# **Innovation and the procurement process: Goods and services guide**

## What is innovation?

Innovation is about turning ideas into reality. Innovation in procurement is about using the competitive market to come up with better ideas before turning them into reality. It also includes improvements to internal procurement processes although this is not the focus of this note.

## Why encourage innovation?

Most businesses exist in a competitive market. Competition drives innovation—most businesses must continually improve to survive. The competitive market can be better placed than government to come up with innovative solutions. It can help you access market experience and expertise to come up with new and different ways to achieve your desired outcomes.

Encouraging innovation also provides a catalyst for suppliers to improve their products and services which in turn, gives them cutting edge products or services marketable to the wider business community.

This note does not cover intervening in the market to correct market failures or addressing market immaturity.

Such intervention strategies require specific expertise and the application of economic models that are outside the scope of standard procurement activity conducted by departments.

## Integrating innovation into the procurement process

To embed innovation in the procurement process, take action in the following four areas:

1. Organisational alignment
2. Early market engagement (EME)
3. Early supplier engagement (ESE)
4. Innovation support activities

These four areas are described in more detail over.

### Organisational alignment

Innovation should be considered throughout the procurement process from policy/program development and project definition through to contract management.

The greatest potential for innovation occurs at the beginning of the procurement process. Once you have entered into a contract, the potential for innovation is constrained by the conditions of the contract. However, there may be opportunities for innovation if driving continuous improvement is part of the contract structure.

Consider innovation when you:

* identify organisational programs, deliverables and key procurement categories
* prepare your organisation’s procurement strategy (innovation is part of the procurement planning and vendor/supplier analysis sections)
* develop your contract management planning strategy to identify categories of procurement that lend themselves to flexibility in supplier engagement; and
* develop your organisation’s supplier engagement plan.

Supplementary actions include:

* designate people in your organisation as ‘innovation sponsors’ who can help others to encourage innovation when engaging with the market and developing the optimal path to market strategy
* consider innovation as a value for money component; and
* where relevant, monitor supplier performance to ensure that benefits of any innovation have been delivered.

### Early market engagement (EME)

EME is about interacting with the market to gain an understanding of market dynamics and whether there is potential to improve the delivery of your desired outcomes.

Major EME touchpoints in the procurement process are:

* Create procurement activity plan
* Identify category
* Gather market intelligence
* Conduct complexity assessment for each category
* Conduct capability assessment to match complexity of procurement
* Develop category contract pricing strategy

There is no defined process for EME, but any action should be open, transparent and fair. All engagement processes should proceed with clear instructions on how to manage information, communication and intellectual property (IP) to address any reluctance on the part of suppliers to fully disclose IP.

Similar categories of goods and services across multiple departments offer further opportunities for market-based solutions and establishing whole of government contracts.

One way to systematically conduct EME and review developments and trends in particular market sectors is to carry out regular strategic market sector scanning with business associations.

The outcome of early market engagement can help you:

* refine procurement requirements within a category of goods and services
* provide a better understanding of the capability of market sectors relevant to the category
* assess the capacity of the market and structure of the relevant market sector
* assess the scope for small and medium enterprise (SME) participation
* identify issues and risks and
* clarify optimal path to market strategies.

Ideally, your strategic market scanning will inform your market engagement strategies when preparing your procurement activity plan. Disclosing how you will conduct your engagement with the market will reduce ad hoc responses from suppliers.

### Early supplier engagement (ESE)

ESE occurs at the sourcing stages of the procurement process and builds on information gained from the early market engagement activity:

The major ESE touchpoints in the procurement process are:

* Early supplier engagement
  + Review procurement requirement
  + Conduct market analysis and review
  + Develop plan for market engagement
* Procurement process
  + Evaluate negotiate and select supplier
  + Create a contract
  + Commit to a contract
  + Manage contract

Key steps to foster innovation in the sourcing stage include:

* Providing the market with sufficient time to scope and respond to the procurement requirement. Small and medium enterprises (SMEs) with limited resources need time to research the procurement requirements, analyse options or seek partners to fully address the project scope.
* Adopting a multi-stage approach to the market can help suppliers understand the specifics of the procurement requirement. For the department, a multi-stage approach can inform whether further refinement of the procurement requirement is appropriate.
* Flexibility in the conduct of sourcing—wherever appropriate, adopt the practice of permitting alternative bids and variants to stated requirements in the specifications.
* Structuring specifications—adopting text, clauses and conditions that are understood by the relevant market. The focus should be on outcome and output statements and generic performance requirements that are aligned with the findings of the market engagement phase. Differentiating areas of the specification as core and non-core can indicate to suppliers where alternate solutions can be proposed and how it will be considered and measured in the evaluation process.
* Engaging with suppliers in an open and transparent manner to promote competition and maximise innovative solutions—consider briefing sessions where relevant and involve the Industry Capability Network (ICN) early in the process as a channel for contacting appropriate suppliers.

### Supporting innovation

There may also be limits to adopting innovation where the organisation is bound by regulatory or legislative obligations.

An innovative solution can increase the risk to the organisation or clients of services provided by the organisation.

### Activities that can support innovation

#### Pilot project

Piloting a project can demonstrate the suitability of a proposal before fully committing. Conducting a pilot project/program requires clear parameters for proceeding regarding:

* management of intellectual property (IP) used and/or gained during the pilot
* the eventual ownership of IP
* how the IP will be made available if the pilot leads to an open approach to a wider market
* what confidentiality arrangements apply; and
* how participants/stakeholders in the pilot are to be managed

#### Inducements and rewards

Sharing risks and potential savings with suppliers is the most common form of inducement and reward. Other strategies could consider:

* cost sharing from savings;
* longer term contracts to repay investment by the supplier(s); and
* allocating ownership of IP developed under contract with the supplier.

In the latter case, consider licensing back ongoing access to IP developed under contract. Legal advice should be sought when arranging licensing and variations to IP ownership.

#### Risk sharing

The general principle is that risks should be apportioned to the party responsible for its management and mitigation. Moving from the position that the supplier bears all risks can offer cost savings to your organisation from lower insurance and risk premiums arranged by the supplier.

#### Briefings, seminars and workshops

These are integral to your organisation’s ongoing supplier engagement strategy to keep the market informed of core government policy directions and departmental processes.

#### Partnership arrangements

These involve an element of joint benefit and embody consideration of inducement, reward, and risk sharing. Non-financial benefits for suppliers arise from being able to leverage involvement with government through acknowledgment and public recognition. The key element for successful partnerships is to proceed based on a clear understanding and agreement as to what the partnership entails, how it will operate and what it will deliver to the respective parties in partnership.

#### Unsolicited proposals

This is an approach by a person or business with an offer for your organisation outside of any formal approach to the market by your organisation for the supply of specific goods or services. The key issue is to ascertain whether the proposal has merit to justify adoption. For more information, refer to the [Guide to managing unsolicited proposals.](https://buyingfor.vic.gov.au/managing-unsolicited-proposal-goods-and-services-procurement-guide)

## Using this guide

This guide accompanies the [goods and services supply policies.](https://buyingfor.vic.gov.au/goods-services-supply-policies) There are 5 supply policies:

* Governance policy
* Complexity and capability assessment policy
* Market analysis and review policy
* Market approach policy
* Contract management and disclosure policy

This guide supports all five policies.

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