FACTORS AFFECTING THE PROCUREMENT OF ERP IN THE PUBLIC SECTOR

Charity Nkonge
Masters Student, Jomo Kenyatta University of Agriculture and Technology, Kenya

Dr. Agnes Njeru
Lecturer, Jomo Kenyatta University of Agriculture and Technology, Kenya

ABSTRACT

Re-insurance industry plays a key role in Kenya’s development. Very few companies have deployed Enterprise Resource Planning (ERP) system in their management of the supply chain despite the fact that ERP touches many core aspects of a firm’s operations; hence, its successful implementation and use are critical to performance and survival of an organization. In most cases, implementation of ERP fails at the procurement phase with translucent factors. The main objective of this study was to determine the factors that affect the procurement of ERP. The specific objectives were to find out whether Information Technology Infrastructure, Legislative Issues and Supply Chain Functions Management affect the procurement of ERP. This Research adopted an exploratory study with a case study of Kenya-Reinsurance Corporation Ltd (Kenya Re). The target population for the study was the 120 employees in Kenya-Re. The sample size was 50 respondents selected from different departments using stratified sampling method. Data was collected using questionnaires. Data analysis was done using descriptive statistics such as frequency tables and charts and inferential statistics correlation analysis using SPSS computer software. The study concluded that IT infrastructure in public companies is not flexible because hence leading to either delays or avoidance of ERP procurement. The study also concluded that the main legal cause of non-procurement of ERP in the public sector is as a result of external environment. The study recommends that ERP should be categorized as an essential supply as public policy framework should be enhanced to support faster decision making when it comes to procurement of ERP as it is very essential in the smooth running of the organization. The study also recommends that Public organizations should digitalize all their systems in readiness to the procurement of ERP since all the systems to be supported by an ERP has to be digitalized since a successful ERP implementation requires a fit between the ERP system and the organizational processes it supports. Further research should be carried out to establish the skill levels and the effectiveness of the ERP trainers in public sector.

Key Words: Procurement, Enterprise Resource Planning (ERP), Information Technology (IT), Supply Chain

INTRODUCTION

Due to the rationalization and the penetration of ICT, public companies that wish to maintain high performance standards and maintain relevance in the market have opted to digitize their operations. Procurement of computers and having a network has become a mere requirement in all public sectors as this is no longer a measure of efficiency. Companies in the public sector that wish to be efficient have opted to integrate their functions into one platform. One of the platforms is the Enterprise Resource Planning (ERP). According to O’Brien et al, (2009) Enterprise Resource Planning (ERP) is the technological backbone of e-business, an enterprise transaction framework with links into sales, order processing, inventory management and
control, production and distribution planning, and finance. ERP is a cross-functional enterprise system driven by an integrated suite of software modules that supports the basic internal business processes of a company (O’Brien et al., 2009). ERP provides the right metrics and key performance indicators that can aid the global firm when juggling performance, resources, costs and operational logistics from relocated departments and manufacturing facilities (Shah, 2009). Globally, ERP solutions are applied to streamline business processes across multiple locations and geographies with suppliers, partners and manufacturers leading to significant improvement (almost 70%) in time reduction from order entry to delivery of goods (Weele, 2005). According to Weele, (2005) ERP solutions are critical for an international company’s ability to achieve growth and cost reduction goals by going global. ERP provides integration to globalizing companies but they do not provide quick fix to all market penetration and other business infrastructure (Gunson, 2010).

Enterprise Resource Planning (ERP) systems were designed to solve various organizational problems, and to provide an integrated infrastructure. ERP packages offer advantages to enterprises to achieve various benefits. Sometimes, however, they fail to achieve some of the anticipated benefits for example autonomous and heterogeneous applications co-exist in companies with ERP systems and integration problems could arise. According to Themistocleous, (2010), public organizations in South Africa aim to achieve several benefits by implementing ERP software. These benefits include but are not limited to provide solutions to the problems of legacy systems, reduced development risk, increased global competitiveness and enhancing business efficiency. These benefits can be ascribed to an ideal ERP system. Procurement of ERP software has several drawbacks both within and outside the organization; within the organization the challenges are not limited to the perceived implementation complexity, existing systems integration problems, customization problems, budget constraints, employee and supplier resistance to change and problems with business strategy and competitive advantage (Themistocleous, 2010). These challenges cut across the entire globe thus they are not limited only to the African or local perspective but also the developed nations. Public parastatals which are classified under tier one (by the Government of Kenya) and ministries have got an implicit accountability to their government and their stakeholders in the sense that they would be quickly criticized if they made mistakes (Bendel, 2006).

There have been important developments in Kenya Re business during the last eleven years. First was the phasing out of compulsory cessions in the year 2000 that led to a rethink of the marketing strategies and corporate expectations (Government of Kenya, 2003). The second was the retention of the 18% compulsory treaty cessions to the end of year 2004 (Government of Kenya, 2005). The other significant one was the acquiring of Enterprise Resource Planning software (ERP). Kenya Re achieved this by slashing its dividend for the year that ended 2010 and the results were 30 per cent lower than the 50 cent per share the Board approved in the year 2009. These developments were expected to make Kenya Re one of the companies with the best returns in the insurance industry in Kenya.
STATEMENT OF THE PROBLEM

ERP touches many core aspects of a company’s operations; hence its successful implementation and use are critical to performance and survival (Markus et al, 2010). According to Saxena et al (2009), procurement of ERP faces a lot of bottlenecks which include but are not limited to organizational policies and procedures, non-integration with the existing systems, and the failure to synchronize with stakeholder’s platforms. A study conducted by Stefanou, (2001) found out that at least half of all ERP implementation projects failed in the initial stages of procurement. This study however failed to point out the reasons as to why the procurement fails at these early stages. A study by Markus, (2000) found out that up to 90% of all ERP implementation projects usually go over budget, or end up late and about half of them fail to achieve the desired goals. The same study also fails to point out the reason as to why these projects go over budget or have a high rate of failure. Kenya Re is among the first public sector organizations that have successfully procured ERP software. There are limited studies that have aimed at establishing the major impediments faced during the procurement phase as most studies have concentrated in the implementation of the Enterprise Resource Planning and thus ignoring the possibilities of the failure of the ERP in the procurement stage. This poses a gap which ought to be explored hence this study seeks to fill that gap through a case study of Kenya Re.

GENERAL OBJECTIVE

The general objective of the study was to ascertain the factors affecting the procurement of ERP in the public sector.

SPECIFIC OBJECTIVES

1. To determine the effect of IT infrastructure in the procurement of ERP in the public sector.

2. To ascertain the effects of procurement legal framework on procurement of ERP in the public sector.

3. To determine the effects of supply chain functions in the procurement of ERP in the public sector.
THEORETICAL REVIEW

Agency Theory

Agency theory refers to relationship between two persons, one of whom must be a principal (owner) and the other, an agent (manager). Agency theory therefore, is the theory that explains how best the agency relationship can be used for purpose of governing an organization (Brown Governance Inc, 2004). Kenya Re-Insurance is a listed company and thus the principals are charged with the core responsibility in agency governance, i.e. to select and put in place the auditors (external independent body that audits and reports on integrity of manual reporting and controls), and ensure that there is an efficiency governance system in place. They are responsible for day to day operations and other activities throughout the organization (Sarbanes-Oxley, 2004). The division of responsibility which is inherent in the agency governance mechanism, makes it possible for accountability to be achieved since the flow of power and authority is well defined and understood in the organizations. The management of Kenya-Re who will form the target population of the study is responsible for the management of the IT infrastructure, interpretation of the legislative framework and the management of the supply chain functionalities and hence their input on these effects was sought and used to make inferences.

According to agency theory, the objective of the organization is to maximize shareholder wealth through efficiency. The firms’ performance is judged in this model by profitability and shareholder value. Therefore, managers and Directors have an implicit responsibility to ensure that organizations are run in the best interest of the shareholders. The challenge in agency theory arises from the principal agent relationship occasioned by separation of ownership and executive decision making. Agency cost includes monitoring expenditure by principle such as auditing, budgeting, control and compensation systems bonding expenditure by the agent and residual loss due to divergence of interest between the principal and agent. Fama (2000) argues that separation of ownership and control can be explained as a result of efficient form of economic organization. The theory prescribes stronger directorship and shareholder control, it advocates fundamental function of board of directors to control managerial behavior and ensure that managers act in interest of shareholders which can be measured by the extent to which they adopt new systems in the organization such as the ERP and whether they have a positive effect on the overall performance of the organization.
Management Theory

The proponents of management theory contend that the modern corporation is sophisticated and only experienced and professional management team can effectively direct and control it. Management theorist’s points that agency theory was perhaps workable for the simpler, smaller corporations of Adam Smith’s days, but in today’s world, corporations are large, complex, multi-faceted entities that are challenging to direct and control (Brown Governance Inc., 2004). It is however important to observe that under management theory, direction and control have been ceded by owners and boards (principals and governors) to the management team. The result is a breakdown in accountability as the correct separation of powers (division of duties) fails to occur. According to Cadbury report, this arrangement vests immense discretionary powers on management who may misuse the powers to enhance their prestige and wealth at the expense of the principals.

There is no denying the fact that the modern organization is complex, but it is inappropriate in terms of accountability to allow managers inordinate discretionary latitude over both governance (direction and control) and day-to-day management. In fact, Adam Smith’s position is that the more complex social organizations get, the more people need to specialize, to divide their labor in order to enhance efficiency and internal control. According to Cadbury report, Boards (governors) are not given responsibility for governance because they understand the corporation any better than managers, but precisely because they are not the managers. It is argued that one of the reasons Japan has failed to completely recover from its economic troubles of the early 1990’s is because of its continued adherence to management theory (Brown Governance Inc., 2004).

Stakeholder Theory

The basis of stakeholder theory is that companies are so large and their impact on society so pervasive that they should discharge accountability to many more sectors of society than solely their shareholders. Not only are stakeholders affected by companies but they in turn affect companies in some way. They hold a “stake” rather than simply a ‘share’ in the companies. Stakeholders include shareholders, employees, suppliers, customers’ creditors’ and communities in the vicinity of the company’s operation and the public in general. These key players have a say on whether the organization can procure an ERP by gauging the IT capability. The negative side of the traditional stakeholders is that it’s difficult, if not impossible, to ensure that corporation fulfills the larger objective of all their stakeholders and as such the decision making process is very slow. Such decisions are often revisited even when strategic direction is approved. Stakeholder theory (Blair, 2005) argues that the idea failed to give clear guidance to help managers and directors set priorities and decide among competing socially beneficial lists of
corporate resources and provide no obvious enforcement mechanisms, to ensure that corporations lined up to their social obligations.

**Stewardship Theory**

Stewardship theory argues that managers are inherently trustworthy and not prone to misappropriate corporate resources. Donaldson (2010); Donaldson and Davies (2004) agree with the arguments of the stewardship theory that managers are good stewards of the corporation and diligently work to attain high levels of corporate profits and shareholder returns. The stewardship theory would suggest that control be centralized in the hands of the firm managers. The theory appears to motivate the top management and fails to take the knowledge of the rampant cases of failures of managerial integrity, and managerial competence. This omission makes the stewardship theory inadequate framework of analyzing corporate governance mechanism in the modern corporation. Stewardship theorists assume that managers are good stewards to the firm. They are trustworthy and work diligently to attain high corporate profits and shareholders returns (Donaldson and Davis, 1994) these stewards can cooperate and work closely with the principal to achieve a goal alignment. Agency theory appears to effectively mitigate all the inadequacies of the other governance theories (managerial and stewardship theory). The principle of agency theory is applicable to both private and public sector and all other social organizations.

**EMPIRICAL REVIEW**

According to Weele (2005), three components of IT infrastructure flexibility (connectivity, modularity, and IT personnel) have significant positive impacts on ERP procurement. That is because, these three components facilitate strategic alignment which is a major characteristic of modern business environments. Otieno, (2008) indicates that another major component of IT infrastructure that affects the procurement of goods and services is connectivity; this means that every person, every functional area, and every application in the organization has to be linked to each other as this enables smooth implementation of ERP. As a result, these linking communications throughout the organization are enhanced, and users can rapidly share information across organizational boundaries. This sharing enables rapid response to necessary changes in the firm’s strategy, thus increasing strategic alignment. Markus, (2000) indicates that IT personnel are a factor of infrastructure that affects the procurement and subsequent performance and efficiency of ERP. He indicates that an organization lacking these attributes may experience a delay in the procurement and implementation of ERP.

According to Lozada, (2011), highly-skilled IT personnel are the essential ingredient of applications implementation. These professionals have knowledge of the firm’s set of IT resources and of other technologies in the firm’s external environment (Duncan, 1995). IT professionals’ also have knowledge of the firm’s business processes to be able to facilitate
business strategies with new and existing applications. According to Enshassi (2009), several organizational factors in the procurement entities seem to be influenced by the legal and national institutional set up of public procurement. These organizational factors include procurement budget adequacy, the requirements for procurement planning, the organizational structure including the definition and re-definition of the roles and responsibilities of different organs within procurement entities.

According to Jensen and Stone (2004) factors that delay ERP procurement as a good are as a result of external environmental conditions such as differences in competitive conditions, whether the product is locally available or has to be imported and others may influence the level of compliance to the procurement laws and policies. Where countries have entered into Free Trade Agreements and other economic arrangements, conflicts often arise regarding the degree of compliance with the law as public procurement professionals are torn for example between adhering to the FTA and advancing their countries’ economic development when trying to select between domestic or foreign firms. According to Naimet al, (2010) logistics associated with the overall procurement and implementation of ERP plays a key operational function in enabling the flow of materials and resources between suppliers and customers and as such is a key factor in enabling supply chain flexibility. Failure of supply chain flexibility implies supply chain disruption. A supply chain is never stronger than its weakest link, and that (having a weak link) is the greatest supply chain risk. Transport is the key ingredient of any supply chain (Naimet al, 2010). Balakrishnan et al, 2008 states that the factors that cause supply chain disruption are mostly to do with intra-industry processes as opposed to externally-generated factors such as transportation bottlenecks and external market variations.

**Critique of the Existing Literature Relevant to the Study**

According to Bhatti (2005), adequate IT infrastructure, hardware and networking are crucial for an ERP systems’ success. It is clear that ERP implementation involves a complex transition from legacy information systems and business processes to an integrated IT infrastructure and common business process throughout the organization. This study however fails to recognize the importance of the human resource aspect of infrastructure and thus the expertise needed in the procurement and adoption of the entire system. According to Jensen and Stone (2004), the factors that affect procurement in the public sector include the level of the procurement function within the organizational hierarchy, the length of the procedure for authorization and finances. They elaborate their argument by indicating that the level of the procurement function within the organizational hierarchy influences the speed at which procurement decisions can be taken and the effectiveness of implementation. They failed to elude the fact that with the systems in place in a country such as Kenya that has one authority i.e. Public Procurement Oversight Authority (PPOA); the procurement efficiency can be compromised. As far as procurement human resource capability is concerned, Thai (2001) indicates that the number of staff in the
procurement function in an organization should be sufficient for the procurement task in a specific procurement entity. This literature is not sufficient as no specific formula is provided but organizations are expected to achieve a balance between the size of the procurement task, probably by the volume and frequency of procurement transactions and the procurement values involved. ERP software is a very costly and technical venture thus an understaffed organization can lead to delays in the procurement of the system. Regarding logistics, McKinnon et al., (2010) identifies four sources of logistics practices that cause supply chain disruption of a good or a service. He breaks them into four sides which are; the process side (example, no measures of process performance or non-proactive maintenance), supply side (example, short-notice amendments to suppliers or no vendor measures of performance), demand side (example, infrequent deliveries to customer or poor visibility amongst adjacent processes) and control side (example, continuous product modifications or poor stock auditing). This only concentrates on tangible goods and thus it only assumes that the same parameters affect the supply of systems such as ERP.

RESEARCH METHODOLOGY

Research Design

A case study design was be appropriate in investigating the factors that affect procurement of ERP in the public sector. The study was a cross sectional survey carried out at the Kenya Reinsurance Corporation. The design was useful in describing the characteristics of the firm and determining the frequency of key attributes of the study.

Target Population

A population is a complete set of individuals, cases or objects with some common observable characteristics while target population refers to that population to which a researcher wants to generalize the results of study (Mugenda and Mugenda, 2003). The population for the study was 120 employees in Kenya.

Sampling Frame

Mugenda &Mugenda (2003) defines a sampling frame as a list, directory or index of cases from which a sample can be selected. The sampling frame was divided into strata since not all the 120 employees could be listed here as the sampling frame.
Sample Size and Sampling Technique

The study took 41 percent of the population, a sample size that is considered appropriate (Mugenda & Mugenda, 2003). The study covered a sample of fifty (50) employees which is considered representative of the total population. The sampling technique that was used to select the sample is the stratified random sampling method. This method involved dividing the population into two or more relevant and significant strata based on one or a number of attributes. A stratum is a subset of the population that shares at least one common characteristic. According to Mugenda and Mugenda (2003), a sample size of 10 to 30% is a good representation of the target population. The employees of Kenya Re were divided based on their departments in the organization. As such, six strata came up: Finance, Human Resource and Administration, Property, Reinsurance department, Marketing, Information and Communication Technology, and Others (Executive, Corporate Affairs, Risk, Audit, Records). Simple random sampling technique was then used to pick respondents from each stratum.

Data Collection Instruments

Data was collected using survey questionnaires. The research instruments were self-administered. There are both structured (close-ended) and unstructured questionnaires (open-ended). This method was effective as it was economical (time and money) and was easy to administer as the questionnaires.

Data Collection Procedures

There were two types of data that the study utilized. These are primary and secondary data. For primary data, the researcher was able to collect firsthand information from the respondents. The researcher used questionnaires to collect the primary data from various categories of personnel. According to Kothari (2004), questionnaires are very economical in terms of time, energy and finances. The primary data is useful to the research because it is reliable and accurate. For secondary data the researcher used procurement documents in Kenya Re, The Public Procurement & Disposal Regulations, 2006 and the Public Procurement and Disposal Act, 2005. The researcher collected important information from the library books, annual reports from Kenya-Re, journals and publications from research institutions.

Data Processing and Analysis

The study collected adequate data which was organized in such a way that further analysis and interpretation of data was made easy. The data was edited, coded and classified so as to present the results of analysis in a systematic and clear way. The primary data collected through the
questionnaire was analyzed using descriptive statistics such as measures of variation and measures of central tendency. The study also used correlation analysis to establish the relationship between the dependent variable and independent variables. Data analysis was done using SPSS and Microsoft excel.

Data Presentation

Data Analysis generated quantitative reports through tabulations, percentages, and measure of central tendency. Tables and figures were used to present the results for ease of understanding. Qualitative data was presented in a prose form in a systematic manner where many words of text were summarized. Correlation analysis was carried out to determine the degree of relationship between the dependent and independent variables.

RESULTS AND FINDINGS

Constructs

Since single parameters framed as questions were used to construct a variable, the average score of each construct was computed and used in further analysis mainly the correlation analysis. The final average of each construct ranged from 3.45 and 3.41.

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<th>Table 1: Descriptive Statistics for Constructs</th>
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Multivariate Correlation

Correlation is a measure of the relation between two or more variables. Correlation coefficients can range from -1.00 to +1.00. The value of -1.00 represents a perfect negative correlation while a value of +1.00 represents a perfect positive correlation. A value of 0.00 represents a lack of correlation. The total number of respondents in this study as indicated was 50. Since there were some missing values, the number of respondents in all the independent variables was different. All the tested variables were significant as all of them had a p value of less than 0.05 at 99% confidence interval level (2 tailed). From the correlation analysis it can be observed that legal issues were the major impediments for the procurement of ERP with a correlation value of 0.717.
followed by IT infrastructure with a correlation value of 0.656 and Supply chain functions with a correlation of 0.497.

Table 2: Multivariate Correlation between Variables

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<th>ERP procurement</th>
<th>Legal issues</th>
<th>IT infrastructure</th>
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<td>ERP procurement</td>
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<td>Correlation</td>
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**. Correlation is significant at the 0.01 level (2-tailed).

Discussion of Findings

Most companies failed to procure ERP due to the insufficient IT infrastructure ranging from the cost of the software and high cost of training the members of staff as these parameters had the highest mean scores in a five point likert scale. The study revealed that the main impediments to the procurement of ERP emanate from legal constrains and restrictions. This was evident as issues such as Re-definition of the organization structure and procurement planning were identified as the major issues that affect the overall procurement.

As far as the supply chain functions are concerned, the study revealed that external market variation and management stimulation and appreciation were the major impediments in the procurement of ERP as they had mean scores of greater than 4.0. Other contributing factors were stringent purchasing policies within the organization and compatibility with the existing suppliers.
CONCLUSIONS

This study concludes that IT infrastructure has an effect in procurement of ERP in the public sector. It is clear that most public organizations do not have the capacity to implement the ERP since it is a very expensive venture. The study also concluded that IT infrastructure in public companies is not flexible this is because; they lack sufficient IT personnel to handle a smooth handover of ERP hence leading to either delays or avoidance of the same. It can also be concluded that despite the availability of fiber optic network in Kenya, most public companies do not have sufficient bandwidth to support the cross section sharing of information a factor that has led to the low procurement of ERP.

The study concludes that most public companies fail to procure ERP due to legal issues barring them. The study also concludes that the major legal impediment is the budget allocation and appropriation limit set by the Government. The study also concludes that the main legal cause of non-procurement of ERP in the public sector is as a result of external environment. The study concludes that the main supply chain function that affects the procurement of ERP in the public sector is the integration with the existing systems. Bearing in mind that the public sector is dependent on external suppliers, most stakeholders don’t have the necessary capacity to employ compatible systems thus affecting the procurement.

RECOMMENDATIONS

Public organizations should digitalize all their systems in readiness to the procurement of ERPs since all the systems to be supported by an ERP has to be digitalized since a successful ERP implementation requires a fit between the ERP system and the organizational processes it supports. Public organizations should train their members of staff to have basic IT skills which will enable them to work cooperatively in cross-functional teams using many technologies. In addition IT management should provide the necessary connectivity and modularity that enable rapid organizational response to changes. The management should always be on the alert on the drastic technological changes in ERP and be ready to embrace it by ensuring that the latest ERP system is what is being used and is fully implemented. ERP should be categorized as an essential supply as it has more advantages than disadvantages and hence public policy framework should be enhanced to support faster decision making when it comes to its procurement. Public policies should also be changed to ensure that once an organization has decided to procure the system, sufficient support is accorded to it. The government and management of public companies should schedule meetings to critically discuss areas of improvement with regard to procurement and be able to adopt problematic issues of Enterprise Resource Planning System that arise from the end users.
Public companies should ensure that they are compliant with the public Procurement and Disposal Act of 2006 to ensure a smooth process in the procurement of ERP and other related business process management programs. The government should ensure that directive involving information systems in the public sector are compatible in order to minimize incidences where there is process duplication. Since the ERP is very expensive, the study recommends that due diligence should be exercised in the entire tender process since a small loop hole discovered by the PPOA may render the whole process null and void. Senior managers in public companies should always ensure that there is a regular schedule for deploying ERP system enhancements and that ERP software cost management is well-controlled bearing in mind that the software costs millions of shillings. ERP procurement aims at integrating organizational process thus all departments should fully participate/be involved in the entire procurement process as this will improve efficiency in the organization due to process ownership by the stakeholders. Effective procurement of ERP should consider the supply functions management since it is the key to successful supply chain management.

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