain price breaks and other tangible benefits in return for that exclusivity of contract. This has some obvious drawbacks, including bundling implications, which are especially troublesome considering congressional and other mandates to support small and socio-economic businesses. The limited sourcing approach is especially problematic given that the commodities most often chosen for this type of sourcing (e.g., office supplies, IT equipment, etc.) are those where small businesses have enjoyed outstanding success selling to the federal government. The downside impact could easily be a reduction in small businesses sales, and reduced small business goal attainment among federal agencies.

An emerging alternative to limited sourcing arrangements is the use of new or refined purchasing tools to implement commodity purchases under what might be termed “dynamic strategic sourcing.” Dynamic strategic sourcing is a procurement approach that is able to gain significant efficiencies through competitive and other market forces, yet does not require a static relationship with one vendor or a very limited number of vendors. Dynamic strategic sourcing enables agencies to employ tools that bring powerful market forces to bear on each purchase, whether aggregated or not, to drive commodity prices lower while still allowing a large pool of qualified vendors, including many small businesses, to participate. On-line reverse auctioning tools are one method that has demonstrated the types of efficiencies envisioned by OFPP. This dynamic approach has several important benefits, both to the agency using it and to governmentwide procurement in general. One such benefit is that small business is not locked out of the procurement process under dynamic strategic sourcing. With the long-standing government requirement to support small businesses, this is a significant consideration.

Limited sourcing also requires that an agency perform complex analyses of spending patterns and implement complicated logistics plans, usually resulting in either a greater workload for existing personnel or the need for more people to implement the program, which increases agency costs. Dynamic strategic sourcing allows agencies to use established processes to buy from qualified sources, yet they obtain lower prices and other benefits, such as quantity



queuing, which can make purchases at pre-planned quantity levels to gain additional price breaks. Additionally, dynamic strategic sourcing keeps the government buyer continually in charge of the purchasing process, allowing decisions to be made to change direction as agency needs change. Under limited sourcing, the government can be locked into a relationship that limits the flexibility to change direction as necessary. There is also the potential hazard under limited sourcing that agencies will fall into the trap of specifying brand-name products in violation of rules against such a practice.

Among the most powerful tools in the dynamic strategic sourcing arena is the on-line commercial procurement marketplace, where commercially available tools, such as FedBid, can enable government agencies to implement dynamic strategic sourcing with the benefits described earlier. The process is inclusive, available without cost to the Central Contractor Registry (CCR) registered vendors, and prices are driven lower through a dynamic pricing mechanism that is akin to a “reverse eBay” approach, where prices fall as vendors compete to underbid each other. The government applies the normal *FAR* and other regulatory approaches, but uses the on-line marketplace tool to maximize efficiency, competition, and cost-savings, while avoiding potentially costly and problematic limited sourcing issues. A flexible on-line marketplace can also access several governmentwide contracts such as GSA and others, sorting out the best buying approach and the best terms at the lowest cost, which is the essence of dynamic strategic sourcing. The on-line commercial marketplace approach for government purchasing has been endorsed by OFPP, and has gained the attention of House Government Reform Committee Chair Tom Davis. Most importantly, however, the success of this approach at the buyer level is evidenced by the hundreds of millions of dollars worth of procurements that have been made and continue to be made by agencies across the federal government.

In those instances where agencies successfully implement an

agency-wide limited sourcing process, there is also opportunity to gain a second level of advantages by combining it with dynamic strategic sourcing to maintain those discounts that were gained at the first level contract. For instance, an agency blanket purchasing agreement (BPA) could add a dynamic strategic sourcing tool at the purchase level to gain additional advantages, such as keeping the steep discounts in place through continual competitive pressures at the task order level. This is an effective means of reducing the vendor “buy in, get well” approach that can occur under a limited sourcing program.

The growing success of dynamic strategic sourcing for federal government commodity procurements stands in sharp contrast to the results of limited sourcing as the government’s primary means of achieving strategic sourcing results. On one hand, the downside effects of the limited sourcing model, such as requirements to perform extensive analysis, limited government post-award options, the negative impact on small businesses, and other risk factors, have delayed or limited implementation among federal agencies. On the other hand, the dynamic strategic sourcing approach provides agencies with an effective procurement solution since it provides for easy implementation, minimizes requirements to define specific areas of interest, enables continuation of government control over the contracting process, and avoids the negative impact on small businesses, all while maximizing efficiency, competition, and cost savings. **CM**

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