efficiency bulletin

Oct. 27, 2016

Color Code: Green

DELIVERING THE NUCLEAR PROMISE

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Efficiency Bulletin: 16-29

Optimize Strategic Sourcing to Deliver Savings

Organization and process inefficiencies in the procurement supply chain result in significant hidden costs. This bulletin will improve efficiencies and cost savings opportunities by reorganizing, standardizing and prioritizing the strategic sourcing function.

Addressees: **Chief nuclear officers, NEI APCs and INPO APCs**

Issue: **SC-01, Strategic Sourcing**

Summary of Efficiency Opportunity

- Desired end-state—
  - (SC-01.1) Sourcing departments are staffed with strategic category managers that can focus on evaluating and leveraging enterprise spending to deliver savings through strategic contractual relationships with suppliers. Tactical procurement is separated from strategic sourcing. Fleets should centralize the sourcing function under one management team and single sites should develop a strategic sourcing team. Staffing levels of strategic category managers and tactical buyers align with a recommendation in white paper based on company spending levels.
  - (SC-01.2) Incorporate strategic sourcing prioritization through spending review, category plans and business partner engagement.
  - (SC-01.3) Implement noncompetitive bid justification process to optimize procurements awarded based on competitive bidding.

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- Value proposition (vision of excellence)—
    - (SC-01.1) An appropriately staffed strategic sourcing group is able to effectively source and contract with suppliers resulting in strategic partnerships that deliver cost savings through leveraging spending, increased efficiencies, and improved quality and delivery.
    - (SC-01.2) Lower costs and improved supplier contractual relationships are achieved by prioritizing categories for sourcing with the most opportunity to achieve savings. Understanding of category spending, market conditions and future needs drives results.
    - (SC-01.3) Competitive bidding leads to significant savings compared to sole source procurements, with a 10 percent average cost savings on materials and services that had not been competitively bid within the prior year.
    - Implementation of a strategic sourcing group with effective category plans, business partner engagement and prioritization model can yield an increase in savings of 2.4 percent.

- Why is it important?—
    - (SC-01.1) Use of strategic category managers to effectively contract with suppliers through a diligent strategic sourcing process will help the organization achieve reductions in cost and save time. The strategic sourcing approach emphasizes leveraging spending for cost savings, supplier relationship development and performance management to improve quality and delivery and identify efficiencies.
    - (SC-01.2) Improved understanding of spending categories will lead to better cost control and savings opportunities.
    - (SC-01.3) Noncompetitive procurements should be avoided where practical to ensure competitive prices are paid for materials and services resulting in increased savings.

Relevant Standards

- None

Guidance

- SC-01.1, white paper titled "Strategic Sourcing Organization," dated Sept. 27, 2016.
- SC-01.2, white paper titled "Strategic Sourcing Prioritization," dated Sept. 27, 2016.
- SC-01.3, white paper titled "Non-Competitive Sourcing Guideline," dated Sept. 22, 2016.

Recommended Industry Actions

- Review the white papers and implement actions to align with recommendations and best practices.

Change Management Considerations

Industry Activities

- Industry webinar to provide background for the initiative, discussion, and an open forum to clarify expectations and ask questions. Webinar information can be found at the following site: https://web.inpo.org/Pages/Nuclear-Promise-Issues.aspx.

Key to Color Codes:

Red: NSIAC initiative – full participation required for viability
Blue: Action expected at all sites, but is not needed for broad industry viability
Green: Utility discretion to implement, consistent with its business environment

- Suppliers should evaluate their business with companies to identify areas for improved enterprisewide strategic relationships.

Company Actions
- Evaluate supply chain organization to determine if staffing levels for a strategic sourcing organization are appropriate. (SC-01.1)
- Complete an evaluation of spending to prioritize sourcing categories. Implement category plans to provide strategic direction on supply-managed spending. Improve supply engagement with business partners. (SC-01.2)
- Implement the proposed best practices guidelines for non-competitive sourcing. (SC-01.3)

Guiderails
- Ensure that a process exists for the utility to be able to calculate and report cost savings.

Report Your Site's Results

Please report your company's implementation of this improvement opportunity, including the date of completion. Send this information along with your company point of contact to EfficiencyBulletin@NEI.org.

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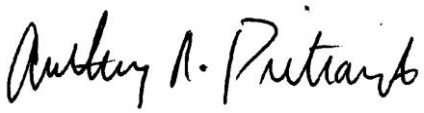

Strategic Sourcing Organization

September 27

2016

Supply chain organizations should implement a strategic group with category managers whose responsibility is to evaluate all spend within categories of materials and services and set strategic relationships with suppliers to leverage spend, reduce inefficiencies, improve quality and problem resolution, and drive savings.

Delivering the Nuclear Promise Improvement Opportunity SC-01.1

INTRODUCTION

The fundamental goals of the supply chain are to obtain products or services at the right time, quality, and cost. For supply chains that support nuclear, this translates to the goals of reducing dose, duration, and dollars, which along with safety, are the major success factors. While tactical sourcing has delivered successes, strategic sourcing can deliver sustainable tangible cost savings and additional benefits such as transactional efficiencies, improved quality and performance, reduced risk, and increased contract compliance through utilization of the seven step sourcing process.

In organizations where buyers are transacting without strategic oversight, there is potential for duplication of effort in establishing contracts with suppliers. Contracts may be developed and maintained at the site level, resulting in different contractual relationships with suppliers, or the tactical volume and focus on immediate site needs may prohibit the supply organization from taking the time to evaluate and develop strategic solutions. Additionally, the suppliers need to maintain and manage multiple relationships resulting in potential additional administrative costs on the supplier side which could be passed on to the buying organization, limiting the leverage to be gained by a strategic sourcing approach. Without supplier relationships that have been developed via strategic sourcing, supplier performance management becomes more difficult and costs to manage performance gaps associated with poor quality and untimely deliveries may increase.

Supply chain organizations should implement a strategic group with category managers whose responsibility is to evaluate all spend within categories of materials and services and set strategic relationships with suppliers to leverage spend, reduce inefficiencies and risk of business continuity interruptions, improve quality, service levels and problem resolution, and drive savings. Using the benchmark data provided in this report, organizations can determine if resources need to be added or removed to have a right-sized strategic sourcing group.

BACKGROUND

The distinction between strategic and tactical sourcing is important to understand. Tactical sourcing focuses more on a specific transactional short-term need. Strategic sourcing takes a more long-term, holistic and systematic approach in order to develop partnerships with suppliers to minimize cost, risk, and quality defects.

A strategic sourcing group includes strategic category managers who are responsible for category strategy, sourcing activities, claims and dispute resolution, supplier performance management, and facilitating process improvements and cost reduction initiatives across the category of spend they are managing. Strategic sourcing typically follows a seven-step process which includes the following activities:

1. Category/Scope Definition
2. Select Sourcing Strategy
3. Supplier Qualification
4. Execute Sourcing Strategy
5. Negotiate and Select Suppliers
6. Implementation and Transition
7. Benchmark and Track

One of the biggest benefits of strategic sourcing versus tactical sourcing is supplier relationship management. Strategic sourcing looks to create solutions that are a win-win for the company and supplier over a period of time. A relationship is developed that adds value to the supply chain through improved contract terms, process efficiencies, pro-active performance management, and shared desire to keep costs down. Strategic suppliers become partners to the business to help achieve goals of reducing dose, dollars, and duration. This

relationship is often not cultivated in tactical sourcing as each award is a one-off transaction that looks to meet the immediate need at the lowest cost.

The distinction between the two functions can be summarized as follows: strategic category managers are responsible for establishing, developing and maintaining the contractual relationship with key suppliers to provide long-term value, whereas tactical buyers are responsible for executing transactions against the established strategic contracts and sourcing lower dollar requirements. Some of the key qualification differences are listed in the table below.

Table 2: Job qualifications – Tactical Buyer vs. Strategic Category Manager

Tactical Buyer	Strategic Category Manager
• Bachelor's Degree in business, engineering, science or related field with two (2) years' experience or High School diploma or equivalent, with six (6) years of experience. • Strong PC and computer skills • Strong analytical skills • Strong communication skills • Working knowledge of the Inventory, Purchasing, and Accounts Payable modules and eSourcing tool. • Understanding of commodities, suppliers, market alignments and supply concepts and technical and non-technical clients.	• Bachelor's Degree in business, engineering, science or related field with a minimum of five (5) years' experience or High School diploma or equivalent, with nine (9) years of experience. • Demonstrated project and change management skills. • Demonstrated knowledge of category and supply management concepts. • Adept and persuasive communicator (verbal, written). • Cross functional/organizational team management and facilitation skills (internal and external). • Demonstrated data analysis capability. • Demonstrated negotiation skills. Ability to hold Suppliers accountable for performance. • Conflict management experience. • Technical aptitude (category-specific requirement)

ANALYSIS

A survey of nuclear operating companies was conducted to determine the appropriate size of strategic groups, and evaluate industry trends. The survey results (which enveloped ten responses) were divided into three buckets based on the size of the nuclear organization.

Large companies were those with five or more sites (8-22 units), mid-size companies were those with two to three sites (3-7 units), and single site companies (1-3 units). Additionally, the three year average values from the CAPS Research Supply Management Metrics Report for Utilities (Publication years 2014-2016) were used for comparison. The key metrics for analysis in staffing strategies were: percentage of strategic employees to overall procurement employees and managed spend per strategic and tactical employee.

The three-year average CAPS Research survey data for the utility industry was the baseline for comparison for the survey results. CAPS Research is jointly sponsored by member companies, the W. P. Carey School of Business at Arizona State University, and the Institute for Supply Management® (ISM). The CAPS survey data was a useful benchmark to gauge the structure of a strategic sourcing group, however, it is important to note that the CAPS research provides an average of all responding utility companies and does not take into account how the size of the organization can impact the average values as was evident in the nuclear survey responses.

Table 1: Summary of survey results

Organization	Strategic/Tactical Procurement Ratio	Spend per Strategic Category Manager	Spend per Tactical Buyer	Percent of Companies with Separate Roles
CAPS Research	30%/70%	$59M	$24M	N/A
All Nuclear Survey Responses	30%/70%	$131M	$40M	65%
Large (5+ Sites/ 8-22 Units)	24%/76%	$105M	$33M	100%
Mid-size (2-3 sites/ 3-7 units)	45%/55%	$52M	$42M	50%
Single Site (1-3 units)	25%/75%	$200M	$41M	60%

The nuclear industry survey highlighted a couple of notable characteristics of the sourcing and procurement groups. For companies with strategic groups, the function was often performed centrally. Several companies also indicated the move to centralized tactical purchasing to leverage category expertise at the tactical level. All but one survey response also indicated that spend was leveraged across non-nuclear specific business units within the greater corporation. The ability to leverage spend across all parts of the company can result in savings through enterprise contract and vendor management, and improved volume pricing.

Additional statistics from the nuclear industry and CAPS Research surveys were useful references for evaluating and structuring a strategic group. The first value to consider was the supply management operating expense per supply employee. According to the nuclear industry survey, strategic employees have an average annual fully loaded operating expense of $125,000[1] whereas tactical employees average $112,000.[2] The CAPS Research average was $133,000 per supply management employee, however it does not distinguish between strategic and tactical roles. When evaluating the supply cost for your organization, consider your own operating costs as these may vary drastically from company to company.

The second value of consideration was the return on investment (ROI). The average cost reduction and cost avoidance savings achieved per category managers in mature strategic sourcing groups was $3.24M.[3] Given an average annual operating cost of $125,000, category managers in these organizations achieved an ROI of 2600%.[4] The CAPS average ROI for supply management procurement employees was 500%; however, that benchmark is representative of both strategic and tactical procurement professionals. Using either metric, one can demonstrate that supply procurement employees bring value in savings that far

[1] Rounded average of overall survey results for Strategic Employees ($95,900; $130,000; $149,000)
[2] Rounded average of overall survey results for tactical employees ($82,200; $107,000, $110,000, $150,000)
[3] Average of total savings divided by number of strategic category managers ($2.84M, $3.63M)
[4] ROI is calculated using the average savings of $3.24M divided by average operating expense of $125,000 and represented as a percentage (rounded)

exceeds their cost. Assuming the CAPS survey represents normalized staffing levels in the utility industry, one can assume that diminishing returns may occur when the average spend per strategic category manager drops below $59M.

RECOMMENDATION

Companies should evaluate the survey data provided in this report to guide the development or optimization of the strategic sourcing group. The size and structure of a strategic group will depend on the overall company structure and the maturity of the sourcing group. Since an increased skill set is required for strategic sourcing compared to tactical sourcing, it is recommended that supply chain groups separate these functions into distinct roles.

Table 2: Recommended Staffing Strategy

Divide the company supply managed spend by the spend per value to determine the recommended staffing levels.			
Organization	Strategic/Tactical Procurement Ratio	Spend per Strategic Category Manager	Spend per Tactical Buyer
Large (5+ Sites/ 8-22 Units)	28%/72%	$105M	$40M
Mid-size (2-3 sites/ 3-7 units)	40%/60%	$59M	$40M
Single Site (1-3 units)			
Alternative recommendation	30/70%	$95M	$40M

Companies that are new to strategic sourcing may need to invest in personnel to help develop the strategic category management approach. While the annual average fully loaded operating cost of a strategic supply management employee supporting nuclear is $125,000, the return on investment averages 2600%.

Where and when possible, companies should implement a centralized strategic sourcing group. Companies with portfolios that include non-nuclear generation and/or distributed utilities should consider areas of overlap in development of the strategic sourcing group. Companies should also consider centralizing tactical procurement and assigning a fleet wide category approach for tactical buyers in order to leverage category expertise and volumes at the tactical level, reduce redundant interactions with suppliers, and drive staffing efficiencies. Physical location of employees under a centralized structure should be determined by the organization. Team members under a centralized management reporting structure may be geographically dispersed.

In order to determine the effectiveness of the strategic sourcing group, companies should have a mechanism to track savings and obtain business partner buy-in for removal of hard savings from budgets. Strategic sourcing organizations should distinguish hard savings (cost reduction) from soft savings (cost avoidance). Additional measurements of effectiveness include percent of transactions under strategic contracts which will lead to efficiencies in tactical procurements.

CONCLUSION

A strong strategic sourcing group can add great value to the supply chain. Strategic category managers can evaluate company-wide spend in distinct categories and develop strategies that will leverage volume and reduce operational inefficiencies to drive supply chain savings which directly impact the business. Organizations may need to invest in strategic sourcing employees in order to increase supply chain savings, however the return on investment is high. While this paper focused on guidance for establishing and right-sizing the strategic sourcing group, "SC-01.2 Strategic Sourcing Prioritization" focuses on strategies that help strategic organizations deliver best-in-class savings. With the right size strategic group

and sourcing strategies, organizations can achieve best-in-class savings of 5.0% or $5.65M per unit.[5]

[5] Refer to SC-01.2 Strategic Sourcing Prioritization for more details. Average spend per unit is reported as $113M.

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3. 'Cross-Industry Report of Standard Benchmarks, Published 2014 July, CAPS Research, capsresearch.org
4. Industry Survey Results

Strategic Sourcing Prioritization

September 27

2016

By improving the strategic sourcing focus through use of category plans, business partner engagement, and a sourcing prioritization model, savings can increase an additional 2.4% to reach best-in-class savings achieved within strategic organizations.

Delivering the Nuclear Promise Improvement Opportunity SC-01.2

INTRODUCTION

One of the challenges of a strategic sourcing group is the mechanism and ability to collect, analyze and take action on the magnitude of available data with a proactive rather than reactive approach. When sourcing groups are able to move their focus away from immediate need (reactive) to overall category sourcing (proactive), the opportunity for savings can improve. Based on industry data, the best-in-class nuclear strategic sourcing group achieved 5.0%[1] cost reduction savings compared to the utility industry average of 2.6%[2] on the supply managed spend portfolio. A solid understanding of business need, spend analysis and market conditions through use of category plans and business partner engagement will help identify and prioritize areas to target for sourcing savings opportunities to help achieve best-in-class savings levels.

ANALYSIS

A survey of nuclear operating companies was conducted to determine best practices in strategic sourcing. Survey responses were categorized as "Strategic Organizations" or "Tactical Organizations" based on the business partner's view of the sourcing group. Three organizations were classified as "Strategic" based on being viewed as 65-80% strategic and 20-35% tactical by their business partners. The "Tactical" organizations were viewed as either 50/50% (2) or 80% tactical (3) by their business partners. Strategic organizations scored higher for their use of category plans and business partner engagement.

[1] Values are from the nuclear survey responses for strategic organizations and are representative of the average savings divided by the average supply managed nuclear spend from 2013-2015. This percentage is not limited to only those procurements that have been strategically sourced (See SC-01.3 for statistics on savings as a result of competitive bids).
[2] Value represents the average of 2013-2015 CAPS Research benchmark survey response for the Utility Industry. Savings values were not tracked or provided by more tactical nuclear organizations; therefore the CAPS Research benchmark is used as a baseline assumption.

CATEGORY PLANS

Category plans are an important strategic tool for understanding sourcing prioritization. All three of the strategic organizations utilize category plans, whereas only one tactical organization indicated the use of category plans. The value of category plans are evident as three of the tactical organizations are working to develop category plans, and most strategic organizations identified they are working to improve category plans. Key components of the category plan include: historical spend analysis, market conditions and forecasts, contract expirations, long-term asset plans, and supplier demographics profiles. Category plans are typically reviewed annually with senior supply management.

The category plan serves as the tool for understanding the category drivers and identifying and executing a strategic sourcing plan to meet the needs of the organization. Category plans can and should be developed utilizing resources outside of the category manager role. Internal analysts can be utilized to help gather and summarize data. Third party organizations such as Denali, IHS, Gartner, and Power Advocate can be utilized to better understand market conditions and sourcing opportunities. Industry conferences are also a resource to better understand the category dynamics and all strategic organizations surveyed were supportive of category managers attending industry conferences as required.

The number of category divisions varied widely in the survey responses, from two categories to well over one hundred. Category groupings should be established based on similar materials or services where opportunities to leverage spend may be optimized. When reviewing categories, it is also important to consider the enterprise opportunity outside of the nuclear organization. Category plans are recommended for those categories with greater than $5M annual spend. The size of the organization may dictate the need to summarize spend into higher level categories or distinguish more finite categories. In order to be successful in analyzing category spend it is imperative that each transaction is categorized appropriately and

that the spend data is refreshed and reviewed regularly. A list of potential categories is included in Exhibit A.

Once all of the relevant data is gathered for the category plan, it becomes easier to develop a strategy to achieve savings. The historical spend analysis can help identify areas that need to be sourced to be managed under strategic relationships and opportunities for supplier consolidation. Understanding the market conditions can help determine a sourcing strategy versus renegotiation of existing contracts. It is important to know the key contract expiration schedules in order to plan the sourcing strategy based on changing market conditions.

BUSINESS PARTNER ENGAGEMENT

One of the most important factors for category understanding and strategic sourcing prioritization is business partner engagement for future needs awareness. Sourcing groups that are more "strategic" have better awareness of upcoming procurement needs by being engaged in the business planning process for projects and capital modifications, having an understanding of Long-Term Asset Management Plans and by attending project funding approval meetings as well as having sourcing leadership sign-off on project funding requests. Additionally, top down buy-in from business partners in enforcing sourcing managements' role in purchasing is critical for achieving optimal savings in the strategic sourcing process. Strategic sourcing groups should also ensure regular report outs to the business partners for approval in strategic sourcing initiatives. Business partner subject matter experts are key members on strategic sourcing project teams. The savings that result from sourcing initiatives are reported to the business partners for removal from the budget.

BENCHMARK SAVINGS RESULTS

Based on the nuclear industry survey, the best-in-class annual cost reduction savings achieved within the strategic organizations was 5.0%. A benchmarking study conducted by

CAPS Research[3] indicated an average cost reduction savings of 2.6% of managed spend from 2013 thorough 2015 for the utility industry. By improving the strategic sourcing focus through use of category plans, business partner engagement, and a strategic sourcing prioritization model, savings can increase an additional 2.4% from the benchmark average to reach best-in-class savings achieved by the strategic organizations.[4] With an average supply managed spend of $113M per unit[5], and assuming the organization currently operates at the CAPS Research benchmark average savings level; the increased savings opportunity can be $2.71M, with best-in-class organizations achieving a total of 5.0% savings or $5.65M per unit annually.

RECOMMENDATION

Strategic Sourcing savings is best achieved when sourcing focus can shift from tactical and emergent (reactive) to strategically planned and executed (proactive). In order to implement a strategic sourcing plan, the full category opportunity must be understood and evaluated for target focus areas. Sourcing organizations can improve the strategic focus by implementing category plans to analyze trends and opportunities to drive savings. Category plans should include spend analysis, market conditions and forecasts, contract expiration schedules, project and long-term asset plans, and supplier demographic profiles. It is important that spend data is reviewed, cleansed, categorized and analyzed on a regular basis to be the most effective in category management. Additionally, category plans should be updated annually and reviewed and approved by supply and business partner leadership.

Organizations must work to engage business partners to understand and prepare for future demands. This relationship can be improved if strategic sourcing groups are involved in the nuclear business planning process and engaged in project funding reviews. Business

[3] CAPS Research is jointly sponsored by member companies, the W. P. Carey School of Business at Arizona State University, and the Institute for Supply Management® (ISM®).
[4] Savings opportunity may be more or less depending upon the current savings record of your organization.
[5] Average from survey results

partner leadership must provide top-down enforcement of the role of strategic sourcing in procurement process to ensure success.

With the information gathered in support of the category plan and discussion with business partners on upcoming projects, a strategic supply organization can better prioritize categories for strategic sourcing. The following table, taken from the article "Prioritization is the Secret Ingredient for an Efficient Sourcing Process", provides a simple series of questions to help determine whether or not to work on a category. While the article was written for and appears in the Association for Healthcare Resource and Materials Management, the guidance is appropriate for the nuclear supply chain.

Table 1: Prioritization Variables

Variable	Negatively impact decision to work on category	No impact on decision	Positively impact decision to work on category
What is the financial impact and spend volume?	Low	Med	High
What is the time to value?	Slow	Med	Fast
Is the category complex?	Complex	Med	Simple
Are market conditions favorable?	No		Yes
What is our ability to change suppliers?	Low	Med	High
When does out current contract expire?	Soon	Med	Later
Do we have current contract coverage?	Yes		No
Are there diverse suppliers or more sustainable product choices to consider?	No		Yes

Using the table above, categories to be prioritized for sourcing are those with the following criteria: highest spend, shortest sourcing cycle, simple complexity, favorable market conditions, competitive environments, time to source before contract expiration, lack of contract coverage, and/or diverse spend opportunities. Categories that meet these criteria will deliver the largest return on investment from the strategic sourcing process. The categories

that have characteristics that fall under the "negative impact" column may be better suited for contract extensions.

CONCLUSION

With a strong strategic sourcing group in place per SC-01.1, nuclear organizations can achieve an additional 2.4% savings by increasing and prioritizing their strategic procurements through improved category understanding via utilization of a category plan and increased business partner engagement. With better category understanding, strategic sourcing groups can evaluate the prioritization variables to identify which areas will bring the best opportunities for cost savings and business need fulfillment. Assuming units are operating at the average spend level of $113M per unit, this category management, business partner engagement, and sourcing prioritization approach can result in a savings increase of $2.71M per unit, with best-in-class strategic sourcing groups achieving a total of 5.0% savings or $5.65M per unit annually.

EXHIBIT A: POTENTIAL CATEGORIES

Materials	Services
Bolting/Fasteners	Contaminated Laundry
Chemicals/Fuels/Lubricants	Cooling Towers
Chillers & Parts	Diving
Diesel Equipment	Engineering/Technical Consulting
Electrical Equipment	Equipment Rental
Electronic Components	Heavy Hauling and Lifting Services
Fans and Air Handling Equip	In-Processing/Badging Services
Filters	Inspections NDE (non-NSSS)
Gases	Machining & Fabrication Services
Instrumentation/Controls	Maintenance Services - Chillers
Mechanical/HVAC Material	Maintenance Services - Condenser Cleaning
Motors	Maintenance Services - I&C Techs
MRO	Maintenance Services - Leak Services
NSSS Materials	Maintenance Services - Scaffolding/Insulation
Pipe & Fittings	Maintenance Services – Snubber Testing
Pumps - parts, repairs, & services	Maintenance Services - Valves
Sealing Devices	MMC
Station Batteries & UPS	NSSS Services
Structural Steel	Off-Site/On-Site Testing Services
Tanks, Condensers, FW Heaters, Boilers - Equipment & Parts	Overhead Crane Maintenance
Traveling Screens	Rad Pro Services
Turbine / Generator Materials	Rad Waste
Valves	REMP
Water Treatment - Chemicals	ROV
Weapons/Ammunitions	Security Services
	Sirens
	Spent Fuel Storage
	Supplemental Labor
	Turbine / Generator Services
	Turbine Combustion
	Water Treatment Services
	Welding

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Non-Competitive Sourcing Guideline

September 22

2016

Implement a non-competitive bid justification process to optimize procurements awarded based on competitive bidding.

Delivering the Nuclear Promise Improvement Opportunity SC-01.3

SUMMARY

The Non-Competitive Sourcing Guideline process improvement effort is an initiative to reduce the potential cost impact associated with non-competitive sourcing events by strengthening Single Source and Sole Source guidelines to reduce exceptions to competitive sourcing requirements through the use of nuclear industry best practices. In addition, Non-Competitive Sourcing exceptions should be used sparingly to avoid any ethical concerns in the contracting process. This document will cover when to use, how to document, and who should approve such exceptions.

DEFINITIONS

A. Single Source – Purchase of materials or services without competitive bids, not made under an existing contract or sourcing agreement, for which there might be an alternative source available. (Also known as Directed Source)

B. Sole Source – Purchase of materials or services from the only supplier capable of providing the materials or service; any attempt to obtain bids would result in only one qualified supplier.

MINIMUM SPEND THRESHOLD

As a general rule, and to the extent practical, sourcing should be made on the basis of competitive bidding. What is "practical" may differ greatly from utility to utility. Given the inefficiency in competitively bidding all materials and services at lower dollar levels, almost all nuclear utilities set minimum spend thresholds below which competitive bidding is not required. However, this minimum level varies widely from as low as $2,500 to as high as $300,000, with the industry average at $100,000 for both materials and services sourcing.

Economically, the minimum spend threshold should reflect the approximate level where savings achieved from competitive bidding is greater than the internal cost of the total time and effort spent to solicit bids. On an individual material or service level, this threshold

will vary based on the industry and maturity of the goods or services purchased, with more mature goods and services generally providing less opportunity for savings due to increased competition and general availability. Additionally, the maturity and sophistication of the supply chain organization soliciting bids may impact opportunities to generate savings (see SC-01.2).

A utility can determine what the approximate level should be with the following information:

A - Average cost per hour of sourcing employees and business unit employees (cost of employment per year divided by expected work hours per year)

B - Average number of hours spent by each group of employees to competitively bid the material or service (inclusive of background research, bid preparation, pre-bid meetings, bid event, evaluation, award and purchase documentation, for all individuals involved) over and above that necessary to Single Source

C - Average cost savings percentage from competitive bidding materials and services

D - Minimum Spend Threshold needed to justify competitive bids

Thus, $D = (A \times B) / C$

For Example:

Average cost of employee	Hours per year	Average employee cost per hour (A)	Total hours for bid (B)	Internal cost to bid	Expected cost savings % from bid (C)	Minimum Spend Threshold (D)
$150,000	2,080	$72.12	65	$4,687.50	3%	$156,250

For those utilities without sufficient data on cost savings from previous sourcing events, research indicates that savings can range from between 5-30% and 3-37% with savings from reverse auctions between 10-40% (IJMVSC Vol. 2, No. 3, Sept. 2011). In contrast, the American Purchasing Society reported 10% average cost savings on materials and services that had not been competitively bid within the previous year. Note that as the expected cost

savings (C) decline, the minimum spend threshold (D) increases. Alternatively, as the internal cost to bid (A x B) decreases, the minimum spend threshold (D) would also decrease.

Given the variance in hours needed to solicit competitive bids on materials versus services, it is recommended that utilities ascertain and establish separate minimum spend thresholds for materials and services. However, it should be noted that certain utilities may be subject to federal, state and/or municipal laws, regulations or commissions and the minimum spend threshold may not be subject to change.

NON-COMPETITIVE SOURCING JUSTIFICATIONS

Once the minimum spend threshold is met for a given material or service, that material or service must be competitively bid unless the requestor or the procurement individual provides a justification as to why the particular material or service should not be competitively bid. The industry survey of exceptions to the competitive bid process revealed the following set of exceptions as a best practice:

Requester provided exceptions:

1. When, based on recent bids, test of the market, or similar information, the costs involved in undertaking a competitive process or changing to a new supplier are greater than the potential advantages (which may be savings, or could be other opportunity). Requester to provide the cost analysis.
2. When business unit or delivery requirements do not allow sufficient time to bid. Requester to provide the required-by date and justification as to why the required by date cannot be moved to an alternate date to allow for competitive bidding (e.g., legal, regulatory, or other documented time requirements, or a plant condition having direct and immediate impact on the capacity factor of the plant).
3. When purchaser specifications or technical requirements limit procurement to a single source. Requester shall not impose technical requirements that restrict competition.

Requester must document what the specification or technical requirement is that limits to the particular source (i.e., supplier encompasses extensive and unique knowledge required for specialized scope, specific program, system, or process).

4. When the material or service is required under emergency conditions. Requester to provide the emergency condition. Reference: Emergency Definition - A critical condition exists involving immediate or imminent risk of death, serious bodily injury, threat to employee or public health.
5. When the material or service is procured via a Sole Source, i.e., it is necessary to contract with a specific supplier due to technical, configuration control, or proprietary reasons. Requester to provide the technical justification of Sole Source.
6. When the purchase is for research, trial or pilot purposes. Requestor to provide documented business unit and engineering approvals and cost justification, as applicable.
7. The business line desires to standardize equipment (or software) or for parts availability, maintenance, operational, training & repair purposes. Requester to provide price analysis and technical justification as applicable.

Procurement individual determined exceptions:

1. When, based on recent bids, test of the market, or similar information, the costs involved in undertaking a competitive process or changing to a new supplier are greater than the potential advantages (which may be savings, or could be other opportunity). Buyer to document the cost analysis.
2. When the material or service is procured via a Sole Source, i.e., it is necessary to contract with a specific supplier due to technical, configuration control, or proprietary reasons (Buyer to document supplier search).
3. Purchases made from Supply Chain Alliance Partners (i.e., inter-utility sales, USA, STARS, PIM Program) (does not include suppliers).

4. Restricted by law or professional code of conduct (e.g., engineering services in Alabama).

Notwithstanding the requestor's submission of an allowable exception, typically through a Non-Competitive Sourcing form, the supply chain organization should challenge or reject Non-Competitive Sourcing Justifications that set forth insufficient support or analysis, or otherwise fail to meet the standards set for the declared exception. Supply Chain should also review all such requests and consider all commercial elements to ensure the best business decision is made on behalf of the utility. The procurement individual should ensure pricing is fair and reasonable under the circumstances and should engage in further commercial negotiations using available supply chain tools and resources as appropriate under the circumstances.

NON-COMPETITIVE SOURCING APPROVAL

At a minimum, the Non-Competitive Sourcing Justification should be approved by at least one management level above the purchasing level required of the purchase, with prior approval signatures of all subordinate levels in management chain. For example, if the minimum spend threshold for competitive bidding was $25,000 and a First Line Supervisor with $50,000 of purchasing authority was presented with a $49,000 Purchasing Requisition accompanied by a Non-Competitive Sourcing Justification, the Non-Competitive Sourcing Justification would require the additional approval of the First Line Supervisor's manager. Each utility should also strongly consider the spend level threshold at which executive level approval for non-competitive sourcing is required (e.g., a significant number of nuclear utilities require vice president level approval of all non-competitive sourcing justifications valued at $250,000 and above). Importantly, at the time of each management level of review by the requesting line of business, it is expected that each such management level will challenge, when necessary, or independently confirm the supporting evidence and analysis for the chosen exception.

The approved Non-Competitive Sourcing Justification documentation setting forth the exception(s), supporting analysis and all required approvals should be maintained with the record of purchase, whether it be a contract or purchase order, to provide an audit trail. This record should be maintained according to company standards in connection with the sourcing award for which it was approved (i.e., if the justification supports a contract award, the justification documentation should be maintained through the disposition date of the contract records).

CONTINUOUS IMPROVEMENT

In order to reduce reoccurring reliance on the use of non-competitive sourcing, a category sourcing review/assessment should be conducted at some frequency to monitor and detect opportunities for strategic sourcing improvements and leveraging competitive procurement activities in order to execute competitive, non-Single/Sole Source engagements. See SC.01.2 - Strategic Sourcing Prioritization.

Bibliography

1. Wyld, David C. 'Current Research on Reverse Auctions: Part 1 – Understanding the Nature of Reverse Auctions and the Price and Process Savings Associated with Competitive Bidding', International Journal of Managing Value and Supply Chains (IJMVSC) Vol. 2, No. 3, September 2011
2. Industry Survey Results