

Direct Source Procurement

Audit Report No.11 2010–11

Opening Statement by Matt Cahill, Group Executive Director ANAO

JCPAA Review 2 March 2011

1. Chair, Members of the Committee, the objective of the *Direct Source Procurement* audit was to assess how well agencies had implemented the Commonwealth Procurement Guidelines (CPGs) and relevant FMA legislation when undertaking Direct Source procurement.
2. By way of context, the Commonwealth Procurement Guidelines (referred to as the CPGs) establish government policy for procurement. The CPGs establish procurement principles that apply to all procurement processes, and promote value for money as the core principle. Applying the procurement principles is a requirement of the CPGs and necessitates a considered approach when establishing arrangements for individual procurements.
3. The CPGs and related Department of Finance and Deregulation (Finance) guidance define three procurement methods: Open Tender, Select Tender and Direct Source procurement. Direct Source procurement is a process by which an agency may invite a potential supplier or suppliers of its choice to make submissions such as quotes or tenders. By its nature, Direct Sourcing is less competitive than Open and Select Tendering as it does not provide the opportunity for all or, in many instances, a number of potential suppliers to compete for the provision of property and services.
4. For covered procurement (generally valued at more than \$80 000), the CPGs require that Direct Sourcing only be undertaken in a limited number of specified

circumstances, such as when an approach to the market has failed. For non-covered procurement, agencies should conduct an appropriately competitive procurement process commensurate with the scale, scope and relative risk of the procurement. In all cases, agencies need to be mindful that it is generally more difficult to adhere to the procurement principles such as value for money, encouraging competition and ethical use of resources when Direct Sourcing, but under the CPGs the onus is on them to do so.

5. Overall, agencies were reasonably familiar with the Government's procurement framework and the CPGs. However, in practice, key elements of the CPGs were not consistently followed across the four audited agencies when choosing and conducting Direct Source procurements. For the majority of Direct Source procurements examined, from the circumstances of the procurement and/or procurement documentation, it was not evident that one or more CPG obligations, requirements or specified sound practices had been met, including for higher valued procurements.
6. The agencies examined had in place policies and guidance to assist agency staff when undertaking procurement. However, the agencies needed to more clearly address Direct Sourcing arrangements, including attaining value for money, encouraging competition in procurement activities and ensuring accountability and transparency of decision making and processes.
7. Agencies also experienced difficulties in distinguishing Direct Sourcing from Select Tendering. In part, this reflected a lack of clarity in Finance's definitions of methods for non-covered procurements; an issue which Finance recognises and had advised it intends to address.

8. To assist the committee, I will draw your attention to some key findings. In particular, the ANAO examined procurements valued between \$10 000 and \$305 million and found that irrespective of the value or type of Direct Source procurements, there was often limited evidence to demonstrate that agencies' practices for individual procurements provided value for money. This does not necessarily mean that value for money was not achieved; rather that, in many cases, procurement practices applied to the particular circumstances, including the supporting documentation, did not engender confidence that value for money requirements of the CPGs were satisfied. The audit also highlighted issues in agencies' application of the other principles set out in the CPGs such as accountability and transparency in procurement decision making.
9. Examination of Direct Source procurements across all four agencies provided evidence that, in 85 per cent of instances, agencies approached only one supplier and either did not seek, or only sought one quote prior to procurement. The practical application of the CPGs can justify Direct Sourcing in certain instances, for example, for simple low cost items where market forces readily determine product price.
10. For complex procurements, there may not be an obvious competitive market. In these cases, where Direct Sourcing can be justified, it is prudent for agencies to obtain a small number of quotes from suppliers with a history of proven performance, and to increase the rigour applied to documenting key procurement decisions and the reasons for those decisions.
11. For higher valued Direct Source procurements, that is covered procurements, the agencies could not consistently assure that their procurements complied with the CPGs. That is, from the circumstances of the procurement and/or procurement documentation, it was not evident that a valid condition for Direct Sourcing had

applied to these covered procurements, as required by the CPGs. When an agency's central procurement unit was involved in decisions to Direct Source covered procurements, this generally had a positive impact on compliance.

12. In general, it is our view that to improve the alignment of agency procurement practices with the requirements of the CPGs, agencies should give more consideration to the procurement need and risk level, how it may be met through an appropriately competitive procurement process (one that has regard to the current procurement market) and be able to clearly demonstrate that these considerations have taken place.
13. Having regard to the underpinning expectations of the CPGs (including that procurement will achieve value for money and promote competition) and the scale of Australian Government procurement, agencies should also strive to better balance the broader benefit of competitive tendering and streamlined procurement practices. Such a balance would see agencies giving greater consideration to the scope of the potential procurement need at the outset of a procurement; more often seeking opportunities to approach the market to enhance the potential to achieve value for money; and adopting more strategic approaches to procurement, such as greater use of panels and other standing offer arrangements. In general, a greater emphasis on earlier planning for procurement activities would improve the procurement outcomes.
14. To assist the committee in its deliberations, with me today I have Stuart Turnbull, the Executive Director, and Tracey Martin, the Audit Manager.