

**For discussion
on 11 December 2006**

**Legislative Council Panel on
Information Technology and Broadcasting**

Implementation of Pilot e-Procurement Programme

PURPOSE

This paper seeks Members' support on the proposal to implement a pilot e-Procurement programme in the Government of the Hong Kong Special Administrative Region.

BACKGROUND

2. E-Procurement is one of the priority initiatives identified under the new wave of e-government programme which has been included in the 2005 Policy Agenda. It aims to automate and integrate the procurement processes within the Government to enhance transparency, efficiency and cost-effectiveness, and to achieve more competitive pricing for Government procurement. Externally, given the large number of suppliers interested and involved in Government procurement, adoption of e-Procurement practices by the Government would encourage the adoption of IT and e-business practices among local suppliers, particularly small and medium sized enterprises (SMEs). This will enhance their competitiveness in a business environment with increasing emphasis on efficient and quality services.

3. At present, the approval authority for Government procurement activities varies according to the contract value. Purchases of low-value goods (i.e. those with value not exceeding \$1.3 million) and services are delegated to bureaux/departments (B/Ds). These purchases account for over 99% in terms of purchase orders and 30% in terms of purchase value of all Government non-construction related goods and

services procured by the Government. These procurement arrangements are largely paper-based and conducted through manual processes except in a few B/Ds such as the Leisure and Cultural Services Department and the Hong Kong Police Force, where automation has been introduced for certain parts of the procurement process. Purchase of goods with a contract value above \$1.3 million are handled by the Government Logistics Department (GLD).

4. To exploit the potential of e-Procurement in the Government as a whole, we conducted a consultancy study in 2005 to map out a strategy for taking forward e-Procurement to handle high volume, low value purchases (i.e. those not exceeding \$1.3 million) at the B/D level by making reference to the best practices of other governments and successful implementers in the private sectors. The study recommended to adopt a new procurement approach by deploying an integrated range of e-Procurement tools and services with a view to enhancing efficiency, improving the quality of procurement information and promoting supplier base in the adoption of e-Procurement practices and technologies. Key elements of the e-procurement programme include the setting up of an e-Procurement platform or portal, e-sourcing and automation of the entire purchase-to-pay process. A schematic presentation of the proposed e-Procurement strategy is enclosed at **Annex**.

5. The migration to e-Procurement will be a major transformation programme involving a large number of users and suppliers. It will generate significant business changes for all the stakeholders. To minimise risks inherent in major transformation initiative and to enable better change management to support stakeholders, the study recommended an incremental approach for implementation. Specifically:

- (a) pilot programme should be implemented in a few departments before considering service-wide roll-out in the Government;
- (b) e-invoice will not be covered under the pilot programme as its implementation will require the presence of the necessary backend accounting or finance computer system at the suppliers' end; and
- (c) engage suppliers on sector-by-sector basis according to their e-readiness.

6. An incremental approach will also help verify the costs and potential benefits identified in the study and will enable the Government to better evaluate the cost-effectiveness of the proposed e-Procurement strategy and decide on the way forward for service-wide implementation of e-Procurement.

THE PROPOSAL

7. We propose to conduct a pilot e-Procurement programme in three departments, namely, the Office of the Government Chief Information Officer (OGCIO), the Immigration Department (ImmD) and the Environmental Protection Department (EPD) to deal with high volume, low value purchases not exceeding \$1.3 million.

8. The pilot programme will implement by steps the following four e-Procurement initiatives. In addition, a product coding standard will be identified during the pilot implementation with a view to its adoption across B/Ds. Such standard will help to categorize procurement data in an effective and meaningful way thereby facilitating the analysis of procurement information for contract strategy formulation.

(a) *Procurement Portal* – a Government procurement website which will be a gateway for B/Ds to exchange procurement related information internally and with suppliers.

(b) *Purchase-to-Pay System*

i. *Internal Workflow System* – a common software application supported by a standard product coding. The application will streamline and automate the entire procurement process from initiating a requisition, confirming availability of funds, placing a purchase order, confirming delivery and acceptance, to updating payment information to the Treasury accounting system.

ii. *Sourcing* – a web-based solution to support B/Ds to perform the sourcing process. It will automate the process on request for information/quotation/proposals for low value purchases and for purchases under the

Standing Offer Agreement (SOA) ¹.

- iii. *E-Catalogue* – a web-based e-catalogue procurement facility to facilitate B/Ds in preparing and placing purchase orders.

9. Apart from the necessary system development, change management for both user B/Ds concerned and external suppliers will form an integral part of the pilot programme. Seminars, workshops and training will be conducted for Government users and suppliers to promote the benefits of the new system and to guide them on how to use it. Suppliers with computers and broadband connection will be able to communicate with the pilot B/Ds through the procurement portal. Following international best practices, suppliers who are more receptive to the use of IT would be encouraged to participate in the pilot programme first.

10. We plan to conduct a review six months after the full operation of the e-Procurement programme in the three departments concerned. The review will examine the experiences and lessons learnt, the impact on stakeholders, and assess the actual costs and benefits. The findings will become a useful reference for the Government to consider before deciding on the way forward for service-wide implementation of e-Procurement, and the planning parameters of such a wider exercise.

POTENTIAL BENEFITS OF E-PROCUREMENT

11. In other countries, implementation of e-Procurement has brought about financial savings arising from cost reduction through streamlining and unifying the procurement processes, as well as price reduction through aggregate buying. Intangible benefits are also achieved in reducing procurement lead time, enhancing transparency of procurement management information and providing a catalyst for change in joining up different parties within government and promoting e-commerce.

¹ Standing Offer Agreement (SOA) is a non-exclusive agreement entered with short-listed suppliers who agree to supply a range of products to Government at a price not exceeding a ceiling price committed by the supplier. B/Ds will obtain quotations from the short-listed suppliers to purchase the required items as necessary.

12. Overseas experience shows that successful implementation of e-Procurement can bring about benefits to both the Government and the suppliers.

E-Procurement is expected to bring the following benefits to the *Government*:

- a) improve efficiency and effectiveness – international benchmark reveals the potential to reduce the procurement cycle time from two weeks to four days. The Hospital Authority has experienced ordering lead time improvement by 14 days in respect of the procurement of common consumables, stationery and other office supplies;
- b) improve quality and accessibility of procurement information;
- c) reduce human errors and enhance traceability;
- d) expand supplier base as B/Ds can share and access supplier information from the central database. Such information may not be readily available to B/Ds in a paper-based system;
- e) reduce transaction cost – overseas experience indicates potential transaction cost reduction of around HK\$300 per purchase order; and
- f) reduce price – by making procurement information more readily available, Government can achieve price reduction through consolidating and aggregating purchases across B/Ds in addition to those already subject to SOAs and Term Contracts. The experience of overseas governments indicates price reduction of around 2%. Although the types and volume of purchases covered in overseas e-Procurement schemes may be different from that of the three pilot departments, we would aim to achieve the 2% benchmark.

To the *suppliers*, e-Procurement will enable them to reap the following benefits:

- a) communicate with the Government more effectively and efficiently by reducing the turnaround time of correspondences and through enhanced accessibility to government procurement information;
- b) expand their business opportunities with the Government by

updating their product catalogues to the e-Procurement Portal which will be assessed by B/Ds; and

- c) encourage the migration to the electronic means of doing business, thereby enhancing suppliers' capability in e-commerce.

13. Although reduction in transaction cost is observed in some cases of e-Procurement adoption, we understand that the main focus of e-Procurement programmes in countries such as Australia and United Kingdom is to enhance operational efficiency instead of cutting staff cost per se. Manual labour freed up from the automated process will help to deliver more value-added activities such as strategic sourcing and aggregate buying leading to price reduction. We will review the actual magnitude of benefits to be achieved after the implementation of the pilot programme.

FINANCIAL IMPLICATIONS

14. We will submit a funding proposal to the Finance Committee in early 2007 for a non-recurrent provision of **\$49.2 million** from 2007-08 to 2010-11 under Capital Works Reserve Fund Head 710 for the implementation of the pilot e-Procurement programme. A breakdown of the cost estimate is as follows:

	<u>\$ million</u>
(a) Hardware	8.3
(b) Software and development	10.1
(c) Implementation services	12.6
(d) Contract Staff	15.9
(e) Contingency	2.3
Total	49.2

15. The pilot also entails non-recurrent staff costs of \$12.1 million for managing project implementation and conducting business process re-engineering study. We will absorb the staff cost through internal redeployment.

IMPLEMENTATION PLAN

16. To facilitate change management and to better manage project risks, we will implement the four e-Procurement initiatives set out in paragraph 8 on an incremental basis.

<u>Activities</u>	<u>Timing</u>
(a) Commencement of tendering exercise	May 2007
(b) Award of Tender	December 2007
(c) Rollout of e-Procurement initiatives	January 2008 to June 2009
(d) Completion of the pilot e-Procurement system	June 2009
(e) Completion of post implementation review	April 2010

17. Subject to the review of the pilot e-Procurement programme, verification of the costs and potential benefits as identified in the study and availability of additional resources, we will consider the way forward on service-wide implementation of e-Procurement.

ADVICE SOUGHT

18. Members are invited to note the scope of the pilot e-Procurement programme as outlined in paragraphs 7 to 10 and support the funding proposal as set out in paragraphs 14 to 15 above.

**Office of the Government Chief Information Officer
Commerce, Industry and Technology Bureau
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Schematic Presentation on the Proposed e-Procurement Strategy

