

Category Management and Strategic Sourcing Update #2

Date: November 15, 2021

To: General Government and Licensing Committee

From: Chief Financial Officer and Treasurer

Wards: All

SUMMARY

This report is to provide an update to the General Government and Licensing Committee in the fourth quarter on the contract with Ernst and Young to support Phase 2 of Category Management and Strategic Sourcing (CMSS) as requested by the City Council on December 16, 17, and 18, 2020.

Considerable progress in the program has been made since the beginning of Phase 2 in January 2021. To date, the City has achieved confirmed benefits of \$15.96M through the application of a strategic approach to procurement. Further opportunities worth \$43.26M are in progress, with \$26M expected to be completed by end of 2021. Together, these represent \$59.22M in benefits, or 54% of the \$110M target set at the beginning of Phase 2.

The City has an additional pipeline of opportunities that are yet to be started, that is expected to yield benefits of \$39.10M, bringing the total to \$98.32M. Apart from the \$15.96M of confirmed benefits, all the remaining benefits are an estimate and will need a concerted partnership with various divisions to refine and achieve the expected benefits.

It is to be noted that the total benefits pipeline of \$98.32M is lower than the aspirational target of \$110M set at the beginning of Phase 2. The decline in the estimated benefits is due to a variety of reasons, including, but not limited to:

- Reduced scope of work to be included in strategic sourcing by Divisions
- Insufficient time to execute strategic sourcing approach due to urgent service delivery priorities
- Divisional hesitation to different approaches for complex and high-spend service delivery projects
- Resource constraints in the Divisions involved in strategic sourcing projects as well as PMMD.

Achieving the aspirational benefits target requires collaboration and partnership between PMMD and the divisions responsible for the delivery of programs. It is envisaged that through the category management governance model, appropriate support will be generated on key strategies to achieve City's long-term capability uplift and procurement transformation goals.

Overall Purchasing and Materials Management Division is on track to be able to continue with CMSS without the support of EY by the end of the contract, post-May 2022.

RECOMMENDATIONS

The Chief Financial Officer and Treasurer recommends that:

1. General Government and Licensing Committee receive this report for information.

FINANCIAL IMPACT

The efforts of the CMSS sourcing projects with the assistance of EY is planned to achieve an estimated \$98.32M in confirmed benefits by the end of phase 2 (May 31, 2022). Benefits achieved from the strategic sourcing events can be in the form of either operating or capital budget cost reduction or cost avoidance. For each strategic sourcing event, CMSS and the Division involved work with Financial Planning to confirm how benefits may be treated in the Division budget. How benefits may be treated will depend on whether it will impact the operating budget or the capital budget, and whether the budget is tax-based or rate-based. Since the estimated benefits are lower than the original aspirational target of \$110M, the success fees payable to EY will be calculated and reduced proportionately.

Any cost savings or cost avoidance as a result of Category Management and Strategic Sourcing initiatives have been considered as part of the annual budget process, and will continue to be during future years.

DECISION HISTORY

At its meeting of December 16, 17, and 18, 2020, City Council adopted, as amended, GL19.2 entitled "Authority to Enter into a Non-competitive Contract with Ernst and Young to Support Category Management and Strategic Sourcing", which authorized the Controller to enter a contract with Ernst and Young to assist the Purchasing and Materials Management Division on implementing Phase 2 of CMSS with a goal of achieving \$110M in benefits. Council directed that staff report on the progress of the contract in Q2 and Q4 2021 and at the close out of the contract in 2022. A copy of the decision document can be found at:

<http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2020.GL19.2>

At its meeting on June 29, 2021, General Government and Licensing Committee received for information the first Category Management and Strategic Sourcing Update Report. A copy of the decision document can be found at:
<http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2021.GL24.16>

COMMENTS

Phase 2 of implementing Category Management and Strategic Sourcing is still on track to meeting the contract obligations and putting the City in a position to be able to continue on with Category Management without the support of a consultant by the end of the contract (end of May 2022). The work being performed by the EY team as well as the traction and progress being made on the fixed deliverables and the strategic sourcing initiatives have met the expectations of the City.

To date we have achieved \$15.96M of confirmed benefits through five strategic sourcing projects, and sixteen opportunities leading to additional estimated benefits of \$43.26M are in progress. Three additional opportunities, expected to lead to benefits of \$17.26M, are scheduled to be started shortly. In addition to the above, the CMSS group is working with various City divisions to validate seven other opportunities with estimated benefits of \$21.84M.

As mentioned in the summary section of this report, concerted level of participation from divisional stakeholders is required to achieve expected benefits from all opportunities, especially those that are yet to be validated. The CMSS team and the Divisions continue to closely work on identifying additional strategic sourcing initiatives and to ensure that a potential strategic sourcing initiative fits both within the goals of the Division and the timing of getting a new contract in place. The benefits pipelines can still change depending on resource constraints and Divisional agreement to move forward on the opportunity.

This report will reflect a progress update in three sections - Strategic Sourcing, Operationalization of Category Management and other Deliverables, and Training and Recruitment to provide the Committee with a detailed update on all the aspects of the CMSS program.

Strategic Sourcing

CMSS has been working with City divisions to identify and execute savings opportunities in five spend categories:

- Construction and Maintenance,
- Facilities,
- Fleet,
- Refuse Management,
- Technology.

During this phase, Transportation Services, Toronto Water, Engineering and Construction Services, Parks Forestry and Recreation, and Facilities have worked collaboratively with CMSS to identify and execute financial benefit opportunities that

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have either already resulted in or are expected to lead to these benefits for the City in the near future. While CMSS has made considerable progress in developing a collaborative relationship with some divisions, further alignment is needed with other divisions to ensure a proportional contribution of these divisions to the benefits pipeline.

The table below shows the distribution and expected benefits from these opportunities.

Table 1: Summary of total operating and capital benefit opportunities¹

Category	Participating divisions	No. of opp.	Savings/Cost Avoidance (\$M/Yr.) ¹				
			Confirmed ¹	In-progress ²	To be started ³	To be explored ⁴	Total
Construction and Maintenance	Engineering and Construction Services	3	0	1.40	7.20	0	8.60
	Toronto Water	12	8.00	17.64	10.06	6.41	42.11
	Transportation Services	5	5.00	20.24	0	0	25.24
Facilities	Corporate Real Estate Management,	3	1.30	0	0	4.93	6.23
	Parks, Forestry & Recreation	1	1.66	0	0	0	1.66
Fleet	Fleet Services	1	0	0	0	1.50	1.50
Refuse Management ⁵	Solid Waste Management	0	0	0	0	0	0
Technology	Technology Services	2	0	1.58	0	0	1.58
	City Clerks	1		1.60	0	0	1.60
City-wide	All divisions	3		0.80		9.00	9.80
Total		31	15.96	43.26	17.26	21.84	98.32 ⁶

¹ The annual savings/cost avoidance reflects the potential annual average savings/cost avoidance based on the contract terms and contract length, which may result in a partial benefit to a particular budget year. For a detail breakdown of cost avoidance and cost reduction on confirmed opportunities, please see Table 2 below. For To be started and

To be explored opportunities, estimates of cost avoidance and reduction may be provided once execution starts.

² Currently, \$35M is estimated to be cost avoidance and \$8M is estimated to be cost reduction. These estimates may change upon conclusion of the sourcing event.

³ There are currently 3 opportunities to be started. Two opportunities with benefits of \$10.06M are scheduled to begin in November 2021. One project with benefits of \$7.20M is scheduled to begin in March 2022.

⁴ To be explored are opportunities that the CMSS team has identified to possibly conduct a strategic sourcing procurement for. However, these have not been explored, validated, or approved with the respective Divisions at the time of this report. Therefore, the estimated benefits included are an estimate based on limited market intelligence and internal data. Should these opportunities move from To be explored to In-progress, the benefits will be updated to reflect an actual estimated amount of benefits.

⁵ While no opportunities for the Refuse Management Category were identified for the work with EY, there are opportunities in the longer term that will be explored.

⁶ For any capital-based programs, how benefits will be treated will be determined with Financial Planning as part of the quarterly variance review and could include reallocation to other capital programs to offset any added capital needs.

The table below lists all the opportunities for which we have confirmed benefits so far.

Table 2: Confirmed benefits from completed opportunities:

Category	Division	Opportunity name	Cost Reduction (\$M/Yr.) ¹	Cost Avoidance (\$M/Yr.) ¹	Confirmed benefits (\$M/Yr.) ¹
Construction and Maintenance	Toronto Water	Multi-year contracts for Watermain re-lining program - Pilot	1.30 ²	0	1.30 ²
Construction and Maintenance	Transportation Services	Sourcing of operational maintenance and capital construction services for traffic signals and electrical equipment	1.30	3.70	5.00

Category	Division	Opportunity name	Cost Reduction (\$M/Yr.) ¹	Cost Avoidance (\$M/Yr.) ¹	Confirmed benefits (\$M/Yr.) ¹
Facilities, Fleet and Refuse Management	Parks, Forestry & Recreation	Provision of arboricultural services at various City of Toronto locations	0	1.66	1.66
Construction and Maintenance	Toronto Water	Construction service for basement flooding program	0	6.70	6.70
Facilities, Fleet and Refuse Management	Corporate Real Estate Management	Operational and capital replacement services for HVAC across multiple divisions	0.09	1.21	1.30
Total			2.69	13.27	15.96

¹ The annual savings/cost avoidance reflects the potential annual average savings based on the contract terms and contract length, which may result in a partial benefit to a particular budget year.

² As this relates to a rate-based capital program, these benefits may need to be reallocated to offset any added rate-based capital needs as determined with Financial Planning.

In the case of the completed strategic sourcing events noted in Table 2 above, the completed sourcing events involving Parks, Forestry and Recreation with respect to arboricultural services and Toronto Water with respect to basement flooding program had benefits in the form of cost avoidance, thus avoiding any further impact on the 2021/2022 budget.

Regarding the completed sourcing events for Transportation Services with respect to traffic signal and Corporate Real Estate Management with respect to replacement of HVAC across multiple divisions, the benefits are in the form of both cost avoidance and reduction.

With respect to the completed sourcing event for Toronto Water involving watermain relining, the benefits are in the form of cost reduction. However, given that the contract is part of Toronto Water's capital program and is rate-based, the realization of the cost reduction identified will be retained by Toronto Water as rate-based funding for use on other Toronto Water funding requirements.

The realization of the benefits confirmed by the execution of the contracts from strategic sourcing events also depends on how the contracts are ultimately managed.

Operationalization of Category Management and other Deliverables

This section describes CMSS progress against the deliverables linked to operationalization of category management.

CMSS has been working on improving the reporting of the benefits achieved, rolling out the category management governance, and designing a contract management and supplier relationship management process that will assist Divisions in managing their contracts and drive further savings through contract management. Designing a contract management and supplier relationship management process will also assist the City to address various Auditor General Reports with respect to contract management. This includes the Auditor General's Report entitled "Previous Audit Reports – Common Themes and Issues" adopted by Council in June 2020, which noted that one common theme is the City's need to strengthen the oversight and accountability for contracts. These deliverables will help the City establish a standard approach to managing suppliers and contracts. The table below shows the progress made against operationalization of category management at the City.

Table 3: Progress against the Operationalization of Category Management

Workstream	Deliverable	Status	Target Completion date	Description of tools and templates developed (for completed deliverables)
Governance	D1 - Refined governance process	Completed	Apr' 21	1. Meeting agenda 2. Meeting template 3. Templates for checkpoints 1, 2 and 3
	First series of CMLT sessions	Completed	Apr' 21	
Reporting	D2 - Performance dashboard	Completed	May' 21	1. Two reporting dashboards 2. Metric database for 12 metrics
Supplier relationship management	D3 - SRM playbook	Final review and approval	Q4, 2021	1. One SRM playbook 2. Supplier segmentation scorecard

Workstream	Deliverable	Status	Target Completion date	Description of tools and templates developed (for completed deliverables)
	D4 - SRM training material	Final review and approval	Q4, 2021	One SRM training document
Contract management	D5 - CM playbook	Final review and approval	Q4, 2021	1. One CM playbook 2. Opportunity assessment tool
	D6 - CM training material	Final review and approval	Q4, 2021	One CM training document
Contract compliance analysis	D7 - Contract compliance reports	In progress	Q4, 2021	-
Category strategy development	Facilities, Fleet and Refuse Management category strategy	To be started (Nov. '21 start) ¹	Q1, 2022	-
	Technology category strategy	To be started (Feb. '22 start)	Q2, 2022	-
	Construction and Maintenance category strategy	To be started (Feb. '22 start)	Q2, 2022	-

¹ We are currently on track to start the development of category strategies for the Facilities, Fleet and Refuse Management in November. The start dates for the development of category strategies for the Technology and, Construction and Maintenance category strategies are estimates and subject to change.

Recruitment and Training

Recruitment

As the Category Management Team continues to mature and continues to hire roles into 2021, dependency on EY will reduce as we move through Phase 2 of the engagement. The main team consists of 15 FTEs, of which 12 are filled (7 permanently filled, 5 temporarily filled, and 3 vacancies).

The recruitment of 1 Category Lead and 5 permanent Sourcing Specialists is estimated to be completed in Q4, 2021.

In order to expand on the work that the CMSS team has been doing and to be able to increase the capacity of the opportunities that can be completed each year, PMMD has put forth a Business Case for additional resources in 2022. The recommendation for additional resources is to address the fact that potential opportunities yet to be explored across the City's divisions are complex, have a high dollar value and in some cases high risk which require a more strategic approach to the procurement of the goods/services for the City and in some cases Agencies as they are involved. Therefore, increasing the current number of resources within CMSS would bolster the existing team to be able to do more strategic procurements and to help continue to build stronger strategic relationships with the Divisions.

As CMSS recruits and on-boards new hires, the EY team is working with the CMSS team to carry out the strategic opportunities identified. This will help the City expedite service levels in a resource constrained environment, especially in the context of the recovery phase past the current pandemic.

Training

The training and development of the Category Management team by EY is an ongoing process. The key activities that are performed for each of the strategic sourcing projects are led by the Category Management team within the Purchasing and Materials Management Division with EY supporting at arm's length. The intent is to have the team fully trained on all the functions that EY is currently fulfilling during the Phase 2 period. This will include further training and development of category management strategies, processes, governance, and data analytics.

On-the-job coaching and training are being provided to the teams throughout the development and delivery of category management activities. This training provides the necessary hands-on knowledge sharing specific to each opportunity, providing the ability to perform the task more independently in the future. This training is in addition to formal training sessions that are appropriately developed, planned, and delivered in Q2, 2022.

The following Table 4 outlines on-the-job training delivered thus far with EY's support.

Table 4: On-the-job training provided by EY to the CMSS team

#	Topic	Attendees	What is being provided:
1	Conducting Category Management Leadership Team Sessions (CMLTs)	Category Management team - Category Managers, Category Leads and Sourcing Specialists	- Provided a walkthrough of the developed governance process and supported document development for the first Category Management Leadership Team Sessions (CMLTs). - Coached the team to develop documents and conduct the second round of CMLTs with minimal external support

#	Topic	Attendees	What is being provided:
2	Calculating baseline and estimating benefits	Category Management team (as stated above) + applicable divisional stakeholders	- Coached the team for ten projects, during development of project charters to develop the baseline and estimate the forecasted benefits using market intelligence, historical spends and trends as well as economic market impacts.
3	Developing negotiation strategy and conducting negotiations	Category Management team (as stated above), applicable divisional stakeholders and Purchasing and Materials Management Division Buyers	- Coached the team for six projects, prior to conducting supplier negotiations (Watermain relining, Electrical Maintenance Contracts, Winter Maintenance, SAP Ariba, Electronic Voting Machine, Basement flooding). The conducting negotiations training has also been provided to Divisions who may require an nRFP without the involvement of CMSS (ex. Office of the CISO).

Formal training session roll-out for CMSS is delayed due to Covid-19 and resourcing complications.

CMSS is also monitoring the level of external support received by the Category Management team to track City's ability to sustain the procurement transformation independently post May 2022. Resource capability is being tracked across six dimensions for each strategic sourcing project, as shown in Table 5 below.

This table is intended to track the level of support provided by the EY team to the CMSS staff through the various phases of each strategic sourcing project. This table includes the 3 roles within CMSS; Category Managers, Category Leads and Sourcing Specialists. As there have been new members added to the CMSS team the later part of 2021 they are in the learning phase of their development. With the continued focus on their development we are confident that the team will all be above 8.5 by the end of March 2022 ahead of the departure of the EY team. As the CMSS team members ramp up on each of the dimensions, the support level from EY will decrease.

Table 5: CMSS Resource Capability

#	Name	Ability to perform tasks independently (scored on a scale of 10) ¹
1	Opportunity identification and kick-off	4.9
2	Overall strategy development	5.5
3	Negotiations	6.0

#	Name	Ability to perform tasks independently (scored on a scale of 10) ¹
4	Benefits confirmation	6.2
5	Stakeholder management	7.0
6	Project management	7.0

¹ Average score for all CMSS personnel

Currently, CMSS staff is able to conduct stakeholder and project management activities with limited support from EY. Key areas of capability development are around sourcing strategy development, negotiation strategy development, benefits calculations and confirmation, and identification of new strategic opportunities. On-the-job trainings, and in planned areas formal trainings, are being provided to continue skill development. The goal is to have each of the CMSS team members perform as close to 10 on the rating scale by May 2022. In the event they have not achieved a 10, we will continue to work with those individuals without EY to further develop their skills in the necessary areas.

Each CMSS resource is rated by their managers on a scale of 1 to 10, 1 being lowest and 10 being the highest, across the six dimensions mentioned above. The scores provided in the table above are an average of all the scores received for that dimension.

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SIGNATURE

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