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REPORT

Office Furniture
Pre-Consultation Report

Prepared by:

The Conference Board of Canada

Prepared for:

PWGSC

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Contact:

Dr. Michael Bloom,
Vice-President,
Organizational Effectiveness and Learning
The Conference Board of Canada

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Section A – Overview

Procurement change is an important initiative for the Government of Canada. Plans for change to federal procurement processes began to be developed several years ago, under the previous government. The current government's stated goals for change are to achieve significant cost savings by reducing the cost of purchases and streamlining procurement processes, and to enhance the quality of goods and services procured. The Government of Canada believes that modernizing its procurement practices is one of the most significant changes in public administration in the last twenty-five years.

Procurement transformation is about more than saving money and getting better prices. It is about getting the best possible value for Canadians. Success will mean savings averaging in the order of more than $500 million annually. (Some of these gains have already been achieved). Success will also mean significant improvements in procurement times and greater satisfaction among client departments and agencies of government. At the same time, government seeks to achieve these gains while minimizing negative impacts on suppliers and helping SMEs, Aboriginal businesses and others to succeed in the new environment.

The big picture of government-wide benefits and the strategic value of the changes to the government's performance is not the primary focus of suppliers who are understandably more concerned about the success of their own operations, and the potential risks they themselves face as a result of procurement change.

Suppliers' views are important to government which recognizes its suppliers' collective importance to its supply system and the future success of procurement. Supplier engagement and cooperation is also important to government, as the basis for building effective and efficient procurement to achieve government performance goals while supporting business success.

To gain an enhanced understanding of suppliers' current views, and to deepen shared understanding, PWGSC has engaged The Conference Board of Canada to host and facilitate a series of ten dialogue sessions with industry associations and supplier communities in three procurement categories: Informatics Professional Services, Temporary Help Services, and Office Furniture.

The objective of these sessions is to obtain industry and supplier perspectives and ideas on the procurement changes, the change process itself, and how the federal government can realize efficiency gains while minimizing disruptions to the supplier network.[1]

The Conference Board is an independent, non-partisan, not-for-profit organization recognized for its research and its expertise in meeting design and facilitation. During this project, the Conference Board has:

- Analyzed the nature of market share and market power of the federal government as a purchaser of goods and services.
- Analyzed the nature of market dependence of individual suppliers on government procurement.

[1] The three procurement categories (IPS, THS and Furniture) accounted for nearly 10 per cent of government procurement spending in the last fiscal year.

- Organized consultations to engage suppliers in open dialogue around the government's procurement change process, policy and strategies and record their issues, concerns and insights.

About The Conference Board of Canada

- A not-for-profit Canadian organization that takes a business-like approach to its operations.
- Objective and non-partisan. We do not lobby for specific interests.
- Experts in running conferences but also at conducting, publishing and disseminating research, helping people network, developing individual leadership skills and building organizational capacity.
- Specialists in economic trends, as well as organizational performance and public policy issues.
- Not a government department or agency, although we are often hired to provide services for all levels of government.
- Independent from, but affiliated with, The Conference Board, Inc. of New York, which serves some 2,500 companies in 60 nations and has offices in Brussels and Hong Kong.

After the ten consultations are complete, The Conference Board of Canada will prepare three independent reports summarizing the session discussions for each of the procurement categories and present them to PWGSC.

Purpose

This paper provides suppliers, industry associations and government officials with a common base of knowledge and understanding within the Furniture procurement category necessary for fruitful discussion. It includes a macro and micro market analysis of the category in order to understand the adjustment risks facing suppliers; an overview of the government's current and intended procurement policy, practices and strategy; and a summary of supplier and government perspectives, issues and challenges.

Procurement

Procurement is the process of acquiring goods, services and construction from third parties. It typically follows four phases:[2]

1. The *pre-contractual* phase—including activities related to requirement definition and procurement planning (e.g., the spend analysis; business requirements; supply market analysis; commodity sourcing strategy; and transition/change management and human resource planning).
2. The *contracting* phase—including all activities from bid solicitation to contract award.
3. The *contract administration and management* phase—including activities such as issuing contract amendments, monitoring progress, following up on delivery, payment action, etc.
4. The post-contractual phase—including final action activities (e.g., client satisfaction, contractor agreement to final claim, final contract amendment, completion of financial

[2] The definition for procurement was taken from a survey developed on behalf of the Honourable Walt Lastewka, Parliamentary Secretary to the Minister of Public Works and Government Services Canada published in September 2004. The survey was used to gather information from government departments and agencies on areas for improvement in federal government procurement. *Procurement and Contracting* [online]. Ottawa: Treasury Board of Canada Secretariat. From: www.tbs-sct.gc.ca/emis-sigd/procurement_contracting_e.asp

audits, proof of delivery, return on performance bonds) and close-out activities (e.g., completeness and accuracy of file documentation and adherence to file presentation standards).

Federal Government Procurement

The Government of Canada buys approximately $20 billion worth of goods and services every year. For PWGSC, in 2005, active government suppliers numbered 16,399, the majority of which (84 per cent) were Canadian or Canadian-based firms. Of these government supplier firms 11,695 (85 per cent) were classified as either self-employed suppliers or small suppliers; 1,283 of them (9 per cent) were medium-sized suppliers; and 1,438 (6 per cent) were large-sized suppliers.[3] The number of suppliers currently doing business with the federal government is much higher than the total for PWGSC. Departments may contract directly with suppliers – about 90 per cent of the 400,000 annual procurement transactions of the federal government are done by departments themselves.[4] Clearly, the federal government is a significant buyer of goods and services and plays a part in shaping the Canadian supplier business landscape.

The federal government's procurement and contracting policies, established by the Treasury Board, are designed and intended to result in best value to the Canadian government and to the Canadian public. Specifically, government policy requires that contracting be conducted in a manner that will enhance access, encourage competition, reflect fairness, and comply with Canada's trade obligations.[5]

Public Works and Government Services Canada

PWGSC supports the daily operations of nearly 140 federal departments and agencies by providing a range of services, including:[6]

- purchasing goods and services on behalf of the government;
- providing office accommodations for public servants across Canada;
- managing national heritage properties; and
- offering services such as information technology, telecommunications, banking, translation, and auditing to the government.

PWGSC is the central acquisition department of the Government of Canada, and is its largest purchasing organization, buying over $20 billion in goods and services—incorporating over 17,000 types of products and upwards of 60,000 contractual transactions—from thousands of suppliers each year.[7] Many purchases, however, are currently done on a department by department basis, and from the standpoint of government, opportunities to leverage its purchasing power to obtain better prices is either mitigated or lost.

[3] From: PWGSC, 2006. Figures represent all suppliers, regardless of Standing Offer. Small firms: <100; Medium-sized firms: 100 - <499; Large firms: >500.
[4] The government is enhancing the capability to capture data on the numbers and composition of its supplier base.
[5] Trade obligations include: North American Free Trade Agreement (NAFTA), the World Trade Organization Agreement on Government Procurement (WTO-AGP), and the Agreement on Internal Trade (AIT). From: www.pwgsc.gc.ca/acquisitions/text/sm/chapter04-e.html
[6] From: www.tpsgc-pwgsc.gc.ca/text/generic/about-e.html
[7] From: www.tpsgc-pwgsc.gc.ca/text/factsheets/goverment_buys-e.html and www.tpsgc-pwgsc.gc.ca/prtf/text/concept_doc-e.html

Procurement Reform at PWGSC

PWGSC has a strong interest in providing Canadian citizens with excellent services at the lowest feasible cost. Currently, PWGSC is looking at ways to improve its efficiency and effectiveness by reforming its procurement processes and practices, and by securing optimal value from suppliers through the products and services purchased.[8] Bringing better value to government and taxpayers is at the stated heart of PWGSC's procurement reform efforts.

For an overview of the Office Furniture category, from the perspective of the Government of Canada, prepared by PWGSC, please see Section C, below.

The Way Forward

PWGSC wants to deliver services smarter, faster and at a reduced cost. *The Way Forward*, which includes a new approach to procurement, is a government-wide system based on principles of accountability, integrity, and transparency.[9] Its goal is to assist federal governments departments, crown corporations and agencies make their procurement activities more efficient and effective. To that end, it will provide government with a series of tools to use in selecting suppliers and choosing products and services in a more transparent and accountable manner.[10] Key points of focus include:

- Emphasize both price and value.
- Provide flexibility to federal government departments, crown corporations and agencies.
- Take into account the circumstances of SMEs and other special supplier groups.
- Incorporate a 'customer satisfaction' component in the evaluation of supplier performance as the basis for continued supplier standing.

Expectations of Improved Efficiencies and Effectiveness

By streamlining the procurement process, using tools to make purchasing easier and quicker, being more disciplined in the way procurement is managed, consolidating what the government buys, and leveraging the government's purchasing power, PWGSC expects to achieve three major milestones:[11]

1. Save $2.5 billion over five years—while maintaining full and fair access to government business by small, medium and large suppliers across Canada, and without

[8] In June of 2005, Bill C-43 came into effect giving the Minister of PWGSC responsibility for procurement of goods and services for the federal government, to enter into contracts on behalf of the government, and to guarantee volume purchases.
[9] *The Way Forward* is a wide-ranging strategy, led by PWGSC, and focuses on increasing efficiencies in three key areas: procurement, property management, and information technology.
[10] In April 2006 the government introduced the Federal Accountability Act and Action Plan in the House of Commons. The legislation is intended to bring forward measures to help strengthen accountability and increase transparency and oversight in government operations, including procurement. From: www.pwgsc.gc.ca/text/transparency-e.html
[11] From: www.pwgsc.gc.ca/transformation/text/faq-e.html

compromising the government's commitments to sustainable development and Aboriginal economic development.[12]

2. Cut the time it takes to conduct procurement by up to 50 per cent.
3. Reduce internal procurement costs by 10 per cent.

PWGSC is working with departments and agencies to improve the way they plan, how they buy, who is authorized to buy and when they buy goods and services. Implementing a more balanced and strategic approach to buying, having better mechanisms and tools in place to monitor departmental and government-wide procurement and to better understand and track the nature of procurement is central to the reform process.

Implications for Suppliers

Overall, government is guided by its stated primary obligation to obtain benefits for the Canadian taxpayer by such means as improving efficiency and effectiveness of its procurement system.

Changes in the way government purchases goods and services may affect suppliers, including:

- Changes in the processes through which suppliers compete for federal government business.
- Changes to the structure and organization of supplier bidding (e.g., through mergers, consortia, etc.).
- Changes to the number of suppliers who choose to, or who are able to compete for government business.

The impact on suppliers is likely to be mixed: some suppliers may be positively affected while others may be adversely affected. In the end, the actual impact will be a product of specific changes in procurement policy and practices, and the ability and willingness of suppliers to adjust.

Broad Policy and Socio-Economic Implications

PWGSC is focusing its effort and attention on government procurement policy and reform. However, the transformation of the procurement system may have implications on other government initiatives and strategies (for example, industrial policy, SMEs, sustainable development). In an effort to address these related initiatives PWGSC has created:

- The Office of Greening Government Operations to advise the government on issues such as green procurement.
- The Office of Small and Medium Enterprises (OSME) to address the need for open and transparent access for small and medium enterprises. OSME works within the government to ensure the procurement system recognizes and addresses the needs of small and medium enterprises, Aboriginal businesses, and the supplier base in the regions where government procures goods and services.
- Tools such as standing offers to facilitate various government departments achieve their targets and commitments. The Aboriginal Business Set-Aside Program, for example, is an

[12] From: www.pwgsc.gc.ca/transformation/text/nfo-fct/fs-2-e.html

Indian and Northern Affairs Canada (INAC) program designed to address Aboriginal business participation through a program of mandatory and selective set-asides and supplier development activities.

Developments during the Procurement Transformation Process

While the planned procurement changes are important, the procurement reform process has resulted in a mix of *positive* and *negative reactions* within the supplier community and among some government departments.

- Industry associations representing suppliers in several procurement categories have called for new consultations.
- Groups of suppliers have registered strong concerns with the approach now being taken to reform procurement and have focused their attention on the potential negative impact on individual suppliers.

Since January, 2005, PWGSC has involved suppliers, industry associations, and government departments in the government-wide review of procurement including through: interviews and consultation meetings with suppliers and industry associations; receiving letters from suppliers and industry associations; issuing Requests for Standing Offers (RFSOs) and Requests for Information (RFSIs); and holding bidders' conferences to seek industry input and feedback.

In response to suppliers' and industry associations' continued expressions of concern, PWGSC has now implemented a new series of consultation meetings, hosted by The Conference Board of Canada. These consultation meetings are another step in the process to obtain feedback and better understand the impact of the proposed procurement changes on businesses within the Furniture industry where there are potential major impacts on Canadian businesses. Continuation of the consultative process is necessary because suppliers have strong ideas about efficiencies and ways to achieve them; as well as insights around how they and the government can and should adjust to new practices and rules of engagement.

The Nature of Goods and Services Markets

Two factors have an important influence on the nature of change to government procurement: market power and market dependence. Both factors are relevant to understanding how procurement changes may affect or influence suppliers. These factors are defined below in relation to the context of the federal government.

Market power is the ability of the government to alter the market price of a good or service and other market conditions. It is an indication of how important government procurement is in the overall market for each category (i.e. the demand side).

Market dependence considers the issue of market structure from the suppliers' view (i.e. the supply side). In this context, it can be simply represented by the percent of a firm's sales attributable to the Government of Canada.

Change Management

Many firms today, operating in the procurement categories of temporary help services, informatics professional services, and furniture, count on the federal government for a high percentage of their sales. Firms that make a high proportion of their sales to the federal government are likely to be disproportionately affected, *regardless of their size,* as dependence on one large customer is ultimately reflected in the way a firm is organized (geographically, in its business processes etc.). As a result, they face an important change management challenge as the government changes its procurement policies and practices.

The government, too, faces a change management challenge since it seeks to significantly alter its procurement system while substantially maintaining its supplier base and ensuring that the well-being of SMEs and Aboriginal businesses are taken into account in the refinement of the particulars of change.

A Model of Change Management

The proposed changes to the way the federal government procures goods and services are designed to improve the efficiency and effectiveness of those expenditures, not eliminate them. It may be able to achieve its goals through several mechanisms:

- Using its market power and the market dependence of some suppliers to engineer price reductions.
- Improving economies of scale in purchases. This may save on procurement administration costs and create situations of discounting for volume.
- Changing the market structure through its purchasing practices to change economies of scale (through, for instance, consortia).
- Streamlining the purchasing process and thereby reduce transaction costs.

These savings have different effects on the overall market and the individual firms. It is possible to categorize some of the effects as follows:

- *Changes in market structure* that lead to a different structure of suppliers (in terms of size) and organization of suppliers. The risk here is that some suppliers will no longer be competitive within the new structure, especially in areas where market power and market dependence are high.
- *Changes in sales processes*. This may require that firms approach bidding with the government in new ways. This may involve restructuring sales processes, making greater use of consortia etc. The risk here is that bidding firms may incur costs to change their sales processes that they cannot afford or that act as a barrier to their future participation in the procurement system.
- *Lower profitability from individual sales*: To the extent that firms are induced to reduce prices for the same quality of sale, firms may find that the profit margin on their government business is reduced.

Recognizing these market dynamics, and the fact that the government is changing the way it procures goods and services, the federal government has essentially three options to act on:

1. *Let the marketplace manage the transformation*: make changes and let the marketplace sort through the implications. No firm is required to bid on government business. After the change in policies, the market will eventually find a new equilibrium. But the search for this equilibrium may impose costs on individual suppliers which hope to continue to sell into the federal government market.

2. *Actively manage the transformation*: in this approach, the federal government would explicitly put in place mechanisms to limit the impact of change on parts of the supplier community that are at greatest risk.

3. *Help the marketplace manage the transformation*: by virtue of entering into a dialogue with suppliers, the federal government is currently taking this route. If suppliers have enough advanced warning, and if their concerns about the efficiency of the bidding process is taken into consideration, it may be possible to achieve most of the savings through efficiency gains with a fairly minimal impact on individual firms.

Section B – Principles and Processes of Procurement Transformation at PWGSC

PWGSC's main goals for procurement change are to standardize what they buy and how they buy it, get better value for money, and simplify the way the federal government buys goods and services. The transformation being implemented to achieve these goals will affect virtually all aspects of PWGSC's procurement process. These adjustments will also affect the way PWGSC's client departments do business with goods and services suppliers, and the way suppliers do business with departments throughout the government.

PWGSC is very clear in its intentions. It is going to be a more demanding customer. It wants better value and prices for the goods and services it acquires. Currently, the government spends in excess of $1 billion a month on goods and services needed for its day-to-day operations.

A Purchaser of Goods and Services

As a central arm of the government, PWGSC is mandated to assist departments in the purchase of goods and services. PWGSC is not in a position, on its own, to invest in or support any particular group, sector or segment of the economy. Industrial policy and competitiveness strategies, for example, are overseen by other government departments and agencies with defined mandates in these areas. Thus, when the Government decides to take action (e.g., Aboriginal economic development), it chooses a department (such as Indian and Northern Affairs Canada (INAC)) to develop policy and run programs to help reach particular economic and social objectives. PWGSC then supports these departmentally-created policies and programs in its role as the Government's major purchaser of goods and services. Specifically, PWGSC:

- Helps client departments define their requirements and select effective procurement approaches. The Aboriginal Business Set-Aside Program is an example of such an approach.
- Manages the bidding process to find the best possible solution for sourcing client departmental needs to meet its policy and program goals.
- Supports client departments by overseeing supplier relationships after a contract is awarded to ensure accountability until close-out of the contract.[13]

PWGSC's Procurement Goals

Through its procurement changes, PWGSC plans to:

1. Achieve better value by improving the way government buys goods and services.
2. Offer fair, simple and open access to businesses interested in providing goods and services to government.

[13] The Acquisitions Branch at PWGSC also provides other services, including: market research to identify what products are available from suppliers; product planning; method-of-supply studies; the maintenance of a statistical data base and reporting capability; policy framework development; policy review and promulgation; and the technological infrastructure to support electronic procurement.

The Procurement Practices of PWGSC

To achieve these goals, PWGSC has established a set of twelve procurement practices that it will adhere to throughout the procurement change process:

1. ***Functionality Focus***. A focus on functionality (technical and supplier-based specifications) rather than brand specification for goods and services. This will allow suppliers to propose innovative products and solutions that meet the functional needs described

2. ***Fewer Models and Configurations***. Reduce the range of goods purchased—fewer models and configurations—while maintaining a reasonable amount of choice. For example, the choice in chairs will be reduced from approximately 2000 configurations to fewer than 100; and, temporary help services will no longer use hundreds of job codes but will align with standard government job codes.

3. ***More Bidding Opportunities****.* Give suppliers more opportunities to bid on Standing Offers by establishing sub-groups of goods and services within each procurement category. This will give interested suppliers an opportunity to compete for business in their area of expertise.

4. ***Value Factored into Evaluations***. Integrate quality-based criteria into the evaluation process and customer satisfaction reports into the bid-evaluation process (e.g., in professional services it is proposed that attributes such as a suppliers' experience, capabilities, and customer satisfaction scores will account for 70 per cent of total points awarded, whereas price will count for only 30 per cent).

5. ***More Active and Systematic Price Competitions***. Take a more active and systematic approach to price competitions, tailored to the specific nature of goods or services (e.g., price competitions for notebooks will continue on a quarterly basis).

6. ***Ensure Supply Continuity***. To insure that an appropriate and adequate supply of qualified suppliers is available, the government will always seek to select an optimal number of suppliers. For example, informatics professional services business will be awarded to several firms on a regional basis.

7. ***Local and Operational Support Requirements***. A mandatory provision to ensure government operations in every region have access to adequate local support networks, tailored to each good or service. For example, temporary help services and informatics professional services business will be awarded by region, with multiple firms in each region.

8. ***Open and Fair Competitions***. A more open and fair competition system that makes it easier and less costly for suppliers to bid will ensure a more level playing field. For example, simplified language in bid documents and contracts will make it easier to bid; and testing of furniture will be performed after successful award of business rather than as a requirement to bid.

9. ***Easier Access to Government Business***. To make it easier to compete and conduct business with the Government, small firms will be given tools and advice to help them

construct consortia to make joint bids. Bids from these consortia of small firms will be treated equally to bids from large firms.

10. ***Higher Probability of Business to Winners of Competitions***. Suppliers who win competitions will be guaranteed business. The Government will channel purchases and business to qualified suppliers and ensure that they benefit from their successful Standing Offer bids. For example, currently there are more than 40 furniture suppliers holding standing offers, yet nearly half of the government's furniture purchases are made outside of the Standing Offers.

11. ***Faster Execution of Orders***. Using standing offers will result in procurements being done in 1-4 days rather than the current 30-60 days.

12. ***More Informed Decisions***. Using electronic tools to give detailed information on who buys what, when, at what price, and from whom will assist the government in understanding how it procures better and help it negotiate better value for Canadians.

Strategies for Promoting Open and Transparent Access for SMEs

PWGSC intends to give SMEs equal opportunity to compete for government business, and has taken a number of steps to address this:[14]

- Where small businesses are too small to bid on government business on their own, PWGSC has made it easier for them to form partnerships and joint ventures.
- Where appropriate, within each category of goods and services, PWGSC has divided the total requirement into a number of sub-categories, allowing firms to bid on these individual categories rather than on the whole requirement. Where appropriate, PWGSC has divided the requirement into regional categories giving regionally-based firms an opportunity to bid on smaller portions of business.
- Where practicable, PWGSC insists that local installation and support be provided. This ensures that a national supplier will provide adequate levels of service to meet the full range of needs of clients in a timely fashion. It also helps to ensure that small local businesses that provide local distribution and support are able to win their share of contracts.

Office of Small and Medium Enterprise (OSME)

Created in 2005, the OSME held consultations across the country to hear the concerns of SMEs. Directors have been appointed across the country to help SMEs access government business. To date, the OSME has already had an impact in how new procurement contracts are worded and how requirements are stated.

Regional Impacts

PWGSC is competing approximately 30 separate standing offers, the majority of which have sub-categories, thereby multiplying the number of opportunities for suppliers to compete. PWGSC is also ensuring that government operations in every region have access to proper support networks—tailored to each good and service. For example, printer manufacturers must have local service and installation offices (usually performed by local SME resellers and service firms) within 100 kilometers of every urban centre having a population of more than 30,000 people.

Focus on Industry Sectors

Procurement teams are now organized into industry sectors giving them a better understanding of the sector from which they are buying (e.g., who the major suppliers are, and the role of distributors and sub-contractors—typically SMEs—within the supply chain network).

[14] To date, this approach has produced a number of positive results. For example: as part of a relocation services contract with a major real estate agent, some $57 million was spent on small and medium enterprises (SMEs) who provided specific relocation services under the contract. From: PWGSC – Way Forward Procurement: Strategies for promoting open transparent access for Small and Medium Enterprises.

Strategies for Promoting Open and Transparent Access for Small and Medium Enterprises (SMEs) (continued)

Specification of Needs

By adopting an outcome-based or functional-based specification approach to what it needs, SMEs are given the opportunity to propose new and innovative products that may not have been tried before.

Simple Language

PWGSC is working on a major language simplification program that will simplify the clauses required to understand what the government is looking for. This will be of particular benefit to many SMEs.

Easier Access

PWSGC is working with the Treasury Board Secretariat to overhaul the policies governing procurement. In the meantime, it is free for SMEs to access MERX—the government's on-line system for publishing bids. Small professional service providers can also register on an on-line system and gain access to client department assignments.

Making Standing Offers Meaningful

Standing Offers have been made mandatory to use for the ten most commonly purchased goods and services. This ensures that a firm that wins a Standing Offer can expect to get business.

Industrial strategy

PWGSC serves Canadians within the limits of its mandate. PWGSC does not have the mandate to act as a venture capital firm, an investment banker, or in picking and choosing which industries to invest in. The government as a whole has specialized departments that look after the health of the economy (e.g., Finance, Industry Canada, International Trade, and the Export Development Bank) and these departments have specific programs that help Canada reach its economic objectives.

Section C – Overview of Office Furniture - Prepared by PWGSC

Overview

This section presents the proposed procurement strategy for furniture.

The Government of Canada is streamlining and transforming the way it buys office furniture. This new approach will provide better value and accountability for Canadian taxpayers.

The proposed procurement strategy was developed in close consultation with departments and agencies, with input from discussions held with furniture suppliers and manufacturers on June 8, 2006, and by benchmarking government procurement practices and pricing. PWGSC has also reviewed data from the call-ups placed on the current National Master Standing Offers in developing our proposal. Examples include: looking at the volume and value of orders within furniture categories; and, the distribution of business volume amongst suppliers.

The Government of Canada spends approximately $138 million a year on furniture.

Current Context

The current system makes it difficult to identify the best value because of several factors. For example, there are currently more than 2,000 configurations of chairs available for departments and agencies to purchase.

All suppliers providing technically compliant products and who meet mandatory conditions are issued a Standing Offer. Suppliers can add new products at any time and can review their prices periodically.

Currently, there are 52 suppliers holding 114 standing offers for office furniture, but there are more than 8,000 vendors selling office furniture to the government, some of which are dealers of the manufacturers. At least 50 per cent of purchases are made outside of the Standing Offers, and requests for volume discounts (RVDs) on individual orders are rarely used. The business volume of the various Standing Offer holders varies considerably; with 11 suppliers accounting for 80% of the business.

A heavy administrative burden is placed on PWGSC, in managing the large number of products and the required periodic price updates for new and existing NMSO products.

Purchase descriptions and CGSB standards are very generic and define a minimum standard resulting in a multitude of products and configurations on Standing Offers. While price competitions should take place at time of ordering, a review of the call-ups has shown that the lowest priced item is not always chosen.

For departments and agencies, it is difficult to identify which products are most appropriate for their requirements, and they are often left to rely on recommendations from specific dealers. When placing orders, departments and agencies are instructed to purchase the lowest priced items, but may use a variety of mechanisms to actually procure furniture. These include:

- Non-competitive orders on the National Master Standing Offers (NMSO) can be made up to $25,000 for all sub-commodities;
- For orders above the $25,000 limit, a competitive process is employed using the e-procurement tool with the upper limit dependent upon the sub-commodity (varies from $75,000 for office seating to $400,000 for panels);
- Orders above the call-up limitation are competed amongst all NSMO holders by the Furniture procurement division as RVDs; and,
- Larger projects are competed individually with requests for proposals on MERX.

The government is introducing the following improvements to the procurement process for furniture:

- ✓ **Reducing** the number of products and configurations on Standing Offer with a focus on **high usage items** meeting government standards and requirements.
- ✓ Concentration of market on **established government needs**.
- ✓ Increased opportunities for **Aboriginal** businesses.
- ✓ Minimal impact on current **SME** vendor base.
- ✓ **Level playing field** for small and medium sized businesses.
- ✓ Increasing the fairness and transparency of the process with firm prices, and different call-up limitations for **price competitive** products.
- ✓ Reducing **administrative burden** required to maintain the existing system with several different series of products and periodic price revisions.
- ✓ **Lowering bidding costs** to suppliers by reducing the series that need to be tested, along with a grandfathering feature allowing usage of existing test data.
- ✓ **Streamlined** purchasing processes resulting in administrative savings.
- ✓ **Lower cost** based on total government business volume.

The New Procurement Approach for Office Furniture

The new procurement strategy will continue to emphasize **functional** specifications. Functional product descriptions for office furniture use CGSB standards or government purchase descriptions. There are no brand name products specified.

There will be **fewer models, configurations and series**. PWSGC has reviewed the call-ups on Standing Offers and has found a considerable number of products listed that are not ordered. As a result, PWGSC is adjusting item descriptions to allow only those that are required. For example, the choice in chairs will go from over 2,000 configurations to fewer than 100. Other products will be handled on an exception basis, with justification, outside the Standing Offers.

In order to **increase bidding opportunities**, PWGSC has divided the furniture commodity into five sub-commodities, with awards being made to both manufacturers and Aboriginal firms. Some manufacturers, who may not produce furniture in all sub-commodities, will continue to have an opportunity to bid on a level playing field with other larger companies.

1) *Clients' Access*

Based on their requirements, departments and agencies will have access to suppliers through one of following procurement vehicles:

E-procurement (GoCM or SAGE)	***Requests for Volume Discounts***	***Standalone Request for Proposals posted on MERX***
✓ Small orders can be placed for a wide range of items up to the call up limitation for the sub-commodity ✓ Above sub-commodity specific thresholds, (e.g. $5K for seating) only the lowest priced product will be available to order ✓ Companies will be allowed one series per sub-commodity	✓ For orders above the call-up limitation ✓ Will be competed amongst all standing offer holders	✓ Specific project work

Note: this document does not address stand-alone Request for Proposals.

The Procurement Process

All manufacturers will be invited to submit a proposal to the revised NMSOs via MERX, and will be limited to a single series per sub-commodity. The mandatory requirements for the five sub-commodities are virtually the same; the only difference is that some sub-commodities are not supported by a CGSB National Standard; in those cases a Government Specification is used.

The RFSOs mandatory requirements will address (but may not be limited to) such issues as:

- Evidence of financial stability.
- Cross-Canada coverage, service, support and delivery of items.
- Delivery methods.
- Product documentation in both official languages.
- Billing and data provision requirements e.g. provide regular spend analysis reports at appropriate level of detail.
- Ability to provide all items within a specific sub-commodity or group.
- Meeting defined specification criteria and appropriate standards.
- Meeting defined standard warranty provision.
- Ability to receive payment by acquisition card within certain limits.
- Agreement to fixed pricing over a 2 year period of the NMSO.
- Environmental and sustainability criteria.
- Testing requirements. Successful bidders will have to provide appropriate testing data. If data is already available it may be grandfathered for up to 6 months.
- The supplier must identify Aboriginal dealers in each of the regions.
- FOB (Free on Board) Destination prices must be provided for the following key cities: NCR, Montreal, Toronto, Vancouver, and Halifax.

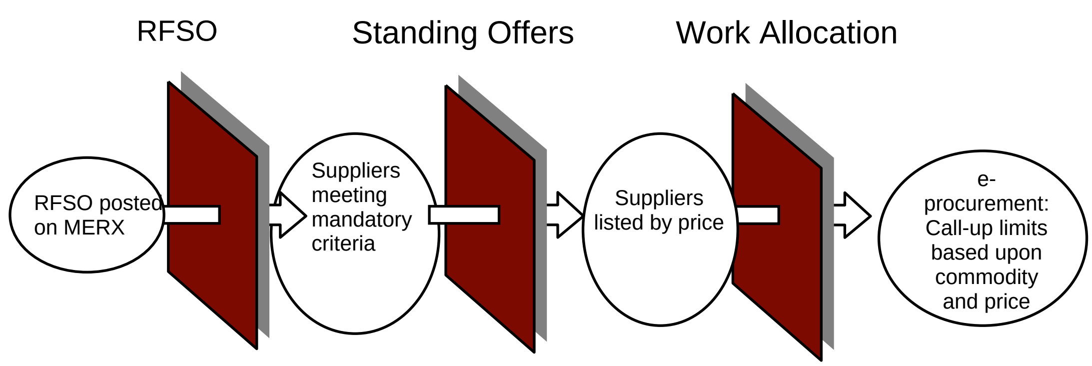
Value will be factored into evaluation. Suppliers will be requested to provide all four cost components for all items in a group or sub-commodity (unit price, installation cost, delivery cost, and volume discount). The items in a group or sub-commodity constitute a market basket of goods that represent the majority of the spend for that group, as determined by analysis of annual NMSO call up data for Office Furniture.

Suppliers will be asked to provide volume discounts in the form of per cent discounts (off the complete price including installation and delivery) for differing order sizes (as measured by the $ spend) that reflect the typical order sizes of the Government of Canada. An average per cent discount across all order sizes will be used in the evaluation calculation.

If data is available, each item's price in a group or sub-commodity will be weighted according to its annual usage. In the absence of any appropriate data, each item's price will be weighted equally.

Prices will be firm for a period of two years. This will also provide greater transparency, reduce the administrative burden both for government and the suppliers and enable better management of the government NMSO products.

Diagram 1: Supplier Screening Process



PWGSC is adopting more **competitive pricing** in its approach to furniture, proposing that manufacturers provide unbundled pricing for four key cost elements: unit price, installation cost, delivery cost and volume discount. The lowest priced products will be given a higher call up limitation that will allow a simpler implementation of small fit-up projects, while alternate higher priced products will have lower call-up limitations—providing price transparency and an incentive for clients to order lowest priced items, while allowing flexibility in ordering small quantities or other products for reasons of compatibility with existing installations.

In order to ensure **local and operational requirements**, bidders will be required to meet mandatory conditions such as: provide local sales coverage across Canada, provide delivery and installation services at client locations and advisory support on the product range offered, and, identify an Aboriginal dealer to service each of the regions.

In order to ensure a **level competitive playing field and open, fair competitions**, testing for furniture will be performed after successful award of business rather than as a requirement to bid, and testing will be conducted on far fewer models and series. Standing Offers with

Aboriginal dealers will be negotiated on the services components such as delivery and installation.

More business for suppliers who win competitions. All suppliers meeting the mandatory criteria stated in the RFSO will receive Standing Offers. The lowest priced suppliers will get a significant volume of government business. The Standing Offers for office furniture have been mandatory since April 1, 2005. Significantly more business is flowing through the Standing Offers since this policy change.

Departments and agencies will also benefit from a **faster execution of orders**, because they will be presented with a rationalized product and series choice, listed in order of price. This will simplify the ordering process. Furthermore, they will only be able to order the lowest priced items for larger orders. For suppliers, this will also make government business more transparent as they will only have one of their series which may be ordered.

Information for better decisions. Within the RFSO, suppliers will be provided with business volume estimates derived from past NMSO call-ups, within each product category, allowing suppliers to make better pricing decisions as well as plan production or order flow, based upon past government ordering patterns. PWGSC will review information from NMSO reports to ascertain business volume and identify any ordering patterns that would require adjustment of the strategy. The NMSOs will be valid for a period of two years, following which the strategy will be reviewed in order to address any emerging issues and incorporate improvements.

Feedback Sought

PWGSC seeks feedback on the new procurement instruments for furniture, more specifically:

- Structure of the proposed procurement instruments.
- Furniture management issues (ie. year-end spending).
- Standardization of products.
- Use of CGSB standards or other standards recommended by the industry.
- Other ideas to reduce cost to suppliers and the Government of Canada.

Section D – Furniture Data Analysis

Macro Analysis of Market Power

Defining the Industry

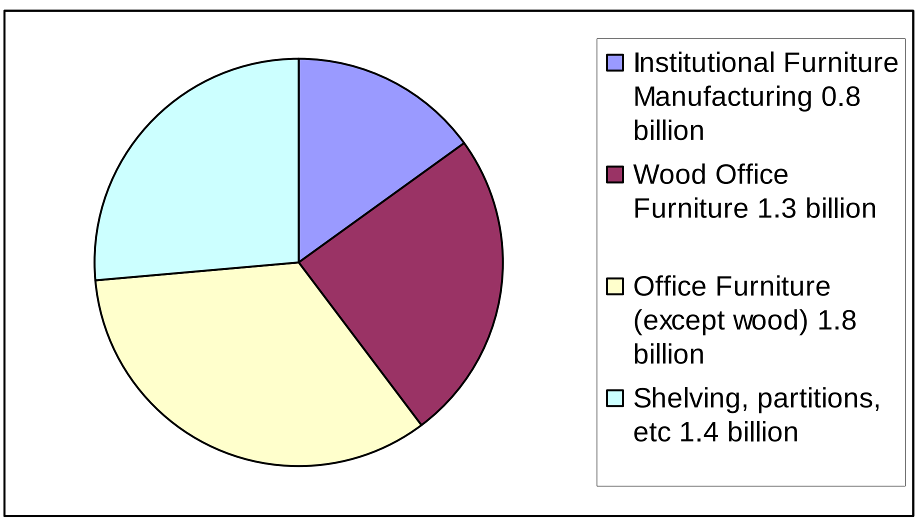
The NAICS code 3372 is the best approximation for our procurement category of furniture. It includes office furniture manufacturing except wood (code 337214) and wood office furniture (code 337213). Although wood office furniture largely consists of up-market products, like executive desks, that the government would rarely purchase, it was considered part of the core industry and thus included in the analysis. Showcases, partitions, shelving and locker manufacturing (code 337215) are also included in 3372 and were also included in the analysis since the government spends considerable amounts on these and other similar items. Institutional furniture manufacturing (code 337127) was also included due to the particular nature of government office space and the spending involved.

With this definition in mind, this section of the report will speak of the industry as the office and institutional manufacturing industry. Appendix A, below, provides a detailed description of the Data Analysis Methodology used.

Defining the Market I: Output and Sales

The 2003 domestic production for office and institutional furniture was valued at $5.2 billion. Of this production, 26 per cent was shelving, partitions and other office systems and 15 per cent was institutional furniture. A full 60 per cent was for office furniture. Of the $3.1 billion of production of office furniture, some 40 per cent was wood office furniture.[15] (See Chart 1) In 2003, Canadians purchased $3.9 billion in office and institutional furniture.

Chart 1: Breakdown of Office and Institutional Furniture Production



Source: Statistics Canada Annual Survey of Manufacturers, 2003

[15] Statistics Canada, *Annual Survey of Manufacturers*, 2003

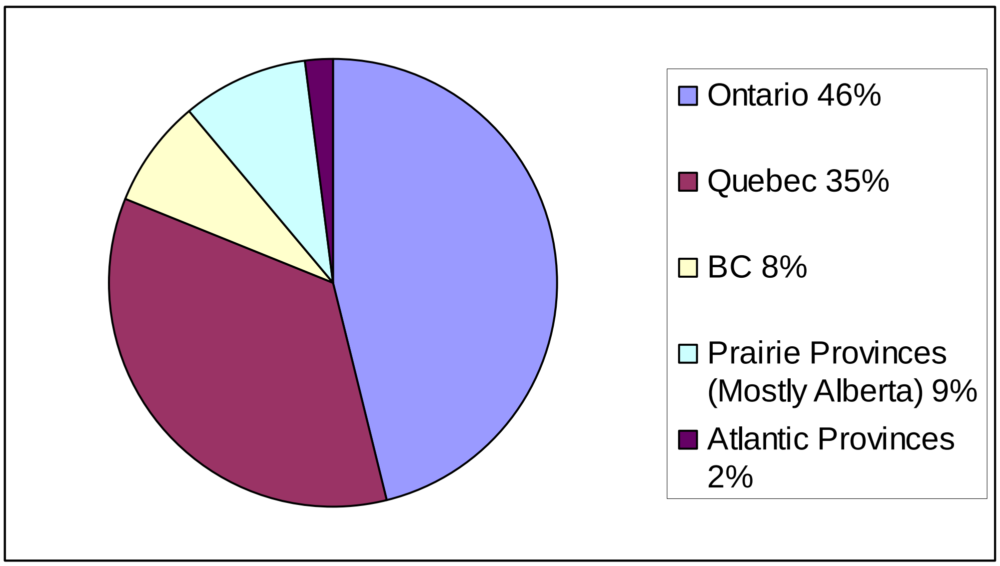
Defining the Market II: Geographic Dispersion of Output and Sales

Canadian firms produced $5.2 billion and exported $3.7 billion in 2003. Almost all of the exports were destined for the United States. So far, selling Canadian-made office and institutional furniture to the American market has not been significantly affected by the rising Canadian dollar.

The remaining $1.5 billion of Canadian production was sold in Canada. Approximately 40 to 50 percent of the Canadian marketplace is served by domestic manufacturers, while the remainder is served by international ones.

Currently the institutional and office furniture industry employs thousands of workers across the country. The industry however is clustered mainly around the Greater Toronto Area (GTA) and Montreal. (See Chart 2)

Chart 2: Location of Canadian Office and Institutional Furniture Manufacturers



Source: U.S. Commercial Service and U.S. Department of State*, International Sector Analysis Report* – March 2006 Canadian Office/Institutional Furniture Market

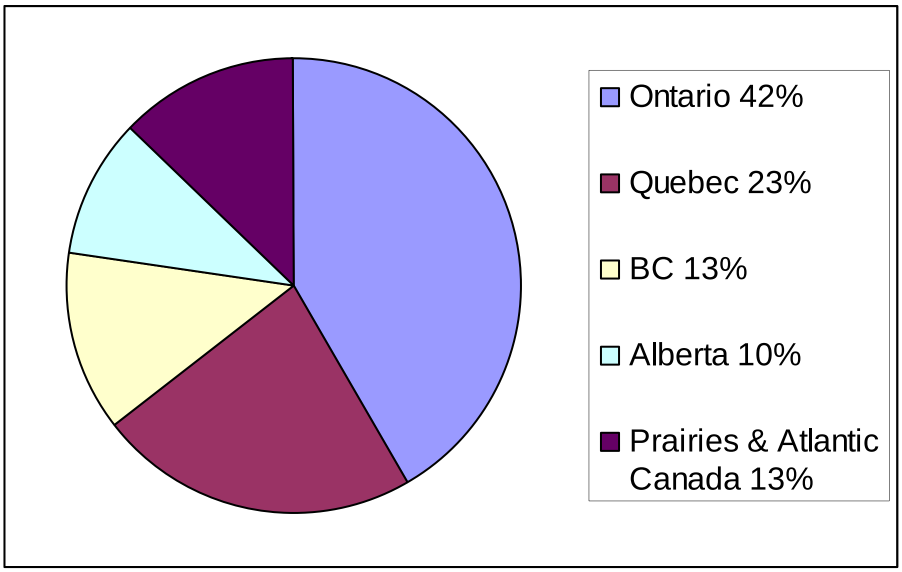
A large proportion of the larger manufacturers are based in the GTA. For instance, one of Canada's leading manufacturers is based in Downsview, in the northern part of the GTA. It employs approximately 4,500 people (though not all at its main location). Another leading manufacturer is based in North York, Ontario, also within the GTA. This company employs 3,700 people, mostly in the GTA area. Thus the dispersion of furniture employment in Canada is likely even more focused on Ontario than the dispersion of firms. Our estimates show perhaps two thirds or more of Canadian workers in the industry are employed in Ontario.

Like many industries, furniture manufacturers rely on a distribution network to deliver their goods to market. Most large and medium-sized furniture manufacturers rely on a system of wholesalers and dealers who operate locally across Canada. It allows them to market their products through showrooms on the other side of the country from where they manufacture it. In this way, large Ontario and Quebec manufacturers are able to maintain their presence at the national level. Although a large buyer may purchase furniture directly from the large and medium-sized manufacturers, buyers typically obtain actual delivery from local or regional dealers.

Small furniture manufacturers may not have access to such wide-ranging dealer networks. Often they must act as their own sales and distribution agents. As a result, while many of these small manufacturers have been quite successful in serving a local clientele, it is harder for them to maintain a national presence.

The demand for office and institutional furniture loosely follows the geographical distribution of the Canadian population. Ontario is home to about 39 per cent of Canadians and consumes about 42 per cent of office furniture. Quebec is home to 23 per cent of output and consumes a matching 23 per cent of furniture products.[16] (See Chart 3)

Chart 3: Demand for Office Furniture by Region



Source Research and Markets: Canadian Demand for Office Furniture and Trends 8th Edition, 2004

Not surprisingly, the office and institutional furniture market is concentrated in Canada's largest cities. About two-thirds of Canada's market is found in its ten largest metropolitan areas. The City of Toronto alone, not including the rest of the GTA, accounts for 21 per cent of the national market. Other significant portions of the domestic market are found in Montreal, Vancouver and Ottawa-Gatineau (also known as the NCR). [17]

Clearly the furniture industry is mainly organized around continental production complemented by regional and local distribution. As a result, the industry should be less reliant on domestic purchasers in general, and on the Government of Canada in particular.

Market Power of the Government of Canada

The Government of Canada spent about $138 million on office and institutional furniture in 2005-06, which amounts to about between 3 and 4 per cent of domestic sales. Although the

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[16] Research and Markets: *Canadian Demand for Office Furniture and Trends 8th Edition*, 2004
[17] Research and Markets: *Canadian Demand for Office Furniture and Trends 8th Edition*, 2004; Population figures based on Statistics Canada estimates

Government of Canada is a large purchaser, it has limited market share and market power in both the Canadian domestic market and the broader continental market.

As a result of procurement changes, the Government of Canada is not planning to purchase less furniture; it seeks to reform *the way* it undertakes purchases. Given the nature of the market as a whole, these changes would likely have little impact on the *overall* levels of output and sales or on the *structure* of the domestic industry.

Micro Analysis of Market Dependence

Notwithstanding our assessment that the Government of Canada's overall market power is limited in the furniture procurement category, there may still be firms that might be exposed to significant adjustment risk through changes in procurement policies and practices. These firms are the ones that currently obtain a relatively large percentage of their sales from the Government. We expect that these firms are most likely small and medium sized manufacturers and dealers.

In order to better understand the nature of the Government of Canada submarket, we conducted an analysis of government purchases in fiscal 2005-06.

The Government of Canada is one of the largest users of office space in Canada. PWGSC is responsible for the stewardship of a real estate portfolio of over 300 government buildings worth $7 billion. It is also responsible for some 2100 leases valued at around $800 million. The government needs to furnish some 6.7 million square metres of space serving 210,000 public servants.[18]

Some $62 million of the $138 million (about 45 per cent) of government purchases were through standing offers. Another $47 million were specific "non-addressable" expenditures for which standing offers are not used. The remaining $29 million was spent outside the standing offer framework. [19] Government officers sometimes go outside the existing standing offer system when they feel that the products available through standing offers do not meet their specific needs in a timely fashion.

Although purchases using standing offers are not the only method by which goods and services are procured, the quality of data resulting from purchases through standing offers is far more detailed and reliable than data for other types of purchase. Because of this data quality issue, where ever possible, data from standing offers is used to explore the overall issue of market dependence even though it actually accounts for slightly less than half of total government furniture expenditures.

Aboriginal Business Set-Asides

A key element of the furniture procurement strategy is opportunities for Aboriginal businesses. This is currently handled via a specific Aboriginal 'set-aside'. Most standing offers are made with the manufacturers rather than the dealers. The exception is for Aboriginal dealers. Furniture may be purchased through standing offers with Aboriginal dealers so that the monies spent can count towards departmental goals of Aboriginal set-asides.

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[18] PWGSC Real Property Fact Sheet <http://www.pwgsc.gc.ca/text/factsheets/real_property-e.html>
[19] Data obtained from PWGSC

As a result, the standing offer data does list some dealers as well as manufacturers. Of the $62 million spent through standing offers in 2005-2006, $9.5 million, or about 15 per cent were through Aboriginal dealer standing offers. Most of the Aboriginal dealers handle the products of the large manufacturers, so it is likely that much of the $9.5 million that went through Aboriginal dealers' standing offers was actually for products from the largest producers.[20]

Size of Suppliers

Although some large producers dominate the marketplace, there are still a considerable number of small and medium size vendors of furniture to the Government of Canada. Of the 47 Canadian "active" manufacturers in 2005[21], only six were large firms with 500 or more employees. The vast majority, 41, were small and medium sized manufacturers.[22]

Of the $62 million spent through standing offers in 2005-2006, $12.2 million was spent on SMEs. This equates to nearly 20 per cent. About half of the funds were spent on seating. SMEs seem to compete quite well on selling 'seating': the amount spent on seating is evenly split between large suppliers and SMEs. SMEs also compete quite successfully on free-standing systems.

Large suppliers account for $40.2 million in direct spending, plus much of the remaining $9.2 million in spending through the Aboriginal dealer standing offers. Panels are an important product for large suppliers to the government market: they account for about half of the spending with large suppliers.

Top Suppliers

Identifying the amounts spent of the $138 million on the top *suppliers* is a complicated exercise. The record of purchase often includes the name of the dealer that delivered the furniture but not the manufacturer's name. This is further complicated since some dealers provide furniture from multiple manufacturers. It becomes difficult to follow the chain of purchase from the government purchaser through the dealer and wholesaler network to the actual manufacturer. Finally, the data is based on spending reports that sometimes contain errors in the classifications of spending. (This is a problem discussed earlier in relation to the challenges of aligning government purchases with specific industries).

An illustrative example is the case of a major Aboriginal dealer with government sales over $2 million, who offers both Teknion and Global products. It is unclear how much of the government's purchases are for Teknion furniture, and how much for Global. Since there are many cases like this, it is difficult to determine exactly how much each *manufacturer* actually receives as their portion of the millions of dollars in furniture procurement spent with dealers.

Although the exact amounts spent on the top manufacturers are hard to discern, it is possible to get a reasonable sense of which suppliers sell the most to the Canadian Government. Of the top twenty suppliers, twelve are listed as dealers, eight are listed as manufacturers. The top 20 suppliers account for $64 million of the $138 million, or 47 per cent of total government expenditure on furniture in 2005. Of that $64 million, $38.3 million can be directly attributed to

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[20] Data obtained from PWGSC
[21] Active means that they had an existing contract, amended a contract or obtained a new contract and supplied furniture to the government under the terms of their contractual agreement.
[22] Data obtained from PWGSC

the eight top manufacturers. For instance Teknion sold $17.8 million to government last year, *plus* whatever was sold to government through their dealers. The amounts listed below (See Table 1) then can be considered minimums for manufacturers, with the complete total sales as yet unknown. [23]

Table 1: Top Furniture Manufacturers Supplying to Government of Canada

Manufacturer	Government of Canada Expenditures $ millions	Location
Teknion	17.8	**Ontario**
Global Upholstery	9.2	**Ontario**
Teknion Roy & Breton	3.9	**Quebec**
Pitney Bowes	2.5	**National (based in Ontario)**
Allseating	1.6	**Ontario**
Haworth	1.3	**Alberta (Canadian branch of large US company)**
Dasco Data Products	1.0	**Ontario**
Steelcase	1.0	**Ontario (Canadian branch of large US company)**
Total	**38.3**	

Source: Conference Board of Canada, based on PWGSC data.

Although the distribution of procurement corresponding to the full government expenditure of $138 million is problematic, the amounts spent through standing offers are easier to analyze. Of the $62 million spent through standing offers in 2005-2006, $47 million, almost 76 per cent, went to the top ten suppliers.[24] (See Table 2)

[23] Data obtained from PWGSC
[24] Data obtained from PWGSC

Table 2: Top Standing Offer Suppliers of Furniture to Government of Canada – Manufacturers and Dealers

Supplier	M = Manufacturer D = Dealer	GOC expenditure	Location
Teknion	M	$12.8 million	Ontario
Global Upholstery	M	$8.8 million	Ontario
Adirondack Technologies	D	$5.1 million	Ontario
Herman Miller Canada Inc.	M	$4.7 million	United States
Teknion Roy & Breton	M	$3.6 million	Quebec
Haworth Ltd.	M	$3.0 million	Alberta (Canadian branch of large US company)
Steelcase Canada	M	$2.7 million	Ontario (Canadian branch of large US company)
Allseating Corporation	M	$2.5 million	Ontario
Inline Systems Next Wood	M	$2.1 million	Ontario
Artoplex Plus	M	$2.1 million	Quebec

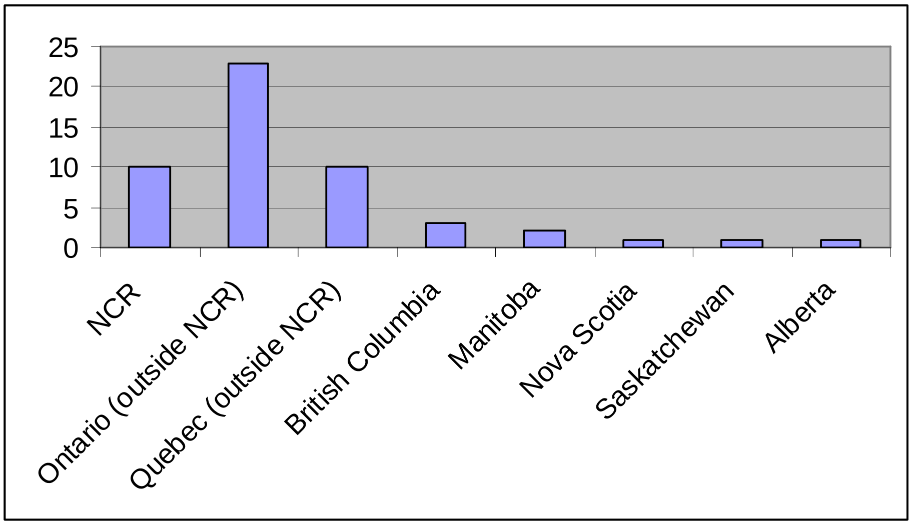
Source: The Conference Board of Canada using data obtained from PWGSC

Geographic Distribution of Manufacturers

In 2005, PWGSC awarded contracts or amended contracts for furniture from 46 manufacturers in seven of the ten provinces.[25] The only provinces where PWGSC did not give or amend a contract was New Brunswick, Prince Edward Island and Newfoundland. As one would expect, the largest share of these firms are in Ontario, and to a lesser degree, Quebec. Ten of these manufacturers are in the NCR. Although this is not a small proportion of these manufacturers, the Government of Canada's furniture procurement does not appear to be overly focused on the NCR. (See Chart 4)

[25] These were firms that PWGSC awarded a contract to, or amended a contract in the 2005 calendar year. This analysis excludes the contracts awarded or amended by other government departments.

Chart 4: Number of Manufacturers with a New Contract or an Amended Contract in 2005 by Province/NCR

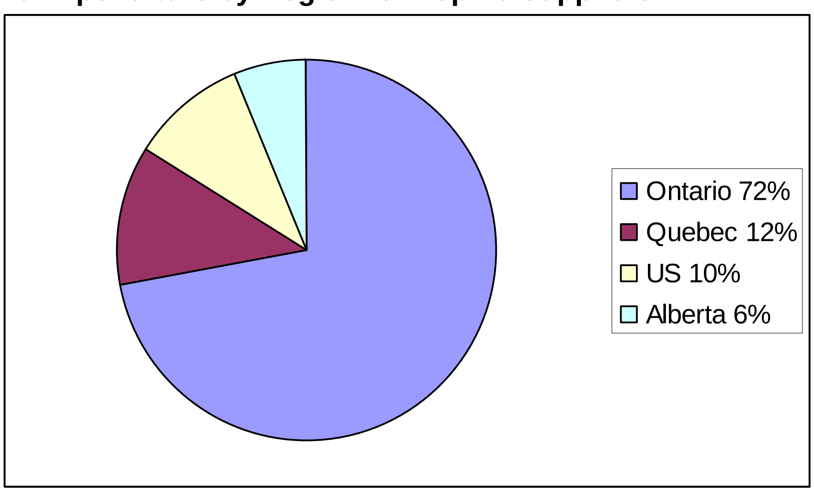


Source: The Conference Board of Canada using data obtained from PWGSC
Note: Some manufacturers are active in multiple provinces and therefore are counted more than once.

Geographic Nature of Standing Offer Spending

A review of the top ten vendors (which includes manufacturers and at least one Aboriginal dealer) reveals more spending with Ontario-based firms. It is likely that the true picture—incorporating all suppliers and not just the top ten—would show more spending on regions outside Ontario. However, given that 46 per cent of all office and institutional furniture producers are in Ontario, and those include many of the largest, it is perhaps not surprising to see Ontario so dominant in this regard. (See Chart 5)

Chart 5: Furniture Expenditure by Region for Top-10 Suppliers



Source: The Conference Board of Canada using data obtained from PWGSC.

A number of the top suppliers are American-based companies. Some of these companies appear to import their goods from production facilities in the United States—Herman Miller for instance. Other American companies have factories in Canada. Steelcase, for instance, has a manufacturing facility in Markham, Ontario. Just how much of the furniture that the Government of Canada purchases from American-based producers is made in Canada is not known at this time. For the purposes of this analysis, it is assumed that all of the furniture bought from these producers is made in their Canadian plants. This may overestimate the proportion of furniture made in Ontario and Alberta, while underestimating the proportion made in the United States.

Assessment of Market Dependence

The procurement change plan will alter how the Government buys furniture and what it buys. This has differing implications for large versus SME manufacturers.

Some manufacturers are significantly dependent on the Government of Canada expenditures. For others, the government business is not fundamental to their financial stability. One large Toronto based manufacturer, for instance, sells about $20 million a year to the Government of Canada, a sizable sum to be sure. That manufacturer's 2005 total revenues, however, were $401 million dollars.[26] Thus the Government of Canada's procurement purchases represent only five per cent of the manufacturer's sales. These revenues, then, are important, but probably not critical to the survival of this large, continentally integrated firm. The same conclusion can also be drawn for other large vendors to the government.

Some SME manufacturers appear to be significantly dependent on their business with the Government of Canada. For instance, one Ontario based manufacturer has annual revenues in the $5 million to $10 million range.[27] The Government of Canada purchased just under $1 million from this manufacturer in 2005, accounting for between 10 per cent and 20 per cent of its total revenues.

Differences in market dependence mean that changes in the procurement process are likely to be much more important to small dependent vendors for two reasons. First, the size of the government's purchases makes them a very significant part of total sales. If procurement rules alter to effectively exclude SME manufacturers from government business, their sales to non-government customers would have to grow or the consequences could be very severe. Second, if changes in government procurement processes increase the cost of doing business, SME firms have a smaller operational scale over which to spread these costs.

Aboriginal dealers, who are heavily dependent on government sales, are unlikely to suffer much due to procurement changes. Although they may be dependent, the impact of change is mitigated by the Aboriginal Business Set-Aside Program which PWGSC plans to continue to support.

The market dependence issue is most likely to affect small and medium-sized firms where the Government of Canada constitutes a large share of the firms' sales. However, in many instances, it is very difficult to ascertain which manufacturers and dealers are most affected. Most of these vendors are private, incorporated companies and therefore not obliged to release financial data so that it is difficult to get accurate information on their total sales. As a result, it is very difficult to assess the overall or aggregate impact of market dependence on many of the supplier firms.

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[26] Teknion 2005 Annual Report
[27] Data available from Strategis Canada

Section E – Office Furniture: Planned Changes, Issues and Perceptions

Suppliers' views have been sought in a variety of ways by PWGSC as it has been going through the process of developing its procurement reform plans. The department has attempted to incorporate some suggestions from individual suppliers and industry associations into its plans. As a result, alterations and refinements to the planned changes in procurement have already been made.

The federal government believes that its current furniture procurement approach limits the way it can do business and causes a number of unintended consequences.

Furniture procurement issues facing PWGSC and client departments include:

1. Current National Mandatory Standing Offers (NMSOs) are established with *all technically compliant* suppliers regardless of their pricing structures.
2. Current price competitions occur only at order-time and only with individual departmental transactions.
3. Current Request for Volume Discounts (RVDs) encourages departments to aggregate their transactions for volume purchases (not government-wide).

The unanticipated consequences include:

1. The sales and marketing efforts of suppliers are driving increased spend with these suppliers.
2. Rather than focusing on 'best value' departmental clients are selecting furniture based on a number of other mitigating factors such as brand loyalty, aesthetics and supplier-client relations.
3. The Request for Volume Discount (RVD) mechanism currently in place has limited impact as purchasing is done in small lots, and the government cannot leverage its government-wide annual purchase volume.

Supplier Consultations

In June 2006, PWGSC met with over 80 furniture suppliers—including representatives from current NMSO holding firms and off-NMSO vendors) to inform them of a proposed new procurement strategy. Informal meetings of the Office of Small and Medium Enterprises (OSME) and the Assistant Deputy Minister, PWGSC, with Aboriginal and SME vendors were also held. The new furniture procurement strategy was met with significant resistance by suppliers. Concerns included that there was a lack of consultation and collaboration with industry in the development of the new strategy; that the proposed consolidation reforms would result in manufacturers going out of business (particularly SMEs); and that Aboriginal businesses could potentially lose their set-asides. Client departments also had some concerns about product compatibility issues, savings, and procurement processes.

Supplier input through individual and coordinated messages to the government, along with an internal government review and assessment, prompted a re-evaluation of the proposed furniture procurement strategy.

The Way Forward: Furniture Procurement

The proposed furniture procurement strategy focuses on best price evaluation and specification rationalization. The federal government believes that its new furniture procurement strategy will help manage better the way it procures by using a 'best value' approach and overcome the inherent weakness of the current system which treats government furniture spending as a series of large un-related transactions (leading to higher costs, the proliferation of specifications, a dispersed vendor base, compatibility issues, and a lack of inventory control). The goal is to strike a balance between product variety and volume consolidation.

Specifically the Government of Canada's furniture procurement strategy and National Mandatory Standing Offers (NMSOs) are intended to:

- achieve savings;
- enable SMEs to participate on a level playing field;
- maintain Aboriginal set-asides;
- ensure that client departments have an accessible supply of furniture; and
- provide a more targeted range of products that meet customer needs.

To achieve these objectives PWGSC is focusing on two key levers: a rationalization of product specifications; and optimized bid evaluations.

Caveat

The issues and perceptions presented below provide a snapshot of the views and perceptions of individual suppliers and/or individuals within client departments. They are not necessarily reflective of the industry or a government department as a whole. As well, in some instances, the supplier or individual within a client department may not be aware of the most current proposed procurement strategy. Consequently, their issues may have already been addressed by PWGSC through its procurement transformation strategy. For instance, the government has recently announced that Reverse Auctions will no longer be part of its procurement strategy.

Objective 1: Achieve Savings

Proposed Strategy to Achieve Savings:

To achieve annual savings, two key levers will be used:

1. *Best Price Evaluation*:
    - For new fit-up panel systems only, price competition will be employed using a strict product and service definition for a like-for-like price comparison. The price evaluation will be based on total cost, comprising four key cost elements: unit price, installation cost, delivery cost, and volume discount. Technically compliant products will be evaluated on a price basis, and the lowest responsive price within each category will have a higher call up limitation than other standing offer items.

- For all sub-commodities, prices will be un-bundled by requesting cost breakdown for all cost components (e.g., delivery, installation, design costs) in order to bring greater transparency.
- For all sub-commodities, prices will be fixed over the term of the NMSO (e.g. 2 years) in order to eliminate any fluctuation due to list price changes. Current, annual furniture price inflation is between 2 - 3 per cent. A reduction in administrative costs will also factor into the savings.
- Enhancements to the e-procurement system will be implemented in order to ensure client departments are taking advantage of the savings opportunities.

2. *Product Specification Improvements*:
   - Rationalize number of product permutations on offer to achieve greater scale economies for vendors which can then be passed on to government through lower prices (e.g., chairs).
   - Limit vendors to a single series per sub-commodity.
   - All furniture will need to conform to Canadian General Standards Board (CGSB) standards or government product descriptions.

Supplier Issues and Perceptions:

- Only a limited number or suppliers will be able to negotiate purely on pricing, and the different components of pricing (e.g., delivery and installation charges).
- Large manufactures may bid very low prices and win all of the NMSOs in a number of the sub-commodities (e.g. seating).
- Overly burdensome government specifications (not made to general standards) add significant costs to the price structure of products.
- Excessive government purchases at year end can cause major demands on industry capacity, resulting in poor pricing and unnecessary spending by departments.
- The requirements of gaining an NMSO (e.g., testing required) adds to the complexity of the process and increases costs for government.

Objective 2: Enable SMEs to Participate on a Level Playing Field

Proposed Strategy to Enable SME Participation on a Level Playing Field:

1. Maintain the number of furniture companies with NMSOs. Currently there are 114 standing offers with 52 vendors across all sub-commodities. The number of standing offers may increase depending on the number of Aboriginal standing offers.
2. All current SMEs holding standing offer that meet the revised NMSO requirements will have the opportunity to maintain their NMSOs and compete for business.
3. The RFSO format has been simplified with fewer requirements placed on companies to bid (e.g., only those vendors awarded NMSOs will be required to provide furniture standards testing data if applicable).

***Supplier Issues and Perceptions*:**

- Only a limited number or SMEs may be potentially selected as larger firms may provide better pricing.
- There needs to be extra consideration given to SMEs in some of the furniture sub-commodities (e.g., seating where almost half the current vendors having a single NMSO in this sub-commodity are SMEs) in order to enhance their chances of getting business.

Objective 3: Maintain Aboriginal Set-Asides

Proposed Strategy to Maintain Aboriginal Set-asides

1. NMSO winning vendors will be requested to select at least one Aboriginal vendor to distribute their products and provide set-asides in major geographic areas (e.g., National Capital Region, Toronto, and Montreal).
2. Separate NMSOs with Aboriginal dealers, identified by successful manufacturers, will be negotiated and awarded.
3. Aboriginal dealers will be required to demonstrate their ability to service the geographical areas for which they have been designated.

***Supplier Issues and Perceptions*:**

- Only a limited number of competitive Aboriginal suppliers will be potentially selected on the basis of competitive pricing.
- Aboriginal vendors perceive a potential loss of business.
- Larger businesses do not necessarily want to be ‘required’ to have Aboriginal dealers in their networks.
- With a limited supply of Aboriginal dealers there is the potential that they move between manufacturers to obtain the best deal.

Objective 4: Provide a More Targeted Range of Products that Meet Client Department Needs

Proposed new Strategy for Targeted Range of Required Products:

1. Focus on products that are most frequently used by departments, and eliminate those products that are not used, or that are infrequently purchased (representing a small proportion of current federal government spending).
    - Chairs – up to 45 configurations.
    - Cabinets – up to 3 types.
    - Inter-connecting panels, free-standing furniture, desking – 1 series each.

2. Ensure that vendors provide a single, competitively priced series for each required product item/configuration.

Supplier Issues and Perceptions:

- Excessive demand at the fiscal year-end stretches capacity of even the larger manufacturers (taking capacity away form other more profitable business contracts).
- This strategy may adversely affect some suppliers more than others depending on what products are selected.

PWGSC is aiming to provide 100 per cent coverage of its furniture business volumes through standing offers (currently 44 per cent of business volumes are through NMSOs, the remainder is on NMSO items not using the NMSO mechanism, project spend, and purchases outside PWGSC control). To reach this target, compliance by client departments will be necessary.

Current NMSO data shows that 60 per cent of the furniture buys are made in the last quarter. The proposed approach does not address this directly although two aspects of the proposed strategy will have an impact. First, the overall furniture industry capacity will be maintained as there is no decrease in the supplier base. Second, the rationalization of the specifications will reduce the variety of products required and potentially enable better planning of production and economies of scale.

Appendix A – Data Analysis Methodology

Overview

This section presents a summary and analysis of data relating to one of the procurement categories in which the Government of Canada purchases goods and services: furniture. It examines data that relates to government requirements and purchasing and to the large, medium and small suppliers who provide goods and services to the Government of Canada.

The methodological approach taken is to analyze the nature and impact of market power and market dependence within this procurement supply category. Market power and market dependence have a major influence on the *impact* of planned changes in procurement processes. Both factors are relevant to understanding how procurement changes may affect or influence suppliers and the Government itself.

The analysis draws attention, where relevant, to difference between actions of large business suppliers versus small and medium enterprise (SME) suppliers.

It is important to clarify the key terms in the context of the Government of Canada's involvement with markets.

> ***Market power*** is the ability of the government to alter the market price of a good or service and to alter other market conditions. It is an indication of how important government procurement is in the overall market for each procurement category (i.e., its importance on the demand side).
>
> The size of the federal government in the market, especially within the National Capital Region (NCR), raises the issue of whether the market is a monopsony, with the Government of Canada being a monopsonist. A monopsony is a market form with only one buyer (the monopsonist) facing many sellers.[28] In purely competitive markets there are many sellers and buyers and this restricts the ability of buyers to determine market clearing conditions (regarding both price and volume). A monopsonist's position allows it to determine market clearing prices and volumes that maximize its welfare at the expense of suppliers.
>
> ***Market dependence*** considers the issue of market structure from the suppliers' view (i.e., the supply side). In this context, it can be simply represented by the percent of a firm's sales attributable to the Government of Canada. Firms with a large percentage of sales to the Government of Canada are said to be dependent on the government market. Dependence on one large customer is ultimately reflected in the way a firm is organized (geographically, in its business processes etc.). Highly market dependent firms are more likely to be affected by changes in their dominant customer's policies and practices.

This section explores the statistical basis for an analysis of market power and market dependence. In the case of market power, it relies mainly on Statistics Canada's industry and output data. When looking at market dependence, it analyzes Government of Canada expenditure data, provided by Public Works and Government Services Canada (PWGSC). The

[28] It is the reverse of monopoly where there is one seller to many buyers in a given market.

analysis utilizes both a macro market analysis and a micro market analysis as key methodologies for understanding the change management issues at play as the government changes procurement policy and practices.

Methodology

The following methodology has been used:

Macro Analysis

- Define the overall market as accurately as possible based on Statistics Canada data.
- Reconcile the industry output with the procurement categories.
- Review government expenditures with the industry.
- Provide an initial estimate of market power based on gross market share.
- Discuss other factors that may have a bearing on the effective market share.

Micro Analysis

- Discuss the industry structure which may have a bearing on market dependence, particularly the size of firms in the industry and their geographic location.
- Consider the current vendor basis and how expenditures relate to vendors.
- Assess the number of firms that may face adjustment risk because of high market dependence.

The Definitional Challenges

A key methodological challenge is to reconcile the various sources of data to construct a "market". The first challenge is to reconcile the PWGSC definitions of procurement categories with Statistics Canada's definitions of industries. It is difficult to do this with precision because PWGSC uses a government accounting framework whereas Statistics Canada uses a national accounting framework.

Statistics Canada assesses industry output from its business surveys. The main unit for analysis is the "establishment". According to Statistics Canada an establishment:

"…. is the level at which the accounting data required to measure production is available (principal inputs, revenues, salaries and wages). The establishment, as a statistical unit, is defined as the most homogeneous unit of production for which the business maintains accounting records from which it is possible to assemble all the data elements required to compile the full structure of the gross value of production (total sales or shipments, and inventories), the cost of materials and services, and labour and capital used in production."[29]

Based on business surveys, Statistics Canada organizes the reporting establishments into industries. Respondents to these surveys first report back by identifying themselves as

[29] See: http://www.statcan.ca/english/concepts/stat-unit-def.htm

belonging to one particular industry. Using these reports, Statistics Canada organizes its industry output statistics into an industrial classification system called the North American Industrial Classification System (NAICS).

Two types of statistical issues may arise when attempting to align commodities to specific industries. First, an establishment may not be totally “homogenous”, in which case its output may spill over into other industries. Second, government purchases for a single procurement category may cut across more than one industry.

These are some of the definitional challenges in reconciling the procurement categories (the demand side) with industry output (the supply side). These challenges are further complicated when one considers geography. Statistics Canada provides very good data at a national and provincial level for incorporated businesses. But the availability and quality of business data is less reliable at the regional or local level. If the geography of the marketplace is such that local firms play a relatively large role, then market shares that are calculated based on national or provincial shares may not be portraying an accurate picture of the effective market.

The analysis addresses statistical shortcomings in the following ways:

- It takes a “whole industry/best fit” approach to reconciling procurement categories with industry sectors. We do not attempt to massage the industry data but report those areas where, in our view, there is the greatest fit between the industry and the procurement category.
- It is transparent in reconciling procurement categories with industries.
- It provides cautionary notes on the interpretation of the subsequent market share.
- It considers mitigating factors including the role of geography, its impact on the effective market and the role of exports.
- It undertakes supplemental analyses, specifically on market dependence, to provide a fuller picture than that portrayed only through market shares.

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255 Smyth Road, Ottawa ON K1H 8M7 Canada
Tel. 613-526-3280 • Fax 613-526-4857 • Inquiries 1-866-711-2262