

Measuring Performance: Validation of Savings



NASPO Annual Meeting
August 28-31, 2006
Boise, Idaho

In the beginning...



Spring 2003 – Challenge to Procurement

- > Save \$200m in two years
- > Build new organization
- > Design on-going support system – Knowledge Management

= **Strategic Sourcing Initiative**

And...

DO IT RIGHT NOW!!



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Measuring Our Success...Initially



Was "how to count" contemplated? Yes.

Savings Validation Committee:

- 6-person team -- consultants, procurement, budget
- Uniform documentation – Savings Validation Form
- Only capture hard dollar and real savings
- Presentations – primary owner of project must convince committee that savings have or will occur
- User agency must sign-off on savings
- Full committee approval required



Initiative → Committee → Capture Savings

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The Budget Can't Wait...

July 2003 – how to get the money NOW?

1. Create Efficiency Initiatives Revolving Fund (EIRF)
 - Tool to collect savings from agencies
 - Method to fund initiative expenses
2. Bill agencies for savings - projected or targeted
3. Collected billings go to General Revenue Fund

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Efficiency Billings...

Fiscal Year 2004:

- Savings projected for each agency as proportion of overall target
- EIRF billing statements sent to agencies totaling ~\$100m (Fall 2003)

Fiscal Year 2005:

- Budgets reduced to reflect FY04 recurring savings
- Savings projected for FY05
- New billings sent to agencies – with category detail (Fall 2004)

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Agency Reaction...



- We did not save this much money
- Our appropriation will not cover our normal operational costs and EIRF billing
- Need more detail on exactly how savings were calculated and in what specific categories

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Enter the Auditors...

Spring 2005 – Findings:



- Efficiency initiative payments made from improper appropriation lines
- Method used to calculate savings did not adequately reflect realized savings for each agency
- Inadequate documentation to support savings validation
- No proof that the efficiency initiatives saved anything

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We need help...

Summer 2005 – Engaged Deloitte Consulting

Objectives

- ✓ Third party validation
- ✓ Define savings
- ✓ Develop and apply sound methodology to:
 - ✓ Meet audit standards
 - ✓ Satisfy scrutiny of all stakeholders: media, budget office, auditors (internal and external), public, vendors, state agencies, legislators
- ✓ Identify clear links and evidence to connect savings to official records

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Scope of Engagement...

Savings validation project went beyond procurement --

Efficiency Initiatives

- Procurement
- Fleet
- IT/Telecom
- Facilities Management
- Internal Audit
- Media
- Legal

- ◆ Covered two years – FY04 and FY05
- ◆ Over 100 individual projects examined
 - ◆ 54 projects were validated
 - ◆ Over 8,000 hours of work

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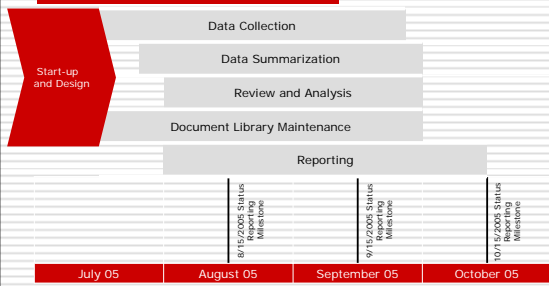
What is Savings...

Definition of Savings

Deloitte: "...the term savings is broadly used to refer to all types of financial benefits gained through the impacts of the Efficiency Initiatives."

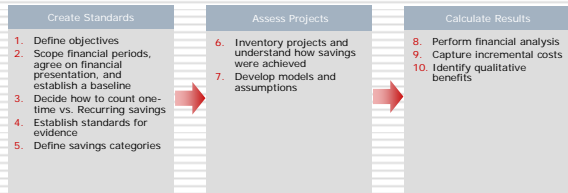
As later refined: "...all types of financial benefits gained including cost reductions, revenue enhancements and cost avoidance – based on a Total Cost of Ownership (TCO) model."

Approach...



and Methodology...

Within the overarching steps included in the project approach, the following tasks were performed:



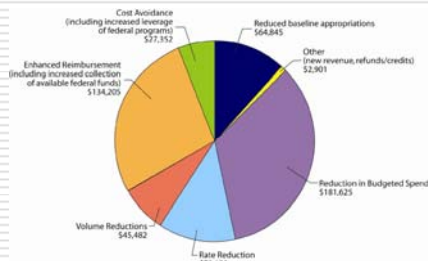
4. Establish Standards for Evidence

- Whenever possible, support savings calculations with information from official and verifiable sources. For example, use "actuals" from following types of sources:
 - Financial reports
 - Expenditure reports from general ledger system
 - Contract/payment records
 - Payroll system
- Goal is to establish a traceable link from official records of actual financial transactions/results to project savings
- Supporting documents also serve as basis for further review and assessment by key stakeholder parties including auditors (internal or external), legislators, reporters, and constituents

5. Define Savings Categories

- **Reduced Baseline Appropriation** — A reduction in available resources based on General Assembly actions or targeted cuts in certain areas.
- **Reduction from Budgeted Spend** — A reduction in the projected/budgeted resources (e.g., staff time, materials, and equipment) used for an activity or business process, as a result of a Savings Project.
- **Rate Reductions** — Obtaining lower rates or prices for goods or services purchased by the State.
- **Volume Reductions** — Reducing the amount of a good or service used. Savings captured in this category included projects that intentionally sought volume reductions through direct action (e.g., demand management).
- **Refunds/Credits** — Payments made to the state by vendors as a result of a Savings Project.
- **New Revenue** — New streams of revenue instituted by the state.
- **Enhanced Reimbursement** — Improvements in the accuracy or completeness of a business process that generates a higher rate of recovery of funds from external organizations.
- **Cost Avoidance** — A benefit resulting from the prevention of a likely, but non-budgeted expenditure in the current or a future period.

Results: \$529 million in savings...



* All initiatives combined FY04 and FY05



Procurement Savings Summary...

Category	Number of Projects	Total Savings
Rate Reductions	15	\$ 26,621,000
Enhanced Reimbursement	8	\$151,438,000
Budget Spend Reduction	3	\$ 37,013,000
Cost Avoidance	1	\$ 1,833,000
TOTAL	27	\$216,905,000

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What's Next...

- Savings validation designed for specific time period around specific set of initiatives
- Continue to identify and implement cost savings ideas and concepts
- Need to establish new baselines to meet new direction while maintaining core principles of savings methodologies – still need to reduce costs
- Develop new models to capture:
 - Cost of transparency
 - Value of improving processes
 - Value a project brings to the State
 - Affect on service levels
- Continue to implement Shared Services

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References...

- Deloitte Report – October 2005
- Measuring and Sustaining Government Efficiency Conference – March 9, 2006
- Government Procurement Journal – June 2006
"Illinois Transforms Procurement and Saves"

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Calculation Models...

Revenue Improvement Categories	Calculation	Evidence
Refunds/Credits	<input type="checkbox"/> Sum of refunds/credits received <input type="checkbox"/> Baseline would be 0. Revenue would be the sum of refunds/credits received for activity in the fiscal year: ■ Revenue = R1 ■ Baseline = 0 ■ Revenue Benefit = R1-0	Payments received
New Revenues	<input type="checkbox"/> Sum of receipts for new revenue streams <input type="checkbox"/> Baseline would be 0. Revenue would be the sum of the new revenues received for activity in the fiscal year: ■ Revenue = R1 ■ Baseline = 0 ■ Revenue Benefit = R1-0	Payments received
Enhanced Reimbursement	<input type="checkbox"/> Measure reimbursements that were obtained as a result of Savings Project. <input type="checkbox"/> Revenue is the current activity level times the current rate of recovery. Baseline is the current activity level times the original recovery rate. ■ Revenue = R1 * V1 ■ Baseline = R0 * V1 ■ Revenue Benefit = (R1 * V1) - (R0 * V1)	Payments received

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Calculation Models...

Explanation of Variables:

- AO = Original appropriated funding
- A1 = Final actual appropriated funding
- EP = Projected level of Expenditure/Spending for the current year that was budgeted before the Savings Project
- EA = Actual Expenditure/Spending level experienced after Savings Project (typically zero)
- PO = Rate/Unit Price paid before Savings Project
- P1 = Rate/Unit Price paid after Savings Project
- VO = Volume/Activity level experienced before Savings Project
- V1 = Volume/Activity level experienced after Savings Project
- RO = Revenue/Rebates/Reimbursement Recovery Rates received before the Savings Project
- R1 = Revenue/Rebates/Reimbursements Recovery Rates received after or as a result of the Savings Project

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Procurement Detail...

Rate Reductions Categories (savings \$000)

- Food Cost (\$6,345)
- Cleaning Supplies – Garbage Can Liners (\$737)
- Cleaning Supplies – Janitorial Supplies (\$28)
- Cleaning Supplies – Paper/Foam and Toilet Tissue (\$154)
- Envirotest – Vehicle Emissions (\$10,225)
- Lottery Instant Ticket Dispensing Machines (\$1,461)
- Paper – Envelopes (\$66)
- Paper – Copy Paper (\$649)
- PC's and Laptops (\$152)
- Utilities – Electricity Purchase (\$3,002)
- Utilities – Gas Purchase (\$147)
- Group Insurance Investment Management (\$148)
- HMO Premium Negotiation (\$1,749)
- Hospital Rate Negotiation (\$466)
- IPHCA Negotiation (\$1,292)

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