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In this issue, two reprints are from the federal government. We hope that state and local procurement officers will submit useful state and local publications that we cannot access.

We welcome all suggestions for reprints. Please mail or e-mail your reprint suggestions directly to:

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**BEST PRACTICES:
USING SPEND ANALYSIS TO HELP AGENCIES TAKE A
MORE STRATEGIC APPROACH TO PROCUREMENT**

U. S. Government Accountability Office*

ABSTRACT. “Spend analysis” is a tool that provides knowledge about who are the buyers, who are the suppliers, how much is being spent for what goods and services, and where are the opportunities to leverage buying power. Private sector companies are using spend analysis as a foundation for employing a strategic approach to procurement. Recognizing the potential in government purchasing, GAO examined if the departments of Agriculture, Health and Human Services (HHS), Justice, Transportation, and Veterans Affairs are using spend analysis to take a strategic approach to acquisition. GAO assessed (1) if agencies use spend analysis to obtain knowledge to improve procurement of goods and services and to reduce procurement costs, (2) how agencies’ practices compare to leading companies’ best practices.

INTRODUCTION

Taking a strategic approach to procurement involves a range of activities—from using "spend analysis" to develop a better picture of what an agency is spending on goods and services, to taking an enterprisewide approach for procuring goods and services, to developing new ways of doing business. Our prior work has shown that such an approach could help agencies leverage their buying power, reduce costs, and better manage suppliers of goods and services, as leading private sector companies have discovered on adopting these activities. One

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survey of 147 companies in 22 industries indicated that such an approach produced savings of more than \$13 billion in 2000.¹

Spend analysis is a tool that provides companies knowledge about how much is being spent for what goods and services, who are the buyers, and who are the suppliers, thereby identifying opportunities to leverage buying, save money, and improve performance. To obtain these answers, companies use a number of practices involving automating, extracting, supplementing, organizing, and analyzing procurement data. Companies establish automated systems to extract and compile internal financial data covering everything they buy; supplement that data with information from external sources; organize this data into complete and consistent categories of products, services, and suppliers; and have the data continually analyzed. Companies then leverage this data to institute a series of structural, process, and role changes aimed at moving away from a fragmented procurement process to a more efficient and effective corporate process in which managers make decisions on a companywide basis.

We have already issued several reports examining the benefits of using a strategic approach to procurement and spend analysis at the Department of Defense (Government Accountability Office (2002a; 2003a; 2003b). Recognizing the potential that similar use might offer in civilian areas of government purchasing, on the initiative of the Comptroller General, we reviewed the activities of five federal agencies--the departments of Agriculture, Health and Human Services (HHS), Justice, Transportation, and Veterans Affairs--whose goods and services spending totaled almost \$37.2 billion in 2003.² Specifically, we assessed (1) if these agencies are using spend analysis to obtain knowledge to improve procurement of goods and services and (2) how these agencies' spend analysis practices compare to leading companies' best practices, including whether agencies have in place the supporting structure, processes, and roles to effectively use the results of spend analysis. We are addressing this report to you because of your jurisdiction over the efficiency, economy, and effectiveness of all agencies and departments of the government.

SCOPE AND METHODOLOGY

To conduct this work, we obtained information from the five agencies about how they used spend analysis in support of a more cost

effective approach to procurement. We interviewed senior procurement management officials at departmental headquarters to obtain information and views about any agencywide spend analysis efforts and how such efforts compared to leading companies' best practices identified in our recent work (GAO, 2002a; 2003a). We reviewed internal memorandums and other documents related to ongoing or proposed agency procurement reforms that leveraged buying power, cut costs, and achieved other performance benefits. For background on the agencies' contract and purchase card spending on goods and services, we used summary fiscal year 2003 Federal Procurement Data System (FPDS) data from the General Services Administration (GSA).³ Because we used FPDS data for information purposes and not to support our findings, we did not verify the data.⁴ We also did not verify the accuracy of any strategic procurement costs savings reported to us by the agencies. We conducted our work in accordance with generally accepted government auditing standards between December 2003 and June 2004.

BACKGROUND

Our past work studying how leading private-sector companies have reengineered their approach to procurement offers federal agencies both valuable insights and a general framework that could serve to guide their efforts.⁵ While each of the companies we studied is a leader in its respective market, each was also not immune to market or stockholder pressures to improve performance or to challenges from senior corporate leadership to improve the manner in which the company acquired goods and services. In turn, these companies adopted a strategic approach to leverage their buying power, reduce costs, better manage their suppliers, and improve the quality of goods and services acquired.

As shown in Figure 1, we identified broad principles and practices that were critical to carrying out the companies' strategic approach successfully. Taking a strategic approach involves a range of activities from developing a better picture of what the company is spending on procurement to taking an enterprisewide approach to procuring goods and services and developing new ways of doing business.

Pursuing such an approach in the private sector clearly pays off. Studies have reported significant cost savings for some companies of 10 to 20 percent of their total procurement costs. And the leading

FIGURE 1
Broad Principles and Practices of Leading Companies' Strategic Approaches

Commitment...Secure up-front commitment from top leaders
<ul style="list-style-type: none"> - Recognize and communicate the urgency to change procurement spending practices - Provide clear and strong executive leadership, including goals and targets
Knowledge...Obtain improved knowledge on procurement spending
<ul style="list-style-type: none"> - Develop information system—i.e., a spend analysis system—to identify how much is being spent with which supplier for what goods or services - Analyze the data to identify opportunities to reduce costs, improve service levels, and provide better management of suppliers
Change...Create supporting structure, processes, and roles
<ul style="list-style-type: none"> - Create or identify organizations responsible for coordinating or managing purchases - Establish proactive business relationships among end users, purchasing units, and other stakeholders - Implement more integrated team-based sourcing processes - Create commodity/service experts
Support...Enable success through sustained leadership, communication, and metrics
<ul style="list-style-type: none"> - Obtain sustained support from senior leadership to facilitate change - Establish clear lines of communication among all affected parties - Demonstrate value and credibility of new processes through the use of metrics

Source: GAO analysis.

commercial companies we studied reported savings and anticipated savings in the billions of dollars.

Conducting a spend analysis to obtain improved knowledge on procurement spending is a critical component of an effective strategic approach. A spend analysis permits company executives to review how much their company has spent each year, what was bought, from whom it was bought, and who was purchasing it. The analysis identifies where numerous suppliers are providing similar goods and services--often at varying prices--and where purchasing costs can be reduced and performance improved by better leveraging buying power and reducing the number of suppliers to meet the company's needs.

Spend analysis is an important driver of strategic planning and execution, and it allows for the creation of lower-cost consolidated contracts at the local, regional, or global level. At the same time, as part of a strategic procurement effort, spend analysis allows companies to monitor trends in small and minority-owned business supplier participation to address the proper balance between small and minority business utilization and equally important corporate financial savings goals for strategic sourcing.

Setting up a spend analysis program can be challenging, according to our prior research. Companies have had problems accumulating sufficient data from internal financial systems that do not capture all of what a company buys or are being used by different parts of the company but are not connected. Because simplified data may not exist or be available, companies have frequently been unsure who their buyers are and have had to contend with databases that include listings of items and suppliers that in reality are identical to each other but which are all stored under different names. Companies have also found that existing databases have not captured anywhere nearly enough details on the goods and services for which vendors are being paid.

Despite the challenges, companies that developed formal, centralized spend analysis programs have found that they have been able to conduct effective and ongoing spend analysis through the use of five key processes, involving automating, extracting, supplementing, organizing, and analyzing data.

Spend Analysis: Key Processes

1. **Automation:** Data automatically compiled.
2. **Extraction:** Essential data culled from accounts payable and other internal systems.
3. **Supplemental information:** Additional data sought from other internal and external sources.
4. **Organization:** Review data to ensure accuracy and completeness; organize data into logical, comprehensive commodity and supplier categories.
5. **Analysis and strategic goals:** Using standard reporting and analytical tools, data analyzed on a continual basis to support decisions on strategic-sourcing and procurement management in areas such as cost cutting, streamlining operations, and reducing the number of suppliers. Scope generally covers an organization's entire spending.

Source: GAO analysis.

Building the foundation for a thorough spend analysis involves creating an automated information system for compiling spending data. The system routinely extracts vendor payment and related procurement data from financial and other information systems within the company. The data are then automatically compiled into a central data warehouse or a spreadsheet application, which is continually updated. Most of the automated spend analysis systems currently in use were developed in-house, although some companies have hired third-party companies for expertise and technology.

The data are primarily extracted from vendor accounts payable financial systems and reviewed for completeness. Accounts payable data can be voluminous and very detailed. Companies process large numbers of vendor invoices for payment each year, and each of those must be examined by their spend analysis systems. When necessary, the accounts payable data are supplemented with other sources, such as purchase card data obtained from external bank-card vendors' systems or other information, such as suppliers' financial status and performance information. Companies must obtain as much information as possible from both internal and external sources to gain a complete understanding of their spending.

For spend analysis to be effective, data files must be accurate, complete, and consistent. The data are subjected to an extensive review for accuracy and consistency, and steps are taken to standardize the data in the same format, which involves the creation of uniform purchasing codes. The data are typically organized into comprehensive categories of suppliers and commodities that cover all of the organization's purchases.⁶

In tandem with building a spend analysis foundation, commodity managers or cross-functional commodity teams are established to access and analyze the information on an ongoing basis, using standard reporting and analytical tools.⁶ Each team is responsible for one or more commodities, which may also include responsibility for a number of sub-categories. Once the spending data has been organized and reviewed, companies use the data as the foundation for a variety of ongoing strategic decisions and efforts.

Our past work also shows how federal agencies, in particular DOD, might apply these private sector best practices to obtain lower prices from suppliers and improve procurement effectiveness. For example, we noted that although DOD's spending on services contracts approaches

\$100 billion annually, its management of services procurement has been inefficient and ineffective (GAO, 2002a, 2003a; 2003b). To achieve the potential for billions of dollars in savings, we recommended that DOD take a more strategic approach to services contracting that includes adopting the spend analysis best practices of leading companies. In response, in 2004 the agency started developing a spend analysis system that will pull purchasing data from disparate databases for analysis by newly organized DOD-wide commodity teams. DOD expects that users of this spend analysis system will be able to identify procurement trends, buying patterns, and opportunities for strategic sourcing, which will result in cost savings and quality improvements.

The government purchase card program offers yet another arena for the use of spend analysis. Through the purchase card program, agency personnel can acquire the routine goods and services they need directly from vendors as long as the purchase is \$2,500 or less. From 1994 to 2003, the use of such cards exploded from \$1 billion to \$16 billion, but we found that agencies generally were not taking advantage of opportunities to negotiate discounts with major vendors (GAO, 2004a; 2004b). We therefore recommended several actions--including conducting spend analysis using available data and gathering additional information where feasible--that would ultimately help agencies to achieve \$300 million annually in potential savings.

AGENCIES HAVE BEGUN ANALYZING SPENDING TRENDS TO IMPROVE KNOWLEDGE AND PROCUREMENT

Three of the five agencies we reviewed--Veterans Affairs, HHS, and Agriculture--have each conducted spend analyses, either by using their own resources or by hiring consultants to do the work. Each agency is beginning to use spend analysis to obtain knowledge and to plan and carry out changes in agencywide procurement processes intended to leverage buying power, eliminate redundant and duplicative acquisition activity, and reduce purchasing costs for goods and services. The departments of Justice and Transportation have not begun to collect the data needed for using spend analysis nor taken steps that would be part of a strategic approach to procurement.

For several years, Veterans Affairs has had significant success using spend analysis on an ongoing basis to take a more strategic approach to pharmaceutical procurement. Reflecting national trends, Veterans

Department of Veterans Affairs**Agency Profile**

Mission Highlights: To restore the capability of those who suffered harm during their military service; to ensure a smooth transition as veterans return to civilian life in their communities. Operates a health care system to provide about 3.8 million veterans health care through 163 hospitals and more than 800 outpatient clinics nationwide.

Organizations: Veterans Health Administration, Veterans Benefits Administration, and National Cemetery Administration.

Spending: In fiscal year 2003, contract spending on goods and services totaled \$8.5 billion. Purchase card spending accounted for another \$5 billion, which includes about \$3.1 billion under the agency's prime vendor program.

Sources: GAO and FPDS.

Affairs' pharmacy procurement costs have risen significantly in recent years, consuming an increasing percentage of the department's health care budget. The \$2.1 billion the agency spent on such items in 2000 were primarily for prescription drugs and their dispensing, but also included some supplies and over-the-counter drugs. To mitigate this increase in pharmacy procurement costs, the agency created a pharmacy benefits management strategic health group in 1995 that analyzes pharmaceutical spending trends across all medical facilities and employs various procurement arrangements for purchasing prescription drugs at substantial discounts (GAO, 2001; 2002b). According to the agency, the pharmaceutical procurement standardization program led to savings of \$394 million in fiscal year 2003 alone.

Veterans Affairs has also made progress in the areas of medical and prosthetics supplies and equipment. In fiscal year 2001, the agency purchased about \$500 million in medical-surgical supplies and \$1.1 billion in medical equipment and prosthetics. For example, VA created a national prosthetics spend database that extracts procurement data from all medical facilities' systems and organizes data on purchased items into commodity categories, such as wheelchairs and aids for the blind. The agency's prosthetics strategic health group also formed a number of commodity teams with stakeholders from across the medical facilities and health care regions to use spend analysis to identify commonly used items that can be purchased at substantial discounts under a national contract.⁸ The prosthetics group also uses spend analysis to monitor medical facility compliance with the national contracts and to ensure

potential savings are realized. As of June 2004, the group's spend analysis and strategic-sourcing efforts have resulted in 23 national contracts and accumulated more than \$57 million in cost avoidance.

The agency is just beginning to develop a spend analysis tool for medical and surgical supplies and high-technology medical equipment. Specifically, it is working with a contractor to create uniform medical-product names for an agencywide spend analysis system. When the system is fully operational in fiscal year 2006, it will automatically extract medical supplies and equipment procurement data into a central data warehouse, organized by common categories of products. Until this system is fully operational, this year the agency decided to form several cross-functional commodity teams to pursue new national contracts on 45 categories of high-technology, high-cost medical equipment and supplies (such as magnetic resonance imaging and ultrasound equipment).

Department of Health and Human Services

Agency Profile

Mission Highlights: HHS is the United States government's principal agency for protecting the health and welfare of all Americans.

Organizations: National Institutes of Health, Administration for Children and Families, Food and Drug Administration, Centers for Medicare and Medicaid Services, Centers for Disease Control and Prevention, and Indian Health Service, to name a few.

Spending: In fiscal year 2003, contract spending for goods and services totaled \$6.7 billion; purchase card spending accounted for another \$392 million.

Sources: GAO and FPDS.

Since 2003, HHS has been obtaining spend analysis and procurement consolidation advice from outside consultants to help reduce the department's operating costs and redirect the savings to programs. Like other agencies, procurement activities in HHS were operating under a decentralized environment of independent, transaction-oriented buying processes, with limited visibility over the agency's total procurement spending.

For example, HHS has conducted a spend analysis of commonly contracted products. In its first phase, \$100 million in yearly spending for thousands of office-related products such as custodial supplies, office

supplies, office furniture, office equipment (such as photocopiers and facsimile machines), and peripheral information technology products (such as computer monitors and scanners) was analyzed to identify opportunities for significant savings to purchase card buyers through agencywide discount agreements.⁹ Between May and July 2004, HHS awarded the first agreements to three vendors for the office supplies, custodial products, and peripheral items.¹⁰ HHS estimates the potential savings from these discount agreements range from 7 percent to 54 percent and could yield at least \$9.5 million in annual savings for the department on just the office supplies, office equipment, and information technology peripherals. Later this year, the agency will work with its consultant to do a new round of spend analysis to identify potential categories and savings opportunities in the next phase of the strategic-sourcing initiative for products.

In a second initiative, HHS procurement headquarters hired a consultant in August 2003 to support a newly organized agencywide group of 100 senior procurement and other key managers to work on consolidation of services acquisitions.¹¹ One of the contractor's key tasks was to conduct a spend analysis of almost \$4.9 billion in fiscal year 2002 HHS contract actions to identify high-volume or high-dollar common services for consolidation. Twenty-four categories--such as security guards and patrol services and office administrative services--were subsequently identified for possible consolidation--totaling almost \$1.7 billion in value.

The consultant's plan included steps to organize and segment HHS contract workload and spend data into categories of services and suppliers. This step was intended to help the services acquisition consolidation working group identify opportunities across divisions to reduce the number of suppliers where competition for new agencywide contracts is practical. However, according to the working group's project officer, in view of small business and contract-bundling requirements and the long lead times needed to obtain division consensus on new contract arrangements, the working group decided instead to pursue alternative consolidation strategies in the near-term.

As a result, HHS headquarters officials expect the working group to finalize criteria and a timeline for selecting existing division service contracts that would be listed in an HHS-wide database that other division purchasers might use before initiating their own new, stand-

alone contracts. Potential contract categories include temporary services, information technology services, focus groups, and conference management and support.

Department of Agriculture

Agency Profile

Mission Highlights: To support agriculture production by ensuring a safe, affordable, and accessible food supply; caring for agricultural, forest, and range lands; supporting sound development of rural communities; expanding global markets for agricultural and forest products and services; and working to reduce hunger in America and throughout the world.

Organizations: Forest Service, Food and Nutrition Service, Farm Service, Rural Housing Service, and Rural Development Service, to name a few.

Spending: In fiscal year 2003, contract spending on goods and services totaled \$4.3 billion. Purchase card spending accounted for another \$572 million.

Sources: GAO and FPDS.

Agriculture is currently using the results of a consultant's October 2001 spend analysis as updated with more recent spending data to obtain favorable prices on small purchase card buys through agencywide discount agreements with major vendors. The contractor analyzed almost \$2.1 billion in fiscal year 2000 spending data from across the agency, organizing the agency's spending in terms of commodities and suppliers to identify high-volume, high-dollar areas that could yield significant savings and other benefits and also identifying 24 commodities for the agency's more detailed review.¹²

In 2003, Agriculture's procurement management division began to use this spend analysis, competitively awarding an agencywide discount agreement with a national office supply vendor that yielded savings of \$1.8 million to the agency's purchase card holders--a price 10 percent less than the vendor's Federal Supply Schedule contract prices.¹³ To receive the discounts, registered agency purchasers must use the national office supply vendor's electronic catalog and ordering system.

Building on this experience, Agriculture recently began to use the consultant's spend analysis to improve its purchase card buying power in additional commodity areas. A temporary "electronic marketplace" subcommittee was organized in January 2004, including representatives from across the agency. According to the co-chair, this subcommittee is

using the consultant's spend analysis and updating it with more recent data on spending with major vendors to help negotiate more favorable prices based on the agency's dollar volume. By October, the subcommittee plans to implement at least three agencywide discount agreements comparable to the 2003 agreement.

In the future, Agriculture plans to provide automated and repeatable spend analysis, data-mining, and reporting capabilities that identify opportunities for savings through negotiated volume discounts. These will be available through electronic catalogs as part of a redesign and modernization of its agencywide acquisition system, an effort that will be complete in about two years.¹⁴ Agriculture began this effort upon recognizing that the current multisystem environment does not provide an integrated, streamlined, or consistent approach to procurement and does not effectively support the agencywide goal for electronic commerce between agency purchasers and suppliers.

To develop its spend analysis capabilities, Agriculture will create a centrally maintained data warehouse to be shared by agency procurement and financial management organizations. This warehouse will extract and capture all Agriculture procurement data, to be supplemented with business intelligence and organizational data from internal and external financial and corporate sources.¹⁵ Once the warehouse is in place, it will allow for comprehensive spend analysis and reporting on procurement in real time, on issues such as the opportunities to be pursued for agencywide discount agreements with major suppliers for specific commodities and the extent of small business utilization.

The departments of Justice and Transportation have not used spend analyses yet to focus management attention on changing the way they purchase goods and services to foster a more strategic approach. One of the obstacles to using spend analysis cited by both was the lack of comprehensive, detailed, and reliable spending data. Nevertheless, future use of spend analysis could become an important tool in their efforts to streamline their administrative functions or improve procurement performance.

Department of Justice

Spend analysis could be useful in assisting the Department of Justice to implement its November 2001 strategic plan, which established

<p>Department of Justice Agency Profile Mission Highlights: Enforcing laws in the public interest and protecting the public from terrorist and criminal activity. Organizations: Federal Bureau of Investigations, Office of Justice Programs, Federal Bureau of Prisons, Drug Enforcement Administration, U.S. Marshal Service, and Bureau of Alcohol, Tobacco, Firearms, and Explosives. Spending: In fiscal year 2003, contract spending on goods and services totaled \$4 billion. Purchase card spending accounted for another \$588 million.</p>	<p>Department of Transportation Agency Profile Mission Highlights: To ensure a fast, safe, accessible, and convenient transportation system that meets vital national interests and enhances the quality of life of the American people, today and into the future. Organizations: Federal Aviation Administration, Federal Highway Administration, Federal Transit Administration. Spending: In fiscal year 2003, contract spending on goods and services totaled \$6.7 billion. Purchase card spending accounted for another \$442 million.</p>
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Sources: GAO, FPDS, and Federal Aviation Administration.

streamlining, eliminating, or consolidating duplicative functions as key elements of supporting the agency's new counterterrorism mission. In February 2004, high-level discussions were begun to plan cross-cutting initiatives to eliminate duplication and cut overall agency operating costs, so that funding can then be redirected to other critical tasks. The agency also formed a core group of financial and management executives responsible for overseeing the streamlining and efficiency initiatives.

Officials told us that it is too early to say if the new core group's efforts would include analysis of Justice's spending trends or considering broad-based structure, process, and role changes to support a more strategic approach to procurement, although some agency officials are familiar with the concepts. Officials said that some Justice components had made incremental progress in consolidating and leveraging certain categories of spending, such as litigation support services, jail detention space services, and prison system medical supplies. Officials also told us that the agency will similarly look into pursuing a comprehensive approach to buying Web-based training services, jail guard services, and employee household relocation services.

In the near term, Justice officials questioned the agency's ability to analyze spending trends effectively, even though the officials agreed that such an analysis could benefit the agency. Lack of a single acquisition and financial management system makes it difficult to collect accurate and complete spending data and identify opportunities for coordinated purchasing, the officials said. Although the agency is trying to establish a single system, it is not likely to be in place until 2009.¹⁶

Before the single system can be put in place, we discussed with these officials the prospects for using existing contract and purchase card data that the agency feeds into the FPDS, in the same way that Agriculture and HHS have used such data to support their spend analysis efforts. Justice officials expressed interest in potentially using FPDS data for this purpose. According to the procurement executive, for financial audit purposes, Justice has been analyzing purchase card data and had already obtained better insight into what goods and services were being bought across the agency and opportunities to leverage buying power in return for lower prices from vendors.¹⁷ Given that Justice has almost \$5 billion in annual procurements, agency officials acknowledged that their streamlining and efficiency efforts could be substantially aided by the expanded use of spend analysis to consider taking a more strategic approach to procurement.

In commenting on a draft of this report, the agency reports that it is working to identify additional opportunities for purchase card savings through current discount agreements and has begun analyzing FPDS data to identify savings opportunities. We commend the agency for expanding purchase card spending analyses, which is also responsive to previous recommendations aimed at achieving agency savings through the purchase card program GAO (2004a). Moreover, by taking the promising first step to analyze FPDS data on contract spending for goods and services--which accounted for another \$4 billion in 2003--we believe that Justice will be able to identify many more opportunities for leveraging buying power and achieve even more significant savings in the future.

Department of Transportation

Transportation's senior procurement officials told us that they plan to use spend analysis to support ongoing implementation of strategic procurement practices across the agency. According to these officials,

such support should be facilitated by the favorable experience Transportation has already gained from similar cross-cutting strategic procurement planning to modernize information systems and standardize computer equipment as part of a fiscal year 2007 office relocation of agency headquarters. Under the agency's chief information officers' council, commodity councils are being formed to help the agency move to a common operating environment and leverage buying power for information technology goods and services.¹⁸

According to these officials, the agency currently has no spend analysis capability, but a first step was taken this year through the agency's procurement performance management program that could help drive the adoption of a more strategic approach to buying goods and services.¹⁹ A general analysis was conducted of fiscal year 2003 FPDS data for \$1.6 billion in agency contracts, sorted by the categories of research and development, other services, and products.²⁰ A more in-depth agencywide analysis has yet to be achieved, however. Officials told us more detailed analysis of spending trends--for example, by high-dollar, high-volume commodity and vendor categories--was inhibited by workload constraints and their concerns about the accuracy of FPDS data and the lack of more specific product and service information. Nevertheless, they indicated that in the future, spend analysis could become an important tool in the agency's procurement performance management program. Specifically, in commenting on a draft of this report, the senior procurement executive indicated that agency leadership supports additional funding in fiscal year 2005 to enhance spend analysis capabilities. He also told us the agency is evaluating software options for a future agencywide spend analysis system as part of the ongoing financial information system modernization.

**AGENCIES HAVE NOT ADOPTED FULL RANGE OF SPEND
ANALYSIS BEST PRACTICES AND LACK SOME SUPPORTING
STRUCTURE, PROCESSES, AND ROLES**

Veterans Affairs, HHS, and Agriculture have made good progress using spend analysis to improve their procurements, and they have adopted some elements of a strategic approach. Like the private sector's experience which indicates that implementing spend analysis can be challenging and take time, these three agencies have not had a lot of time to adopt the full range of private sector best practices with regard to automating, extracting, supplementing, organizing, and analyzing data

that covers all of their procurement spending. Also, to one degree or another, they have not created the type of supporting structure, processes, and roles leading companies institute to make the best use of the knowledge gained and foster a more strategic approach to buying goods and services. The extent to which agencies can do both will determine their success in achieving substantial savings and performance improvements. Private sector experience suggests that agencies that start with effective spend analysis programs will be better able to institute the changes needed to move into a more coordinated, leveraged purchasing environment.

Veterans Affairs has earned a world-class reputation for highly cost-effective pharmaceutical procurement practices, which include spend analysis as well as supporting structure, processes, and roles (See Appendix I, Table 1). Its progress in making similar improvements in its procurements of other medical supplies and equipment has been slower, however, and its efforts related to clinical care or facilities support services are in their very early stages.

A March 2004 inspector general's audit report, for example, noted that the agency's efforts to reform medical supplies and equipment purchasing practices since 2002 have not yet translated into significant national contracting results and medical purchasing cost savings. The audit recommended increasing efforts to pursue aggressively more national contracts that, if implemented, could achieve about \$82 million per year in savings.

A spend analysis tool that would examine Veterans Affairs' medical supplies and equipment spending trends will not, in fact, be ready before 2006, when best practices--such as automated compilation of purchase data, extracted from facilities' procurement and vendor payment systems and supplemented and organized--will be put in place for use by established commodity teams.

The agency is also beginning to focus on taking a more strategic approach to acquiring services for veterans medical facilities from contract providers. In May 2004, the Secretary announced that Veterans Affairs must more effectively purchase contract health care services for veterans (such as skilled nursing and laboratory services) by leveraging its purchasing power as a national healthcare system. The Secretary directed that a national clinical-contracting strategy be drafted by November 2004 that would identify high-value, competitively priced

purchasing options for obtaining medical services from contract providers throughout the country. In addition, in commenting on a draft of this report, the agency stated its intent to pursue national contracts for non-clinical services as well. Facilities now contract locally for a wide variety of support services, such as facilities maintenance, housekeeping, and food service.²¹ According to the agency, both efforts will use spend analysis as appropriate. However, we believe it will be difficult for the agency to accomplish this objective since the new spend analysis tool, expected in 2006, will only capture data on medical supplies and equipment spending trends.

HHS asked its division heads to begin planning for departmentwide consolidation of procurement activities in April 2003. Although headquarters managers had worked with consultants to conduct spend analyses to improve their knowledge of overlapping and duplicative procurement spending, they had no plan to develop an automated tool to repeat the process and only a small number of consolidated procurement actions were expected to result. (See Appendix I, Table 2.)

In June 2004, however, HHS procurement managers told us that an agencywide working group was going to propose obtaining commercial software to develop an automated spend analysis system to compile the necessary data and generate standardized reports. As result, they believe that HHS' spend analysis efforts could make use of an automation tool in the future to enable the process to be repeated consistently, obtain data from HHS sources such as financial management systems, and analyze data on a continual basis. The proposal was intended to augment ongoing plans for an HHS-wide standard electronic procurement system to be phased in over the next year or so. According to these officials, details on the proposed system's spend analysis capabilities are forthcoming, pending approval and funding to implement it.

Agriculture's current spend analysis efforts are also not automated, include no financial management data such as vendor accounts payable systems, and do not analyze data on a continual basis (See Appendix I, Table 3). The agency does have plans to have an agencywide spend analysis system in place by 2006, but the system will be a centralized tool shared by component organizations that may or may not choose to chart their own strategic procurement paths.

A temporary subcommittee in the meantime is reviewing some agencywide spending data to identify a few categories of high-dollar

purchase card vendors for use in negotiating discount agreements. However, a senior procurement policy official told us that a large-scale strategic approach to buying goods and services may be neither feasible or advisable, given the agency's highly diverse missions and decentralized operations. When it comes to changing the buying culture across the agency, the agency wants to use spend analysis to create attractively priced discount agreements with a few vendors that agency purchasers will be encouraged, not mandated, to use. Although he indicated that Agriculture may establish a few agencywide commodity councils in the future to pursue more areas for consolidated buying, he did not anticipate creating new structure, processes, and roles within the agency.

Aside from their spend analysis activities, the three agencies have not consistently created the type of supporting structure, processes, and roles leading companies institute to foster a more strategic approach to buying goods and services. While Veterans Affairs has used the best practice of establishing commodity teams that coordinate buying strategies for pharmaceutical, prosthetics, and more recently high-cost, high-technology medical equipment and supply items, the same practice has not been used to coordinate buying strategies for services. Outside of forming single, cross-agency working groups to leverage a few categories of supplies commonly bought by purchase cardholders, Agriculture and HHS have not fully embraced viewing procurement as an agencywide process for streamlining acquisitions, saving money, and increasing the quality of purchased goods and services when compared to the current decentralized environment of independent, stand-alone contract actions. Agriculture and HHS have not adopted the best practice of using cross-functional commodity teams to establish a network of technical experts to support volume and technical leveraging of agency spending.

CONCLUSIONS

When the government faces enormous fiscal pressures and a growing budget deficit, agencies' transformations of their business processes is more important than ever if the agencies are to get the most from every dollar spent. Leading companies that have successfully used spend analysis as a foundation for their procurement activities set an example for how the federal government can more effectively leverage its buying power.

Federal agencies such as the Departments of Veterans Affairs, HHS, and Agriculture can achieve significant benefits using spend analysis best practices to support a more strategic approach to buying goods and services. Like leading companies, agencies that establish an effective spend analysis program can then achieve a total-spending perspective across the agency; make the business case for collaboration in joint purchasing rather than fragmented purchasing, create supporting structure, processes, and roles to assign accountability and exercise oversight; identify potentially hundreds of millions of dollars in procurement savings opportunities by leveraging buying power; and identify opportunities to achieve other procurement process efficiencies such as reducing duplication in purchasing, supporting small and minority-owned business utilization, and improving supplier performance. In contrast, agencies such as the departments of Justice and Transportation, which have yet to make extensive use of spend analysis and may well miss out on the opportunity to achieve savings to the same extent possible as other agencies.

RECOMMENDATIONS FOR EXECUTIVE ACTION

To help ensure that the varying spend analysis efforts by Veterans Affairs, HHS, and Agriculture go further in emulating the best practices of leading companies and that these agencies have the supporting structure, processes, and roles in place to effectively use the results of spend analysis, we are making the following three recommendations:

- * To identify, track, and evaluate what clinical care and support services are being purchased by veterans' medical facilities, the Secretary of Veterans Affairs should direct procurement headquarters officials to expand the planned development by 2006 of an automated medical supplies and equipment spend analysis system also to capture spending data on services. Such expansion should support automating, extracting, organizing, supplementing, and analyzing spending trends for clinical care and support services in the same way that improvements aimed at medical supplies and equipment are being made. The agency's new spend analysis system needs to include healthcare-related services' procurement data to improve decision makers' knowledge and help them identify opportunities for leveraged buying, including the planned development of a national strategy to contract for services.

- * To address agency leadership's direction to eliminate redundant management activities, the Secretary of Health and Human Services should direct headquarters' procurement officials to identify additional steps needed to adopt a more strategic approach to acquiring goods and services. HHS headquarters' procurement officials should also be directed to consider using current financial and procurement management information systems to extract the type of spending data on an automated and repeatable basis that the agency needs to identify opportunities to leverage its buying power, reduce costs, and provide better management and oversight of key suppliers. Such data would include what categories of goods and services are being acquired; how many suppliers are being used for specific categories; and how much HHS is spending on specific categories, in total and with each supplier. Their assessment should also address the creation of supporting structures, processes, and roles as necessary, such as the establishment of cross-functional commodity teams, to help obtain the necessary buy-ins across the agency's divisions, eliminate duplication of effort, and improve the coordination and volume discounting of high-dollar, high-volume categories of goods, services, and suppliers on an ongoing basis.
- * While waiting until 2006 for the planned agencywide spend analysis system to come online, the Secretary of Agriculture should assess whether the agency's temporary electronic marketplace subcommittee provides sufficient structure, processes, and roles for analyzing spending trends on an ongoing basis and supporting a more strategic approach to acquiring goods and services. Agriculture's assessment should address expanding the subcommittee's current narrow focus on leveraging the agency's almost \$600 million in purchase card buying power, to also yield discounts applicable to larger contract actions across the range of goods and services being acquired and whether the establishment of cross-functional commodity teams would help obtain the necessary buy-in across the agency's diverse mission organizations and improve the coordination and acquisition of high-dollar, high-volume categories across a wide range of goods and services.

In light of the significant potential for savings and performance improvements that the two agencies not using spend analysis could achieve, we recommend that the Attorney General of the United States and the Secretary of Transportation direct officials responsible

for procurement and financial management and other appropriate stakeholders to step up the process of gaining knowledge of their spending to take a strategic approach to procurement, adopting the type of best practices employed by leading companies. Specifically, we are making the following two recommendations:

- * Justice and Transportation should assess using current financial or procurement information systems such as FPDS and purchase card data on an automated and repeatable basis to extract the type of spending data that the agencies need to identify opportunities to leverage the agencies' buying power, reduce costs, and provide better management and oversight of suppliers. Such data would include what categories of goods and services are being acquired; how many suppliers are being used for specific categories; and how much the agency is spending on specific categories, in total and with each supplier.
- * Once an initial spend analysis can be completed to arm the agencies with the knowledge of such opportunities, Justice and Transportation should assess whether their current procurement structure, processes, and roles are adequate to support a more strategic approach to acquiring goods and services, for example whether cross-functional commodity teams would provide more effective, coordinated management of high-dollar, high-volume categories of goods, services, and suppliers on an ongoing basis.

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2. Fiscal year 2003 data for contract actions (about \$30.2 billion) and purchase card spending (about \$7 billion), Federal Procurement Data System and the Federal Aviation Administration.
3. Fiscal year 2003 is the last year for which complete governmentwide data is available. FPDS is the federal government's central database on contracting and purchase card transactions. Additionally, we obtained summary fiscal year 2003 contract action data from the Federal Aviation Administration, which is not required to report their procurement activities to the FPDS.

4. The current system contains known errors, as discussed in Government Accountability Office (2003c). Although we have not fully assessed the extent of reporting errors, we have found sufficient problems to warrant concern about the current reliability of FPDS information. As we understand the design of an ongoing modernization of that system through FPDS-Next Generation, many of the sources of the errors in the current FPDS should be eliminated. In the short term, as the transition to FPDS-Next Generation occurs, we have made recommendations to improve data reliability.
5. Between 2000 and 2003, we studied procurement best practices of eleven companies--Bausch & Lomb; Brunswick Corporation; ChevronTexaco; Delta Air Lines; Dell; Dun & Bradstreet Corporation; Electronic Data Systems Corporation; Exxon Mobil Corporation; Hasbro, Inc; International Business Machines; and Merrill Lynch & Co., Inc. Our past work focused on how the companies used best practices to improve procurement of services where costs were increasing faster than for procurement of goods. However, the companies told us that they followed the same practices to procure goods. See GAO (2002a; 2003a).
6. A commodity is a category of products or services segmented by commonality of materials or service type. The term does not imply an expendable or noncomplex item. This grouping will allow volume and technical leveraging of organizational spending and the establishing of a network of commodity experts.
7. Companies use commodity teams to make sure they have the right mix of knowledge, technical expertise, and credibility. The teams can vary in size but generally include representatives from a company's procurement unit, internal clients or users of the product or service, and the budget or finance office. The teams analyze spending data, define internal needs and requirements, and conduct market research. This approach has helped companies to define their needs better and to identify, select, and manage suppliers and, in turn, helped ensure that users' needs were met at the lowest total costs to the companies.
8. According to Veterans Affairs, national contracts are used to leverage the agency's buying power on health care commodities identified as high usage. The agency develops the requirements for national contracts with clinician customer input and openly competes

the requirements. The agency's national contracts are generally firm, fixed-price requirements-type contracts, with a base year and four 1-year option periods. Veterans Affairs exercises options after market research reveals that the prices are fair and reasonable and the award is in the best interest of the government.

9. Although HHS intends to market the discount agreements to agency cardholders for small purchase card buys, HHS divisions with larger-dollar orders will also be able to buy the same discounted items through the agencywide agreements. However, the agreements are not mandatory sources of supply for either purchase card holders or other agency buys.
10. HHS anticipates awarding two more agreements in August 2004 for the office furniture and equipment categories.
11. HHS hired the consultant to provide spend analysis services and procedural, technical, and briefing support to and collaboration with the agencywide workgroup to help implement various phases of the services acquisitions consolidation initiative. Workgroup members include representatives from the Office of the Secretary and all HHS divisions, such as the National Institutes of Health, Centers for Disease Control and Prevention, and the Food and Drug Administration.
12. For the spend analysis, Agriculture furnished the consultant fiscal year 2000 data files extracted from FPDS and the agency's Purchase Card Management System. The contractor analyzed about 473,000 contract transactions totaling about \$1.6 billion and 2.3 million purchase card buys totaling \$467 million. The contractor organized the spend data into 52 commodity categories of products and services, such as agricultural machinery, construction services, fleet maintenance, telecom equipment, and office supplies and paper.
13. Under the Schedules program, the GSA negotiates to obtain discounted prices on a wide range of commercial goods and services on its contracts with multiple vendors.
14. Since 2002, Agriculture has carried out a cross-agency effort, with contractor technical and program management support, to develop, test, and phase-in the enterprise Integrated Acquisition System to replace more than 40 different procurement systems in use across

eleven agencies and administrative offices. Agriculture plans to have the replacement system fully operational by October 2006.

15. When fully operational, the data warehouse will automatically extract procurement data for all contract actions processed via the Integrated Acquisition System and extract procurement data on all purchase card buys captured in the agency's purchase card management system.
16. In 2002, the agency launched a unified financial management system program to replace six major accounting systems now in use with one agencywide system. Plans for the new system include integration of financial and acquisition management, assure access to timely information, and speed up business process and decision making. Justice hired a contractor in March 2004 to provide software for the new system and plans to replace legacy systems between fiscal years 2005 and 2009.
17. In fiscal year 2003, Justice had 12,842 purchase cardholders that accounted for over \$588 million in small purchases of goods and services for \$2,500 or less. For more information, see GAO (2004a).
18. According to the deputy senior procurement executive director, the agency's architectural review board was expected to approve a charter and an enterprisewide information technology procurement business process to guide the commodity councils' activities.
19. Since 1995, Transportation procurement activities have implemented this program as a major initiative to improve procurement performance. This program assists procurement managers in targeting areas for improvement based on the results of specified metrics chosen for their importance to the administration, agency management, or agency customers.
20. The general analysis did not include data for the Federal Aviation Administration or organizations transferred to the Department of Homeland Security (Coast Guard and Transportation Security Agency). Transportation's analysis used fiscal year 2003 FPDS data for contract actions in excess of \$25,000. Dollars analyzed totaled \$1.6 billion and were sorted by research and development (6 percent), other services (84 percent), and products (10 percent). Transportation did not analyze vendor or individual product and service details available in the FPDS records.

21. For more information on opportunities to improve Veterans Affairs' purchasing practices and increase savings, see GAO (2004c).

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APPENDIX I
GAO Analyses of Agencies' Spend Analysis Practices

We obtained information about agencywide spend analysis efforts through interviews with Veterans Affairs, HHS, and Agriculture procurement headquarters officials and documents they provided to us. We reviewed this information and also discussed with agency officials how their efforts compared to leading companies' best practices identified in our recent work (GAO, 2002a; 2003a).

In analyzing agencies' practices, we compared their efforts with the five key processes that companies adopt that enable them to conduct effective and ongoing spend analysis, which are:

- * Automation--data automatically compiled.
- * Extraction--essential data culled from accounts payable and other internal systems.
- * Supplemental information--additional data sought from other internal and external sources.
- * Organization--review data to ensure accuracy and completeness; organize data into logical, comprehensive commodity and supplier categories.
- * Analysis and strategic goals--using standard reporting and analytical tools, data analyzed on a continual basis to support decisions on strategic-sourcing and procurement management in areas such as cost cutting, streamlining operations, and reducing the number of suppliers. Scope generally covers an organization's entire spending.

The following tables summarize our analysis of agencies' spend analysis practices.

TABLE 1
Veterans Affairs Spend Analysis Practices

Spend Analysis Process	Agency practice
Automation	Automated compilation of pharmaceutical and prosthetic and sensory aid purchase data into two central databases, which are updated continuously. Automated compilation of medical supply and equipment purchase data but not clinical care and support

	services into a central database will be available in 2006.
Extraction	Pharmaceutical and prosthetics spend analysis covers all veterans' medical facilities purchases. Facilities' pharmaceutical purchase and vendor payment data are extracted from centralized commercial distributors' on-line ordering and delivery systems. Prosthetics data extracted from multiple medical facilities' procurement and vendor payment systems. In 2006, standardized medical supply and equipment data will be extracted from facilities' procurement and vendor payment systems. None will be extracted on facilities' purchases for clinical care and support services.
Supplemental Information	Veterans Affairs obtains pharmaceutical sales and payment data from centralized commercial distributors' on-line ordering and delivery systems. The agency's chief logistics office analyzes weekly summaries of bankcard vendor's transactions with the agency. The agency recently required purchase card program managers to consolidate quarterly reviews from the cardholders and analyze purchases.
Organization	Pharmaceutical and prosthetics spend analysis databases fall into logical comprehensive categories of commodities and suppliers. Veterans Affairs is organizing and standardizing procurement data on medical supplies and equipment purchases; a spend analysis database is planned for completion in 2006. In 2004, a naming standard will be developed for each high-technology/high-cost medical product given a national contract. To track compliance with contracted products, a standard name will have to be used when buying. Veterans Affairs will not organize facilities' clinical care and support services procurement data into logical, comprehensive categories of commodities and suppliers.
Analysis and strategic goals	Commodity teams are continually analyzing pharmaceutical and prosthetics spending data to make decisions in contracting and procurement management. In 2003, Veterans Affairs saved \$394 million through discounted pharmaceutical national contracts. As of June 2004, prosthetics contract savings were more than \$57 million. By 2006, standard reporting and analytical tools will be in place for medical supplies and equipment purchases, which new commodity teams will use to help reduce the number of suppliers, cut costs, streamline operations, and address the agency's small business goals. Veterans Affairs' spend analysis system plan does not include purchased clinical care and support services, however.

Source: GAO analysis of agency information.

TABLE 2
Health and Human Services Spend Analysis Practices

Spend Analysis Process	Agency practice
Automation	HHS furnishes services procurement data to one consultant and products procurement data to a second. While both use commercially available automation tools to compile data for more rapid spend analyses, these are one-time or periodic requirements. No automation tool is available to allow HHS to consistently repeat the spend analysis process, but the agency may consider obtaining such a system.
Extraction	HHS wants its acquisition consolidation initiative to cover as many of its services buys as possible, and provided its spend analysis consultant services contract data from one 2002 database. (Contracts for \$25,000 or less were not included.) For its product-focused strategic sourcing initiative, HHS provided a consultant with data from 2002 on office supplies, office equipment, office furniture; peripheral information technology (IT) equipment, and custodial supplies. Furnished data was extracted from two contract databases, actions for \$25,000 or less, and for more than \$25,000. This year, the HHS consultant will receive 2003 purchase data for all other products, extracted from the same two databases, as well as data from HHS financial management sources, such as accounts payable systems.
Supplemental Information	To identify the top-selling office product suppliers, HHS provided the consultant data from the agency's bankcard vendor on all purchase card transactions, as well as other information from prospective commodity suppliers on estimated sales to agency purchasers. This enhances awareness of the volume and scope of HHS purchasing. This year, the HHS consultant will receive 2003 purchase card data as well. HHS sought no additional spend analysis data for the services acquisition consolidation.
Organization	In 2003, both consultants cleansed and validated data that HHS furnished based on their spend analysis experience and supply market knowledge. The consultants used the federal product and service classification to organize categories of commodities and suppliers. This helped them identify and rank high-dollar, high-volume opportunities to target for office product strategic-sourcing and services acquisition consolidation. In 2004, the

	consultant will analyze new data involving small and larger purchase card and contract buys. The data will be organized into logical, comprehensive categories of products and supplies to identify and rank top categories to target for additional strategic sourcing.
Analysis and strategic goals	HHS is not analyzing data on a continual basis. The agency had two consultants analyze data in 2003 and will have one consultant do a second round of product-focused spend analysis in 2004. HHS is using that analysis to support strategic sourcing decisions for national discount agreements with a few major suppliers for office supplies, office equipment, office furniture, IT peripherals, and custodial supplies. HHS will use the consultant's spend analysis of services acquisitions to plan areas where existing contracts can be used by agency division purchasers to leverage buying power and reduce the need for new stand-alone contracts. As of June 2004, HHS is continuing its planning and anticipates shared implementation of at least some of the existing contracts in 2005.

Source: GAO analysis of agency information.

TABLE 3
Agriculture Spend Analysis Practices

Spend Analysis Process	Agency practice
Automation	In 2001, Agriculture furnished 2000 data to a spend analysis consultant, who used commercially available automation tools to compile the data to expedite the analysis to fulfill a one-time requirement. Agriculture plans to create an automated spend analysis tool to extract data from the single acquisition system to begin in October 2006. The data is expected to be compiled into a new shared data warehouse that will extract components' procurement data as the new system goes on line. The warehouse is expected to contain business intelligence and data mining capability so that the spend analysis process can be repeated at the agency or component levels.
Extraction	Agriculture wanted the 2001 spend analysis to cover all products and services procurements other than the nonprocurement-related agricultural commodity purchases. To accomplish this, the

	agency extracted data from three databases--contract actions for \$25,000 or less; contract actions of more than \$25,000; and the purchase card management system. Spend analysis did not include financial management data such as accounts payable systems.
Supplemental Information	Agriculture's purchase card management system obtains data from the bankcard vendor on all purchase card transactions with agency cardholders. The agency furnished 2000 purchase card data for the 2001 spend analysis. In 2004, Agriculture obtained up-to-date purchase card data on agency transactions with high-dollar, high-volume vendors from its bankcard vendor to supplement the 2001 spend analysis.
Organization	Agriculture's spend analysis consultant cleansed and validated 2001 data the agency furnished, based on its spend analysis experience and supply market knowledge. The consultant used federal product and service classification to organize agency spending into 15 categories encompassing 52 more detailed subcategories. Information technology (IT) for example, included telecom equipment, IT equipment, office technology, and IT/telecom services. The spend analysis consultant also proposed a feasibility classification strategy that could be used for more detailed opportunity analyses of high-potential subcategories.
Analysis and strategic goals	Agriculture is not analyzing data on a continual basis. Following the completion of the initial spend analysis in October 2001, Agriculture used the results to support decisions for an agencywide office supply discount agreement with a major supplier. An agreement was awarded in 2003 so that Agriculture purchase cardholders could use the supplier's Web-based catalog to obtain small purchases of a wide range of office supplies at reduced prices. In 2004, Agriculture created a temporary subcommittee of procurement managers to review the 2001 spend analysis report and more recent purchase card data where available. The agency will identify a few more high-dollar, high-volume product subcategories where purchase card buying power can be leveraged through discount agreements with major suppliers.

Source: GAO analysis of agency information.