



## Testimony

Before the Committee on Homeland  
Security and Governmental Affairs,  
U.S. Senate

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# STRATEGIC SOURCING

## Improved and Expanded Use Could Provide Significant Procurement Savings

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# GAO Highlights

Highlights of [GAO-13-765T](#), a testimony before the Committee on Homeland Security and Governmental Affairs, U.S. Senate

## Why GAO Did This Study

GAO has reported that the government is not fully leveraging its aggregate buying power. Strategic sourcing, a process that moves an organization away from numerous individual procurements to a broader aggregate approach, has allowed leading companies to achieve savings of 10 percent or more. A savings rate of 10 percent of total federal procurement spending would represent more than \$50 billion annually. While strategic sourcing makes good sense and holds the potential to achieve significant savings, federal agencies have been slow to embrace it, even in a time of great fiscal pressure.

This statement highlights GAO's recent findings related to the use of strategic sourcing across government, best practices leading companies are adopting to increase savings when acquiring services, and recent actions that could facilitate greater use of strategic sourcing. GAO's testimony is based largely on GAO's September 2012 report on strategic sourcing and GAO's April 2013 report on leading practices for acquiring services, as well as other GAO reports on contracting and acquisition.

## What GAO Recommends

GAO is not making any new recommendations in this testimony. GAO has made recommendations to OMB, DOD, VA, and other agencies on key aspects of strategic sourcing and acquisition of products and services in the past. These recommendations addressed such matters as setting goals and establishing metrics. OMB and the agencies concurred with the recommendations, and are in the process of implementing them.

View [GAO-13-765T](#). For more information, contact Cristina Chaplain at (202) 512-4148 or [chaplainc@gao.gov](mailto:chaplainc@gao.gov).

July 15, 2013

## STRATEGIC SOURCING

### Improved and Expanded Use Could Provide Significant Procurement Savings

## What GAO Found

Most of the agencies GAO reviewed for its September 2012 report leveraged a fraction of their buying power. More specifically, in fiscal year 2011, the Departments of Defense (DOD), Homeland Security, Energy, and Veterans Affairs (VA) accounted for 80 percent of the \$537 billion in federal procurement spending, but reported managing about 5 percent of that spending, or \$25.8 billion, through strategic sourcing efforts. Similarly, GAO found that the Federal Strategic Sourcing Initiative had only managed a small amount of spending through its four government-wide strategic sourcing initiatives in fiscal year 2011, although it reported achieving significant savings on those efforts. Further, we found that most selected agencies' efforts did not address their highest spending areas, such as services, which may provide opportunities for significant savings.

Companies' keen analysis of spending is key to their savings, coupled with central management and knowledge sharing about the services they buy. Their analysis of spending patterns comprises two essential variables: the complexity of the service and the number of suppliers for that service. Knowing these variables for any given service, companies tailor their tactics to fit the situation, and do not treat all services the same. Leading companies generally agreed that foundational principles—maintaining spend visibility, centralizing procurement, developing category strategies, focusing on total cost of ownership, and regularly reviewing strategies and tactics—are all important to achieving successful services acquisition outcomes. Taken together, these principles enable companies to better identify and share information on spending and increase market knowledge about suppliers to gain situational awareness of their procurement environment and make more informed contracting decisions. Like the federal government, leading companies have experienced growth in spending on services, and over the last 5 to 7 years have been examining ways to better manage spending. Officials from seven leading companies GAO spoke with reported saving 4 to 15 percent over prior year spending through strategically sourcing the full range of services they buy, including those very similar to what the federal government buys—for example, facilities management, engineering, and information technology.

Agencies have not fully adopted a strategic sourcing approach but some have actions under way. For example, in April 2013, DOD was assessing the need for additional resources to support strategic sourcing efforts, and noted a more focused targeting of top procurement spending categories for supplies, equipment, and services. VA reported that it had taken steps to better measure spending through strategic sourcing contracts and was in the process of reviewing business cases for new strategic sourcing initiatives. In 2012, the Office of Management and Budget (OMB) released a Cross-Agency Priority Goal Statement, which called for agencies to strategically source at least two new products or services in both 2013 and 2014 that yield at least 10 percent savings. In December 2012, OMB further directed agencies to reinforce senior leadership commitment by designating an official responsible for coordinating the agency's strategic sourcing activities. In addition, OMB identified agencies that should take a leadership role on strategic sourcing. OMB directed these agencies to promote strategic sourcing practices inside their agencies by taking actions including collecting data on procurement spending

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Chairman Carper, Ranking Member Coburn, and Members of the Committee:

I am pleased to be here today to testify on the value of strategic sourcing as an important tool to achieve greater savings and efficiencies in government procurements of products and services. Generally speaking, strategic sourcing is a procurement process that seeks to move an organization away from numerous individual procurements to a broader aggregate approach. The tools and techniques that come with strategic sourcing enable organizations to

- develop a better picture of what they are spending on goods and services,
- better understand cost drivers,
- prioritize their requirements,
- better manage suppliers,
- take advantage of market trends, and
- target savings.

Leading companies strategically manage 90 percent of their procurement spending, and report savings of 10 percent or more of total procurement costs. We have previously reported that leaders across the government need to embrace a strategic sourcing approach, and that saving 10 percent of the total federal procurement spending would produce more than \$50 billion in savings annually.<sup>1</sup>

While strategic sourcing inherently makes good sense and holds the potential to achieve significant savings, federal agencies have been slow to embrace it, even in a time of great fiscal pressure. Reasons for this include a lack of leadership commitment within agencies, a desire on the part of agency officials to maintain control over their contracting, a lack of strategic sourcing expertise, data barriers, and perceptions about strategic sourcing that increase the hesitancy to use it, such as a fear that

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<sup>1</sup>GAO, 2013 Annual Report: Actions Needed to Reduce Fragmentation, Overlap, and Duplication and Achieve Other Financial Benefits, [GAO-13-279SP](#) (Washington D.C.: Apr. 9, 2013).

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reporting savings will lead to budget cuts. My testimony today will highlight GAO's recent findings related to the use of strategic sourcing across government, best practices leading companies have been adopting to increase savings when acquiring services, and recent actions that could facilitate greater use of strategic sourcing.

This testimony is based largely on GAO's September 2012 report on strategic sourcing and GAO's April 2013 report on leading practices for acquiring services, as well as other GAO reports on contracting and acquisition.<sup>2</sup> In conducting work on the government side, we spoke with four agencies and analyzed relevant data. On the company side, we visited seven companies and identified key practices. Details of the scope and methodology are available in the September 2012 and April 2013 reports. All work on which this testimony is based was performed in accordance with generally accepted government auditing standards.

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## Background

GAO has been assessing strategic sourcing and the potential value of applying these techniques to federal acquisitions for more than a decade. In 2002, GAO reported that leading companies of that time committed to a strategic approach to acquiring services—a process that moves a company away from numerous individual procurements to a broader aggregate approach—including developing knowledge of how much they were spending on services and taking an enterprise-wide approach to services acquisition.<sup>3</sup> As a result, companies made structural changes with top leadership support, such as establishing commodity managers—responsible for purchasing services within a category—and were better able to leverage their buying power to achieve substantial savings.

Strategic sourcing can encompass a range of tactics for acquiring products and services more effectively and efficiently. In addition to leveraged buying, tactics include managing demand by changing

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<sup>2</sup>GAO, *Strategic Sourcing: Improved and Expanded Use Could Save Billions in Annual Procurement Costs*, [GAO-12-919](#) (Washington, D.C.: Sept. 20, 2012); *Strategic Sourcing: Leading Commercial Practices Can Help Federal Agencies Increase Savings When Acquiring Services*, [GAO-13-417](#) (Washington, D.C.: Apr. 15, 2013); and *Strategic Sourcing: Improved and Expanded Use Could Provide Procurement Savings for Federal Information Technology*, [GAO-13-408T](#) (Washington, D.C.: Feb. 27, 2013).

<sup>3</sup>GAO, *Best Practices: Taking a Strategic Approach Could Improve DOD's Acquisition of Services*, [GAO-02-230](#) (Washington, D.C.: Jan. 18, 2002).

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behavior, achieving efficiencies through standardization of the acquisition process, evaluating total cost of ownership, and better managing supplier relationships. We have particularly emphasized the importance of comprehensive spend analysis for efficient procurement since 2002. Spend analysis provides knowledge about how much is being spent for goods and services, who the buyers are, who the suppliers are, and where the opportunities are to save money and improve performance. Private sector companies are using spend analysis as a foundation for employing a strategic approach to procurement.

We have previously reported that because procurement at federal departments and agencies is generally decentralized, the federal government is not fully leveraging its aggregate buying power to obtain the most advantageous terms and conditions for its procurements.<sup>4</sup> Agencies act more like many unrelated, medium-sized businesses and often rely on hundreds of separate contracts for many commonly used items, with prices that vary widely. Recognizing the benefits of strategic sourcing, the Office of Management and Budget (OMB) issued a memorandum in 2005 that implemented strategic sourcing practices.<sup>5</sup> Agencies were directed to develop and implement strategic sourcing efforts based on the results of spend analyses.

In addition to individual agency efforts, a government-wide strategic sourcing program—known as the Federal Strategic Sourcing Initiative (FSSI)—was established in 2005. FSSI was created to address government-wide opportunities to strategically source commonly purchased products and services and eliminate duplication of efforts across agencies. The FSSI mission is to encourage agencies to aggregate requirements, streamline processes, and coordinate purchases of like products and services to leverage spending to the maximum extent possible. At the time of our 2012 report, four FSSI efforts were ongoing—focused on office supplies, domestic delivery of packages, telecommunications, and print management—and three were planned

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<sup>4</sup>GAO, *Opportunities to Reduce Potential Duplication in Government Programs, Save Tax Dollars, and Enhance Revenue*, [GAO-11-318SP](#) (Washington, D.C.: Mar. 1, 2011).

<sup>5</sup>OMB, *Memorandum for Chief Acquisition Officers, Chief Financial Officers, and Chief Information Officers, Subject: Implementing Strategic Sourcing* (Washington, D.C.: May 20, 2005).

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related to SmartBUY, Wireless plans and devices, and publication licenses.

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## Expanded Use of Strategic Sourcing Could Save Billions in Federal Procurement Costs

In our September 2012 report, we found that most of the agencies we reviewed leveraged a fraction of their buying power through strategic sourcing. More specifically, in fiscal year 2011, the Department of Defense (DOD), Department of Homeland Security (DHS), Department of Energy, and Department of Veterans Affairs (VA) accounted for 80 percent of the \$537 billion in federal procurement spending, but reported managing about 5 percent of that spending, or \$25.8 billion, through strategic sourcing efforts. Similarly, we found that the FSSI program had only managed a small amount of spending through its four government-wide strategic sourcing initiatives in fiscal year 2011, although it reported achieving significant savings on those efforts. Further, we found that most selected agencies' efforts did not address their highest spending areas, such as services, which provides opportunities for significant savings.

We found that when strategically sourced contracts were used, agencies generally reported achieving savings. For example, selected agencies generally reported savings ranging from 5 percent to over 20 percent of spending through strategically sourced contracts. In fiscal year 2011, DHS reported managing 20 percent of its spending and achieving savings of \$324 million. At the government-wide level, the FSSI program reported managing \$339 million through several government-wide initiatives in fiscal year 2011 and achieving \$60 million in savings, or almost 18 percent of the procurement spending it managed through these initiatives. After strategic sourcing contracts are awarded, realizing cost savings and other benefits depends on utilization of these contracts. We found that only 15 percent of government-wide spending for the products and services covered by the FSSI program went through FSSI contracts in fiscal year 2011. Agencies cited a variety of reasons for not participating, such as wanting to maintain control over their contracting activities, or because the agency had unique requirements. FSSI use is not mandatory and agencies face no consequences for not using FSSI contract vehicles.

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## Barriers to Strategic Sourcing

There are a variety of impediments to strategic sourcing in the federal setting but several stood out prominently in our 2012 review.<sup>6</sup> Specifically, agencies faced challenges in obtaining and analyzing reliable and detailed data on spending as well as securing expertise, leadership support, and developing metrics.

- **Data:** Our reports have consistently found that the starting point for strategic sourcing efforts is having good data on current spending and yet this is the biggest stumbling block for agencies. A spending analysis reveals how much is spent each year, what was bought, from whom it was bought, and who was purchasing it. The analysis also identifies where numerous suppliers are providing similar goods and services—often at varying prices—and where purchasing costs can be reduced and performance improved by better leveraging buying power and reducing the number of suppliers to meet needs. The FSSI program and selected agencies generally cited the Federal Procurement Data System-Next Generation (FPDS-NG)—the federal government’s current system for tracking information on contracting actions—as their primary source of data, and noted numerous deficiencies with these data for the purposes of conducting strategic sourcing research. Agencies reported that when additional data sources are added, incompatible data and separate systems often presented problems. We have previously reported extensively on issues agencies faced in gathering data to form the basis for their spend analysis.<sup>7</sup> However, some agencies have been able to make progress on conducting enterprise-wide opportunity analyses despite flaws in the available data. For example, both the FSSI Program Management Office and DHS told us that current data, although imperfect, provide sufficient information for them to begin to identify high spend opportunities. DHS has in fact evaluated the majority of its

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<sup>6</sup>[GAO-12-919](#).

<sup>7</sup>GAO, *Opportunities to Reduce Potential Duplication in Government Programs, Save Tax Dollars, and Enhance Revenue*, [GAO-11-318SP](#) (Washington, D.C.: Mar. 1, 2011); *Defense Acquisitions: Tailored Approach Needed to Improve Service Acquisition Outcomes*, [GAO-07-20](#) (Washington, D.C.: Nov. 9, 2006); *Homeland Security: Successes and Challenges in DHS’s Efforts to Create an Effective Acquisition Organization*, [GAO-05-179](#) (Washington, D.C.: Mar. 29, 2005); *Best Practices: Using Spend Analysis to Help Agencies Take a More Strategic Approach to Procurement*, [GAO-04-870](#) (Washington, D.C.: Sept. 16, 2004); and *Best Practices: Improved Knowledge of DOD Service Contracts Could Reveal Significant Savings*, [GAO-03-661](#) (Washington, D.C.: June 6, 2003).



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10 highest-spend commodities and developed sourcing strategies for seven of those based on its analysis of primarily FPDS-NG data. Further, we have previously reported that the General Services Administration estimated federal agencies spent about \$1.6 billion during fiscal year 2009 purchasing office supplies from more than 239,000 vendors.<sup>8</sup> GSA used available data on spending to support development of the Office Supplies Second Generation FSSI, which focuses office supply spending to 15 strategically sourced contracts.

- **Expertise:** Officials at several agencies also noted that the lack of trained acquisition personnel made it difficult to conduct an opportunity analysis and develop an informed sourcing strategy. For example, Army officials cited a need for expertise in strategic sourcing and spend analysis data, and OMB officials echoed that a key challenge is the dearth of strategic sourcing expertise in government. VA and Energy also reported this challenge. A few agencies have responded to this challenge by developing training on strategic sourcing for acquisition personnel. For example, the Air Force noted that it instituted training related to strategic sourcing because it is necessary to have people who are very strong analytically to do the front-end work for strategic sourcing, and these are the hardest to find. The training course facilitates acquisition personnel in obtaining the strong analytical skills to perform steps like market evaluation. VA has also begun to develop training to address this challenge.
- **Leadership commitment:** We also found in 2012 that most of the agencies we reviewed were challenged by a lack of leadership commitment to strategic sourcing, although improvements were under way.<sup>9</sup> We have reported that in the private sector, the support and commitment of senior management is viewed as essential to facilitating companies' efforts to re-engineer their approaches to acquisition as well as to ensuring follow through with the strategic sourcing approach. However, we found in 2012 that leaders at some agencies were not dedicating the resources and providing the incentives that were necessary to build a strong foundation for strategic sourcing.

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<sup>8</sup>GAO, *Strategic Sourcing: Office Supplies Pricing Study Had Limitations, but New Initiative Shows Potential for Savings*, [GAO-12-178](#) (Washington, D.C.: Dec. 20, 2011).

<sup>9</sup>[GAO-12-919](#).



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- **Metrics:** A lack of clear guidance on metrics for measuring success has also impacted the management of ongoing FSSI efforts as well as most selected agencies' efforts. We found that agencies were challenged to produce utilization rates and other metrics—such as spending through strategic sourcing contracts and savings achieved—that could be used to monitor progress. Several agencies also mentioned a need for sustained leadership support and additional resources in order to more effectively monitor their ongoing initiatives.

Agency officials also mentioned several disincentives that can discourage procurement and program officials from proactively participating in strategic sourcing, and at many agencies, these disincentives have not been fully addressed by leadership. Key disincentives identified by agency officials include the following:

- A perception that reporting savings due to strategic sourcing could lead to program budgets being cut in subsequent years,
- Difficulty identifying existing strategic sourcing contracts that are available for use as there is no centralized source for this information,
- A perception that strategically sourced contract vehicles may limit the ability to customize requirements,
- A desire on the part of agency officials to maintain control of their contracting,
- Program officials' and contracting officers' relationships with existing vendors, and
- The opportunity to get lower prices by going outside of strategically sourced contracts.

Leaders at some agencies have proactively introduced practices that address these disincentives to strategically source. For example, DHS and VA reported increasing personal incentives for key managers by adding strategic sourcing performance measures to certain executives' performance evaluations. In addition, several agencies including DOD, DHS, and VA have instituted policies making use of some strategic sourcing contracts mandatory or mandatory "with exception," although the extent to which these policies have increased use of strategic sourcing vehicles is not yet clear. Some agencies have made use of automated systems to direct spending through strategic sourcing contracts. For example, FSSI issued a blanket purchase agreement through its office

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supplies initiative that included provisions requiring FSSI prices to be automatically applied to purchases made with government purchase cards. VA reported that its utilization rate for the office supplies FSSI contracts increased from 12 percent to 90 percent after these measures took effect.

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### Agencies Are Reluctant to Apply Strategic Sourcing to Purchase of Services

In fiscal year 2012, the federal government obligated \$307 billion to acquire services ranging from the management and operations of government facilities, to information technology services, to research and development. This represents over half of all government procurements. Making services procurement more efficient is particularly relevant given the current fiscal environment, as any savings from this area can help agencies mitigate the adverse effects of potential budget reductions on their mission. Moreover, our reports have shown that agencies have difficulty managing services acquisition and have purchased services inefficiently, which places them at risk of paying more than necessary.<sup>10</sup> These inefficiencies can be attributed to several factors. First, agencies have had difficulty defining requirements for services, such as developing clear statements of work which can reduce the government's risk of paying for more services than needed. Second, agencies have not always leveraged knowledge of contractor costs when selecting contract types.<sup>11</sup> Third, agencies have missed opportunities to increase competition for services due to overly restrictive and complex requirements; a lack of access to proprietary, technical data; and supplier preferences.<sup>12</sup>

We found that strategic sourcing efforts addressed products significantly more often than services and that agencies were particularly reluctant to apply strategic sourcing to the purchases of services.<sup>13</sup> For example, of the top spending categories that DOD components reported targeting through implemented strategic sourcing initiatives, only two are services. Officials reported that they have been reluctant to strategically source

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<sup>10</sup>GAO, *Defense Acquisition: Actions Needed to Ensure Value for Service Contracts*, [GAO-09-643T](#) (Washington, D.C.: Apr. 23, 2009).

<sup>11</sup>Contract types include time-and-materials contracts, performance-based contracts, and undefinitized contracts.

<sup>12</sup>GAO, *Defense Contracting: Competition for Services and Recent Initiatives to Increase Competitive Procurements*, [GAO-12-384](#) (Washington, D.C.: Mar. 15, 2012).

<sup>13</sup>[GAO-12-919](#).

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services for a variety of reasons, such as difficulty in standardizing requirements or a decision to focus on less complex commodities that can demonstrate success. Yet, like the commercial sector, federal agencies can be strategic about buying services. For example, DHS has implemented a strategic sourcing initiative for engineering and technical services, which is also in the top 10 spending categories for the Army, Air Force, and Navy.

The reluctance of federal agencies to apply strategic sourcing to services stands in sharp contrast to leading companies. As described below, leading companies perceive services as prime candidates for strategic sourcing, though they tailor how they acquire these services based on complexity and availability.

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## Leading Company Practices Generate Significant Savings by Strategically Sourcing Services

Given the trend of increased federal government spending on services and today's constrained fiscal environment, this Committee asked that we identify practices used by large commercial organizations in purchasing services. We reported on the results of this review in April 2013.<sup>14</sup> Like the federal government, leading companies have experienced growth in spending on services, and over the last 5 to 7 years, have been examining ways to better manage them. Officials from seven leading companies GAO spoke with reported saving 4 to 15 percent over prior year spending through strategically sourcing the full range of services they buy, including services very similar to what the federal government buys: facilities management, engineering, and information technology, for example. Leading company practices suggest that it is critical to analyze all procurement spending with equal rigor and with no categories that are off limits. Achieving savings can require a departure from the status quo. Companies' keen analysis of spending, coupled with central management and knowledge sharing about the services they buy, is key to their savings. Their analysis of spending patterns can be described as comprising two essential variables: the complexity of the service and the number of suppliers for that service. Knowing these variables for any given service, companies tailor their tactics to fit the situation; they do not treat all services the same. In our 2013 report, we highlighted quotes from company officials that illuminate what their approach to increasing procurement efficiency means to them (see table 1).

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<sup>14</sup>[GAO-13-417](#).

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**Table 1: Quotes from Company Officials about Increasing Procurement Efficiency**

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- “If you measure it, savings will happen”
  - “Savings is in our DNA”
  - “Unmanaged spend equals inefficiency”
  - “Centralize the knowledge, not the activity”
  - “You must eliminate rogue buying”
  - “You cannot just go with a ‘three bids and a buy’ contracting approach”
  - “When purchasing a service, you are essentially paying for the quality of the suppliers’ management processes”
  - “You must continually stay ahead of suppliers or they will figure you out”
  - “Complexity drives cost”
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Source: Interviews with company officials.

Leading companies generally agreed that the following foundational principles are all important to achieving successful services acquisition outcomes:

- maintaining spend visibility,
- centralizing procurement,
- developing category strategies,
- focusing on total cost of ownership, and
- regularly reviewing strategies and tactics.

Taken together, these principles enable companies to better identify and share information on spending and increase market knowledge about suppliers to gain situational awareness of their procurement environment. This awareness positions companies to make more informed contracting decisions.

For example, in addition to leveraging knowledge about spending, leading companies centralize procurement decisions by aligning, prioritizing, and integrating procurement functions within the organization. The companies we spoke with overcame the challenge of having a decentralized approach to purchasing services, which had made it difficult to share knowledge internally or use consistent procurement tactics. Without a centralized procurement process, officials told us, companies ran the risk that different parts of the organization could be unwittingly buying the same item or service, thereby missing an opportunity to share knowledge

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of procurement tactics proven to reduce costs. Company officials noted that centralizing procurement does not necessarily refer to centralizing procurement activity, but to centralizing procurement knowledge. This is important because there is a perception in the federal community that strategic sourcing requires the creation of a large, monolithic buying organization.

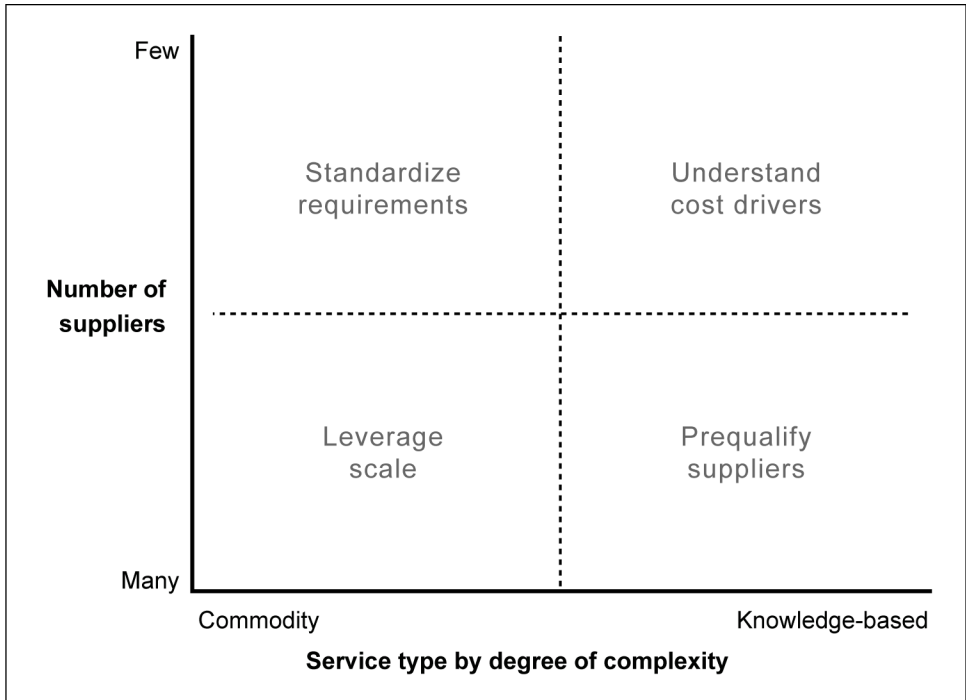
Companies also develop category-specific procurement strategies with stakeholder buy-in in order to use the most effective sourcing strategies for each category. Category-specific procurement strategies describe the most cost-effective sourcing vehicles and supplier selection criteria to be used for each category of service, depending on factors such as current and projected requirements, volume, cyclical demand, risk, the services that the market is able to provide, supplier base competition trends, the company's relative buying power, and market price trends. Company officials told us that category strategies help them conduct their sourcing according to a proactive strategic plan and not just on a reactive, contract-by-contract basis. One company's Chief Procurement Officer referred to the latter as a "three bids and a buy" mentality that can be very narrowly focused and result in missed opportunities such as not leveraging purchases across the enterprise or making decisions based only on short term requirements. Similarly, Boeing says it sometimes chooses to execute a short-term contract to buy time if market research shows a more competitive deal can be obtained later.

In addition, companies focus on total cost of ownership—making a holistic purchase decision by considering factors other than price. This is also contrary to a perception that strategic sourcing can lose a focus on best value. For example, while Walmart may often award a contract to the lowest bidder, it takes other considerations into account—such as average invoice price, time spent on location, average time to complete a task, supplier diversity, and sustainability—when awarding contracts. Humana is developing internal rate cards for consulting services that would help the company evaluate contractors' labor rates based on their skill level. Pfizer's procurement organization monitors compliance with company processes and billing guidelines. The company considers its procurement professionals as essentially risk managers rather than contract managers because they need to consider what is best for the company and how to minimize total cost of ownership while maintaining flexibility.

Companies Tailor Their Procurement Tactics to Each Type of Service Depending on Complexity and Availability of Suppliers

By following the foundational principles to improve knowledge about their procurement environment, companies are well positioned to choose procurement tactics tailored to each service. While companies emphasize the importance of observing the principles, including category strategies, they do not take a one-size-fits-all approach to individual service purchase decisions. Two factors—the degree of complexity of the service and the number of available suppliers—determine the choice of one of four general categories of procurement tactics appropriate for that service: leveraging scale, standardizing requirements, prequalifying suppliers, and understanding cost drivers. Figure 1 below shows how the two factors help companies categorize different services and select appropriate tactics.

Figure 1: Companies’ Transactional Framework



Source: GAO analysis.

For commodity services with many suppliers, such as administrative support, facilities maintenance, and housekeeping, companies generally focus on leveraging scale and competition to lower cost. Typical tactics applicable to this quadrant of services include consolidating purchases across the organization; using fixed price contracts; developing procurement catalogs with pre-negotiated prices for some services; and

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varying bidding parameters such as volume and scale in order to find new ways to reduce costs.

For commodity services with few suppliers, such as specialized logistics and utilities, companies focus on standardizing requirements. Typical tactics applicable to this quadrant of services include paring back requirements in order to bring them more in line with standard industry offerings, and developing new suppliers to maintain a competitive industrial base. For example, Walmart holds pre-bid conferences with suppliers such as those supplying store security for “Black Friday”—the major shopping event on the day after Thanksgiving—to discuss requirements and what suppliers can provide. Delphi makes an effort to maintain a competitive industrial base by dual-sourcing certain services in order to minimize future risk—a cost trade-off.

For knowledge-based services with many suppliers, such as information technology, legal, and financial services, companies prequalify and prioritize suppliers to highlight the most competent and reasonable suppliers. Typical tactics applicable to this quadrant of services include prequalifying suppliers by skill level and labor hour rates; and tracking supplier performance over time in order to inform companies’ prioritization of suppliers based on efficiency. For example, Pfizer Legal Alliance was created to channel the majority of legal services to pre-selected firms. Delphi only awards contracts to companies on their Category Approved Supplier List. The list is approved by Delphi leadership and is reviewed annually.

For knowledge-based services with few suppliers, such as engineering and management support and research and development services, companies aim to maximize value by better understanding and negotiating individual components that drive cost. Typical tactics applicable to this quadrant of services include negotiating better rates on the cost drivers for a given service; closely monitoring supplier performance against pre-defined standards; benchmarking supplier rates against industry averages in order to identify excess costs; and improving collaboration with suppliers (see table 2).



**Table 2: Examples of Services Based on Complexity and Number of Suppliers**

	<b>Commodity services</b>	<b>Knowledge-based services</b>
Few suppliers	<ul style="list-style-type: none"> <li>• Certain types of security</li> <li>• Specialized logistics</li> <li>• Specialized maintenance and repair</li> <li>• Utilities</li> </ul>	<ul style="list-style-type: none"> <li>• Engineering and management support</li> <li>• High-end consulting</li> <li>• Intelligence</li> <li>• Research and development</li> <li>• Specialty legal</li> <li>• Specialty training</li> </ul>
Many suppliers	<ul style="list-style-type: none"> <li>• Administrative support</li> <li>• Automated data processing</li> <li>• Contract and contingent labor</li> <li>• Facilities construction and operations</li> <li>• General maintenance and repair</li> <li>• Housekeeping and janitorial</li> <li>• Landscaping</li> <li>• Telecommunications</li> <li>• Travel and transportation</li> </ul>	<ul style="list-style-type: none"> <li>• Advertising and marketing</li> <li>• Education and training</li> <li>• Financial</li> <li>• Health care</li> <li>• Human resources</li> <li>• Information technology</li> <li>• Legal</li> <li>• Public relations</li> </ul>

Source: GAO analysis based on company interviews.

Companies we reviewed are not content to remain limited by their environment; over the long term, they generally seek to reduce the complexity of requirements and bring additional suppliers into the mix in order to commoditize services and leverage competition. This dynamic, strategic approach has helped companies demonstrate annual, sustained savings. Companies generally aim to commoditize services over the long term as much as possible because, according to them, the level of complexity directly correlates with cost. Companies also aim to increase competition, whether by developing new suppliers or reducing requirements complexity, which could allow more suppliers to compete. In doing so, companies can leverage scale and competition to lower costs.

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## Recent Actions May Facilitate Agencies' Greater Use of Strategic Sourcing

OMB and other agencies have recently taken actions to expand the use of strategic sourcing. In September 2012, GAO recommended that the Secretary of Defense, the Secretary of Veterans Affairs, and the Director of OMB take a series of detailed steps to improve strategic sourcing efforts.<sup>15</sup> More specifically, we recommended that

- DOD evaluate the need for additional guidance, resources, and strategies, and focus on DOD's highest spending categories;
- VA evaluate strategic sourcing opportunities, set goals, and establish metrics; and
- OMB issue updated government-wide guidance on calculating savings, establish metrics to measure progress toward goals, and identify spending categories most suitable for strategic sourcing.

In commenting on the September 2012 report, DOD, VA, and OMB concurred with the recommendations and stated they would take action to adopt them. We reported in April 2013 that DOD and VA had not fully adopted a strategic sourcing approach but had actions under way.<sup>16</sup> For example, at that time, DOD had developed a more comprehensive list of the department's strategic sourcing efforts, was creating additional guidance that includes a process for regular review of proposed strategic sourcing initiatives, noted a more focused targeting of top procurement spending categories for supplies, equipment, and services, and was assessing the need for additional resources to support strategic sourcing efforts. VA reported that it had taken steps to better measure spending through strategic sourcing contracts and was in the process of reviewing business cases for new strategic sourcing initiatives, and adding resources to increase strategic sourcing efforts.

In 2012, OMB released a Cross-Agency Priority Goal Statement, which called for agencies to strategically source at least two new products or services in both 2013 and 2014 that yielded at least 10 percent savings. At least one of these new initiatives is to target information technology commodities or services. In December 2012, OMB further directed certain agencies to reinforce senior leadership commitment by designating an official responsible for coordinating the agency's strategic sourcing

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<sup>15</sup> [GAO-12-919](#).

<sup>16</sup> [GAO-13-279SP](#).

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activities. In addition, OMB identified agencies that should take a leadership role on strategic sourcing. OMB called upon these agencies to lead government-wide strategic sourcing efforts by taking steps such as recommending management strategies for specific goods and services to ensure that the federal government receives the most favorable offer possible. OMB directed these agencies to promote strategic sourcing practices inside their agencies by taking actions including collecting data on procurement spending.

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In closing, current fiscal pressures and budgetary constraints have heightened the need for agencies to take full advantage of strategic sourcing. These practices drive efficiencies and yield benefits beyond savings, such as increased business knowledge and better supplier management. Government-wide strategic sourcing efforts have been initiated, and federal agencies have improved and expanded upon their use of strategic sourcing to achieve cost savings and other benefits. However, little progress has been made over the past decade and much more needs to be done to better incorporate strategic sourcing leading practices, increase the amount of spending through strategic sourcing, and direct more efforts at high spend categories, such as services. Companies have shown that it is possible to save money by strategically managing services. They have done so not just by consolidating purchases of simple, commodity-like services; they have devised strategies and tactics to manage sophisticated services. Companies have also shown that savings come over a wide base and that results can be achieved with leadership, shared data, and a focus on strategic categories that is dynamic rather than static. Strategic sourcing efforts to date have targeted a small fraction of federal procurement spending. As budgets decline, however, it is important that the cost culture in federal agencies change. Adopting leading practices can enable agencies to provide more for the same budget.

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Chairman Carper, Ranking Member Coburn, and Members of the Committee, this concludes my statement. I would be pleased to answer any questions at this time.

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## GAO Contact and Staff Acknowledgments

For future questions about this statement, please contact me at (202) 512-4841 or [chaplainc@gao.gov](mailto:chaplainc@gao.gov). Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this statement. Individuals making key contributions to this statement include W. William Russell, Assistant Director; Peter Anderson; Leigh Ann Haydon; John Krump; Roxanna Sun; Molly Traci; Ann Marie Udale; Alyssa Weir; and Rebecca Wilson.

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