

## Summary

Rambøll and Inventura hereby present a final report of the project "Costs, savings and efficiency through competition". The project is conducted in the period June-December 2013 on behalf of KS. This chapter presents a summary of the report's main findings.

### 1.1 What is the savings using competition for the purchase of supplies/services?

Procurement legislation should ensure effective use of resources for the public and the process should follow the basic requirements stated in the LOA § 5 and § 1.3 FOA. This means that to ensure that the procurement is based on competition and predictability, transparency and verifiability maintained throughout the procurement process. Basic requirements and procedures will also prevent corruption. The overall purpose of the regulations is to promote greater economic growth. How much savings can be achieved depends on several factors, and therefore it is difficult to quantify this. Factors that may affect the savings level is the concentration of volumes, the selection of the correct specification type, the active use of market expertise to get the best suppliers, "buy / make" analysis, quality (purchasing skills) in the procurement process, and the number of times and with what frequency the market has been requested earlier.

In summary we can say that the rates and conditions is achieved will depend on how to formulate needs, prepare the specifications, dialogue with market and quality in the implementation phase. In cases where you have the opportunity to choose a negotiated procedure, better contracts will be achieved.

#### 1.1.1 Transaction costs of the procurement process

Cost estimates indicate that the procurement process costs local government nearly 1.3 billion NOK per year. It is assumed that the municipal sector carries out almost 11,000 procurements annually. Cost estimates show that the procurement of health services and construction has a greater cost per process compared to other procurement of supplies or services.

Findings also show that the local government considers it equally costly to carry out procurement processes with procurements above and below the national threshold and the EEA threshold. This is explained by the municipal sector largely relate to Part II of the FOA, and to a lesser extent to Part I. In addition, the municipal sector are concerned with not to make "mistakes" in the procurement process, and therefore choose often follow a more "strict" legislation than is necessary.

#### 1.1.2 Estimates of savings for local government

There are currently no reliable estimates of what the real savings for the municipal sector is by conducting competitions. Cost savings of several percent can be achieved in certain procurements. In the other procurement savings can be zero. Savings potential will also vary from sector to sector. Analyses of savings by outsourcing of health and social services, such as the operation of nursing homes, conclude somewhat significant savings potential<sup>1</sup>. The potential is partly due to reduced wage and pension expenses, which is not necessarily desirable for political and/or ideological reasons. In the aggregation of numbers / finding there is considerable uncertainty. There are further challenges and uncertainty about the likely differences between exposure and competitive tendering processes.

In an attempt to estimate the possible savings, we choose to base our estimate on a report for the European Commission which concludes that competitions can yield savings of 1% reduction per bidder. This level of savings is our opinion sober and something we, based on our own experiences, can relate to. In Norway there are on average four bidders per competition, which will be equivalent to 4% price reduction. The municipal sector purchased goods and services for 75 billion in 2011. This means that local government can potentially achieve savings of 3 billion.

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<sup>1</sup>Oslo Economics (2013). Sykehjemsdrift i Oslo- effekten av konkurranse

Including the estimated cost of the procurement process (1.3 billion NOK), this provides a potential savings of 1.7 billion. We emphasize that there is considerable uncertainty associated with this number. Estimated transaction costs of procurement processes are based on an estimated population of approx. 11000 annual procurement. The number is probably somewhat low for the municipal sector.

Findings in this report indicate that the informants perceive that they spend too little time in the execution of a procurement process. If we assume that our estimate for the recommended time commitment, 30% increase in time spent, to conduct a good procurement process, this constitute the transaction cost to be roughly 1.5 billion. This means that the local government will have a higher transaction cost by implementing procurement processes. However, there is still an expectation that increased time spent in the execution of a procurement process will lead to a better qualitative process that can provide both lower prices and / or better quality. In light of the importance of increased competence, importance of a procurement strategy and professional procurement resources to follow up the contracts, there is an expectation that there is a greater savings potential than the 1.7 billion that can be taken out with the current use of resources in the procurement process. However, in this report we have no basis for saying how great the saving potential of this can be.

Outsourcing can provide financial savings for the municipal sector. However the potential savings we will be a very cautious estimate. We believe that potential savings by outsourcing will be a bit more than 4 %, but it is very difficult to say how *much* more. This is because outsourcing has a much greater complexity than just exposure of other goods/services in a competition. A number of considerations must be taken in assessing what could be savings, including costs associated with construction / buildings. In addition, one major reason for savings is related to pension expenses. The municipal sector has a defined benefit pension plan. The commercial providers of nursing home operation have a defined contribution plan. The cost of the two schemes is very different for the employer.

An assessment of the economic gains from outsourcing requires a separate and thorough study, where all the factors examined before a final conclusion can be promoted.

## 1.2 Do procurement regulations prevent maximal efficiency gains?

In our opinion, FOA Part II complexity and rigidity can lead to unnecessarily high processing and procurement costs. High processing costs because extensive expertise and resources and time, cost money. The findings show that the local government considers it as time - consuming and costly to implement procurement with value above and below the national threshold for the EEA threshold. Ramboll and Inventura finds that the estimated time spent for procurement under national threshold is disproportionately high. This is because the regulatory requirements for procurement under national threshold include fewer procedural requirements for procurement. Because transaction costs for procurement above and below the national threshold is approximately equal in absolute terms, this means that the relative costs of procurement under national threshold is far higher than above the national procurement threshold. If the relative costs should be similar for the municipal sector for these two types of procurement, this means that the savings of local government by conducting procurement under national threshold must be higher than for the procurement of the national threshold. Our assessment is that this is not necessarily due to procurement regulations in itself, but knowledge about the rules. According to informants, they have a greater focus on following the requirements for procurements that fall under FOA Part II than Part I. Meanwhile, the municipal sector is concerned not to make mistakes in the procurement process with the risk of being reported for violations. The municipal sector chooses to follow a more strict set of rules for procurement under national threshold than is necessary. This suggests that local government does not necessarily follow the intention of the legislation.

The study points to a number of other conditions that the municipal sector considers cost drivers upon completion of a procurement process. Lack of backing of a procurement strategy and procurements has implications for how public procurements are prioritized in terms of resources

and economically. A lack of strategy makes the sector have fewer goals for procurements, and thus no established incentives to conduct good and cost-effective procurements.

Procurement competence and resources are important for prioritizing time spent on the procurement process. Findings show that small and partly medium-sized municipalities have fewer professional procurement resources and opportunities for capacity building, compared to large municipalities and purchasing network. Expertise and access to resources is also significant for the tendering procedures chosen. Lack of competence in conducting negotiation and on the legislation are cited as an explanation for why this procedure is deselected. Lack of competence on the procurement legislation is also used as an explanation of why the municipal sector to a lesser extent conducts market research.

### 1.3 The procurement process

The procurement process is divided into three main phases: the preparation phase, the implementation phase and the follow-up phase.

Findings from the survey show that the municipal sector mainly prioritizes and uses far the most time in the implementation phase. The majority of interviewees in this study stated that the municipality lacks an overall procurement strategy, resulting in a lack of political and administrative backing of purchasing activities. Nor is market research and - dialogue a priority in the procurement process. This reflects the fact that there are limited resources dealing with procurement processes, as well as the municipality sector is unsure whether the procurement rules allow dialogue with potential bidders. Informants agree that increased focus on monitoring phase will entail faster deviation monitoring, better deliveries under existing contracts and better contracts with suppliers for new contests.

#### 1.3.1 Time spent on the procurement process

The time per process varies by type of competition and the contract value. Time estimates show that municipalities use between 244 hours and 275 hours respectively an open tender process and a negotiated procedure. Similarly regional government spends between 224 hours and 257 hours. Networks uses between 307 hours and 337 hours. In the procurement above the EEA threshold local government spend about 261 hours per process, regional government use 228 hours, while purchasing network using 383 hours per process. Purchasing network has the highest use of time, which is also expected. This is explained by good professional procurement expertise, priority resources in the procurement process, procurement of major contracts and more employees involved.

The project has also been a focus of competition exposure of services within the health care sector. Time estimates show that on average the municipal sector use 520 hours per process in this sector. The explanation is that the procurement of services within the health care sector is considered very extensive and complex. This relates both to ensure good descriptions of what kind of service you wish to purchase, but also the evaluation phase is considered to be demanding.

### 1.4 More can be saved in the municipal sector

Our survey indicates that more can be saved by the use of competition. Savings can be related to the simplification of the regulations. Simplification of FOA Part II may involve removing and simplifying some of the procedural provisions of Part II. When it comes to rigidity this may involve extended right to correct errors and omissions on offer. The municipal sector also points out that the regulations are perceived as unclear in relation to the opportunities municipal sector dialogue ahead of the competition in the market. Better dialogue with the market ahead of the competition can contribute to a sharpening of the descriptions in the tender for what should be sought after. Meanwhile, dialogue ensure that the municipal sector demand what actually exists in the market.

Increased capacity and expertise on procurement process in the municipal sector are important. This means more purchasing professional resources in municipalities dealing with public procurement and purchasing practices. Particularly the need for more professional purchasing resources to ensure best practices for contract and supplier monitoring are asked for. There is also

a need for better knowledge about public procurement, procurement regulations and good procurement processes, especially when it comes to conducting procurements under the national threshold. The municipal sector has stressed the need for greater expertise in using negotiations as a tender procedure. The municipal sector has an expectation that more professional purchasing resources and better expertise on public procurement will contribute to a better qualitative procurement process, better and more thorough contract management, which could lead to financial savings.