

The Government Executive Series

Outsourcing in Government: Pathways to Value

Executive Summary



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Introduction

¹ Twenty-two national-level governments were researched: Australia, Brazil, Brunei, Canada, China, Finland, France, Germany, Ireland, Italy, Japan, Malaysia, Mexico, The Netherlands, Norway, Portugal, Singapore, South Africa, South Korea, Spain, the United Kingdom and the United States. We also researched Hong Kong, SAR, China.

For the second straight year, Accenture has conducted research into the current state of outsourcing in government. Looking at the trends over time, we have concluded that while outsourcing in the public sector is particularly challenging, some governments around the world have used outsourcing for remarkable results. Forward-thinking governments have established a management framework through sound policy that enables good outsourcing practices. A few leaders have even achieved breakthrough benefits through what we call transformational outsourcing.

We also discovered that outsourcing success does not have the same meaning for every country. Rather, countries seem to be following one of two separate and distinct paths. These paths of increasing outsourcing maturity, which we call trajectories, are very dependent on a government's end goals. One trajectory leads to greater efficiency of existing operations and is marked by extensive use of conventional forms of outsourcing, such as information technology infrastructure. The other leads to organizational transformation and is marked by more extensive use of higher value-added outsourcing forms, in particular, business process outsourcing.

Our 2003 report on global outsourcing maturity, *Outsourcing in Government: Pathways to Value*, taps into the experience of the executives who are helping to drive their agencies toward one of these two strategic endpoints. Accenture conducted quantitative and qualitative research across national governments in 22 countries.¹ We have distilled the major trends in outsourcing today and present them as an executive summary here, with recommendations based on our research and our own experience teaming with clients to build innovative outsourcing solutions. Our goal is to share a more detailed picture of the elements of successful outsourcing to help all government executives improve their outsourcing effectiveness, no matter their ultimate outsourcing objective.

What is outsourcing?

Governments answer the question differently, based on their own political contexts. Different governments may use terms like "sourcing," "competing" or "market-testing" to convey the same meaning.

We recognize these sensitivities; therefore, for purposes of this report, we define outsourcing as:

Contracting with a private-sector firm to take responsibility for a function or process for which the government remains accountable.

Our definition excludes short-term project work and stops short of privatization, where the government no longer has accountability for the function. Do public-sector employees have to move to the private-sector firm for an initiative to qualify as outsourcing? In a word, no. The term outsourcing applies regardless of whether employees are reassigned, retired or transferred to the outsource supplier, or no employees were impacted. Our definition of outsourcing is consistent with the views of close to 90 percent of the executives we interviewed.



Three major trends

Our research uncovered three major trends in outsourcing in government, which are described in the sections that follow:

- Outsourcing in government is growing.
- Value-added objectives drive outsourcing most often.
- Outsourcing maturity progresses along two trajectories.

Outsourcing in government is growing

Outsourcing in government is growing—by as much as 17 percent through 2004 by some estimates.² Our research this year affirms this trend. Seventy-seven percent of the treasury officials we spoke with rated their governments' position on outsourcing as either encouraging or actively encouraging. Additionally, the same proportion of officials expects their country will outsource more functions and processes over the next five years.

What functions and processes are governments outsourcing? Accenture has developed a useful diagram to illustrate the four main types of IT

and business process outsourcing (see Figure 1). Moving up the pyramid, outsourcing increases in strategic value. At the apex, organizations use outsourcing to fundamentally reshape the way they carry out their missions and to achieve notable results in an accelerated time frame. A business transformation outsourcing initiative offers the greatest opportunities for radical improvement because it involves rethinking critical management processes.

Using this pyramid to categorize the outsourcing initiatives we reviewed in our study, we see that much of government IT outsourcing is focused on infrastructure—the lowest level of the outsourcing value pyramid. However, we also see a significant movement up the value ladder. Outsourcing initiatives with a higher potential value—applications and business process outsourcing (BPO)—are as prevalent as IT outsourcing (see Figure 2). We found that, increasingly, governments are not just doing more outsourcing, they are aiming for more value-added objectives as well.

² International Data Corporation, 2001.

Figure 1. The outsourcing value pyramid.

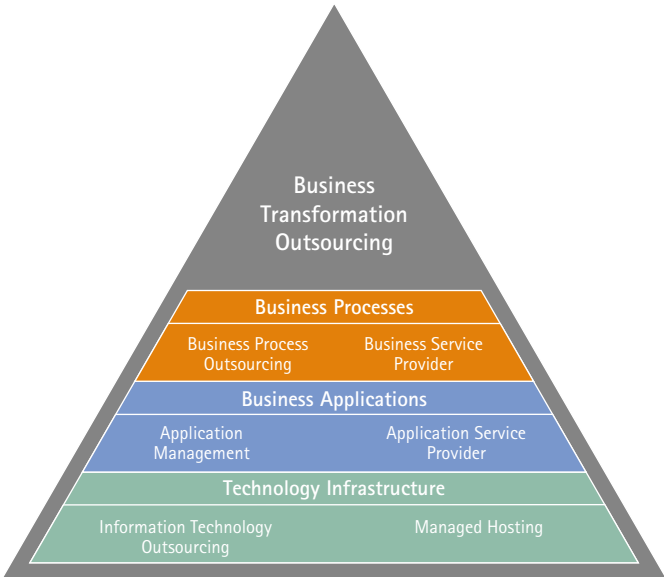
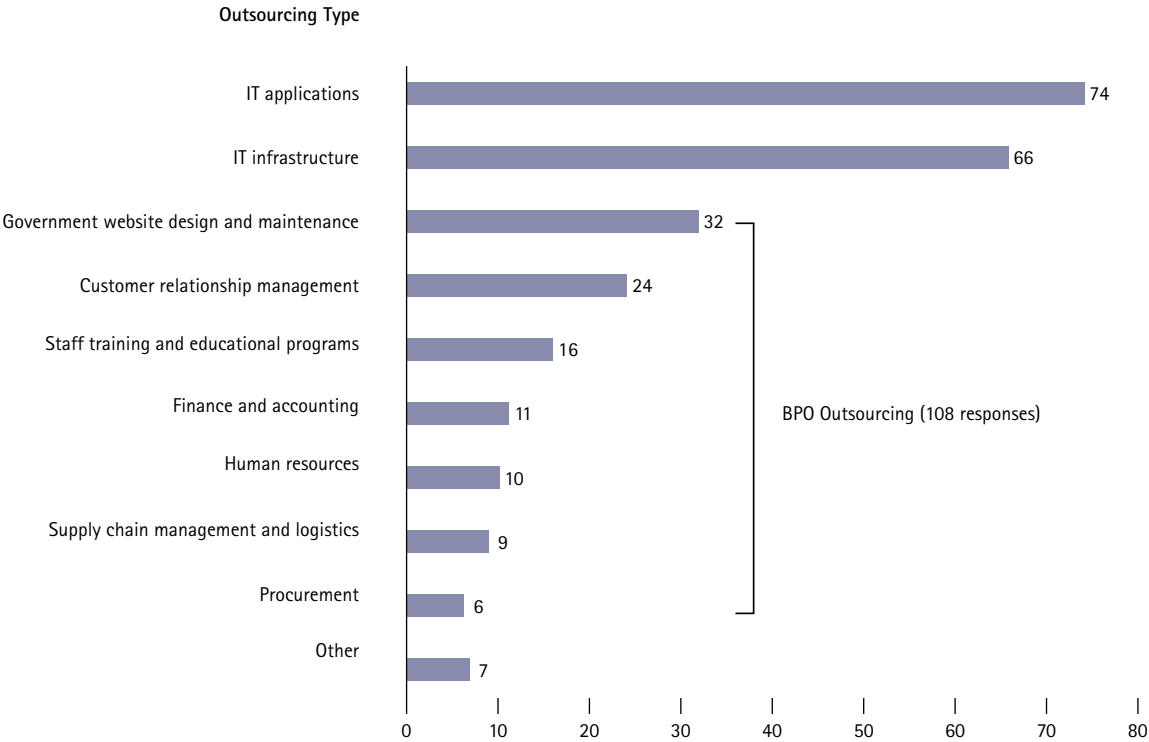


Figure 2. Governments now pursue IT applications and business process outsourcing in greater numbers than they have in the past.



Number of citations (multiple responses possible)
 (Note: The "Other" category includes responses that either fall outside our classification scheme or were left undefined by the respondents.)

Value-added objectives drive outsourcing most often

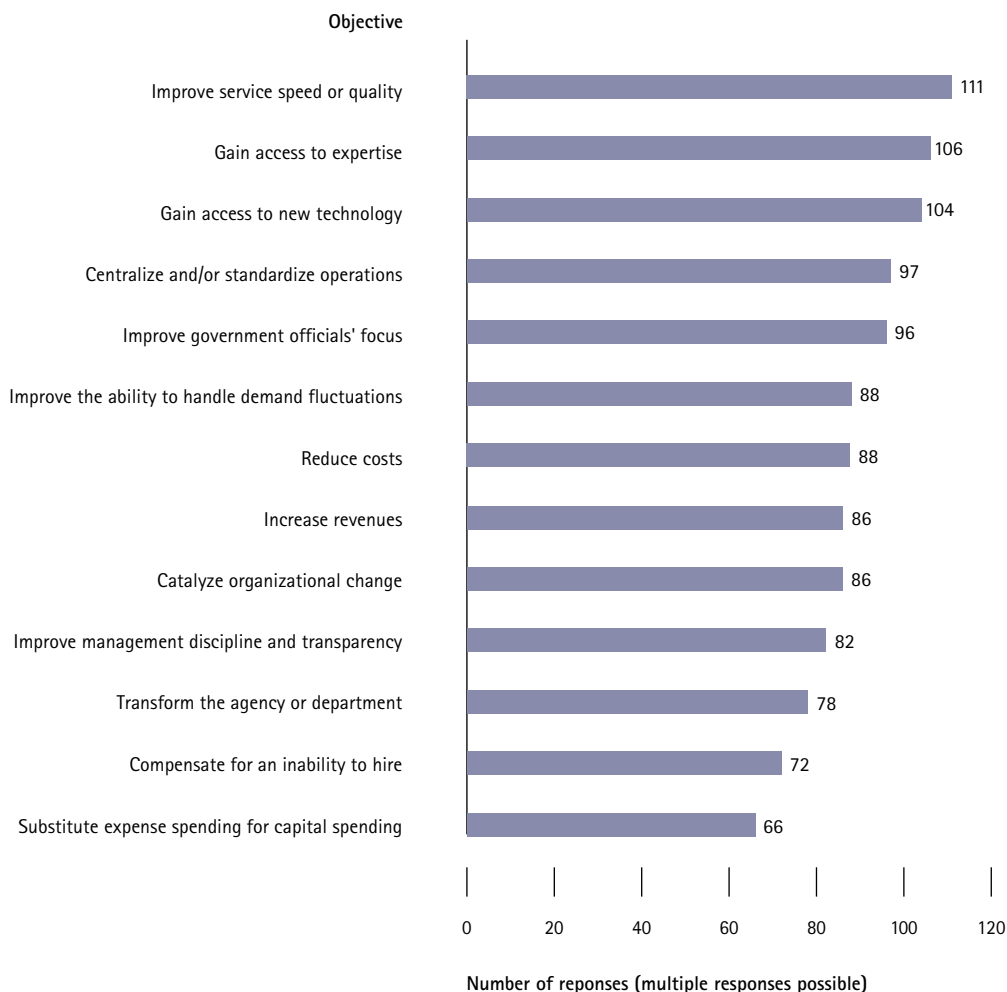
Governments are outsourcing for a broad range of reasons. They are increasingly turning to outsourcing to cope with budget pressures, the need to provide existing and additional services in more citizen-friendly ways and a lack of available expertise and technology to meet these needs.

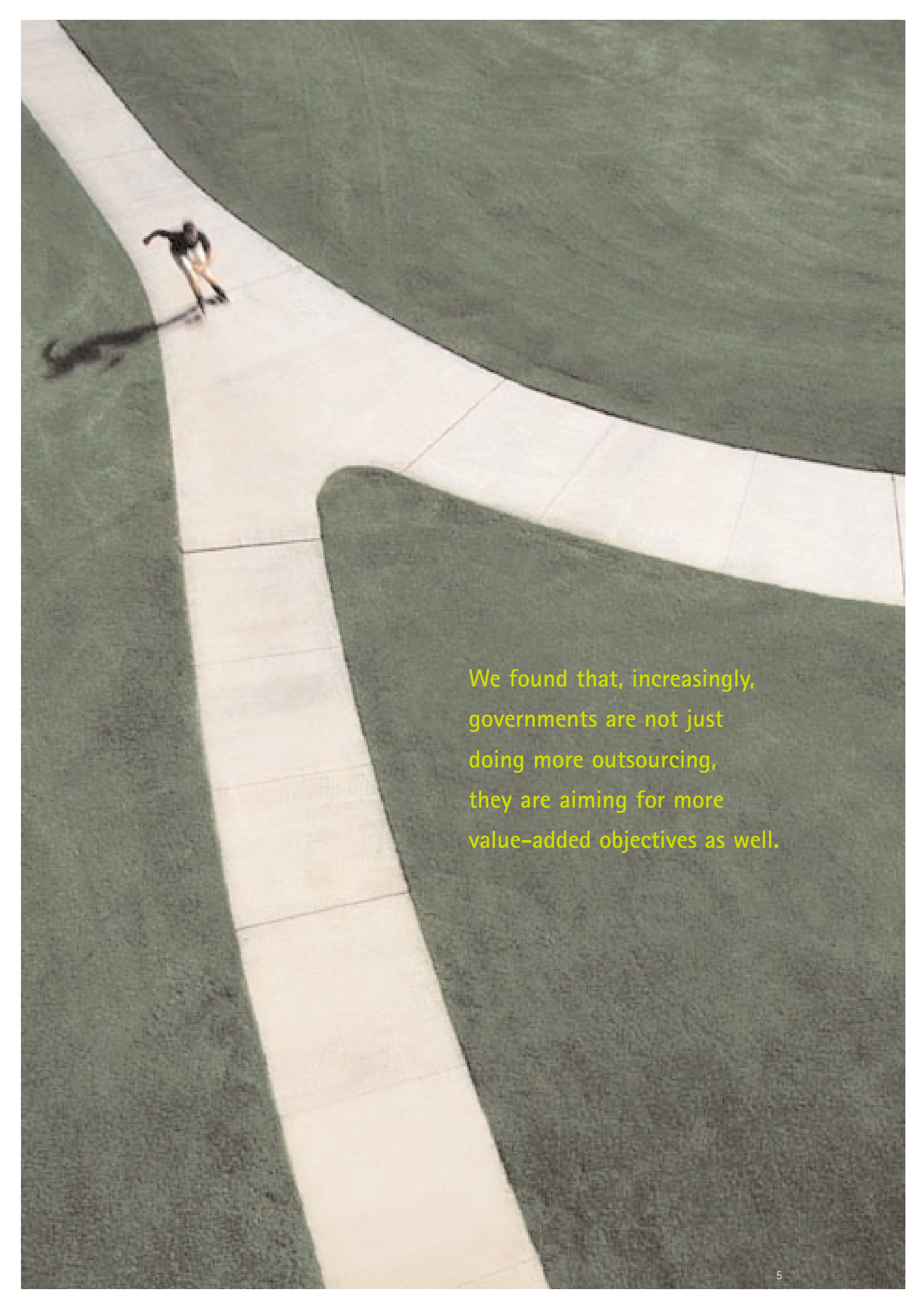
Whatever their reasons, however, executives clearly are realizing that outsourcing is a way to deliver value, not just reduce cost. In fact, they listed the objective of improving service speed or quality most frequently, while reducing costs tied for sixth place. More than 66 percent (78 responses) report they have explicitly outsourced to transform their agency or department (see Figure 3).

In a departure from the conventional wisdom, these executives have outsourced activities and processes that are critical to their mission. Eighty-nine percent of respondents rated their outsourced processes as either important or absolutely critical to the mission of their agency. Only 2 percent viewed outsourcing as relatively unimportant to their mission.

Just as telling is how well their objectives are being met. Only 50 percent of the survey respondents who counted cost reduction as a top outsourcing driver reported that they were largely or fully meeting their objective. In contrast, those who targeted more value-adding objectives reported more success. For example, executives intending to "gain access to new technology" and "centralize and/or

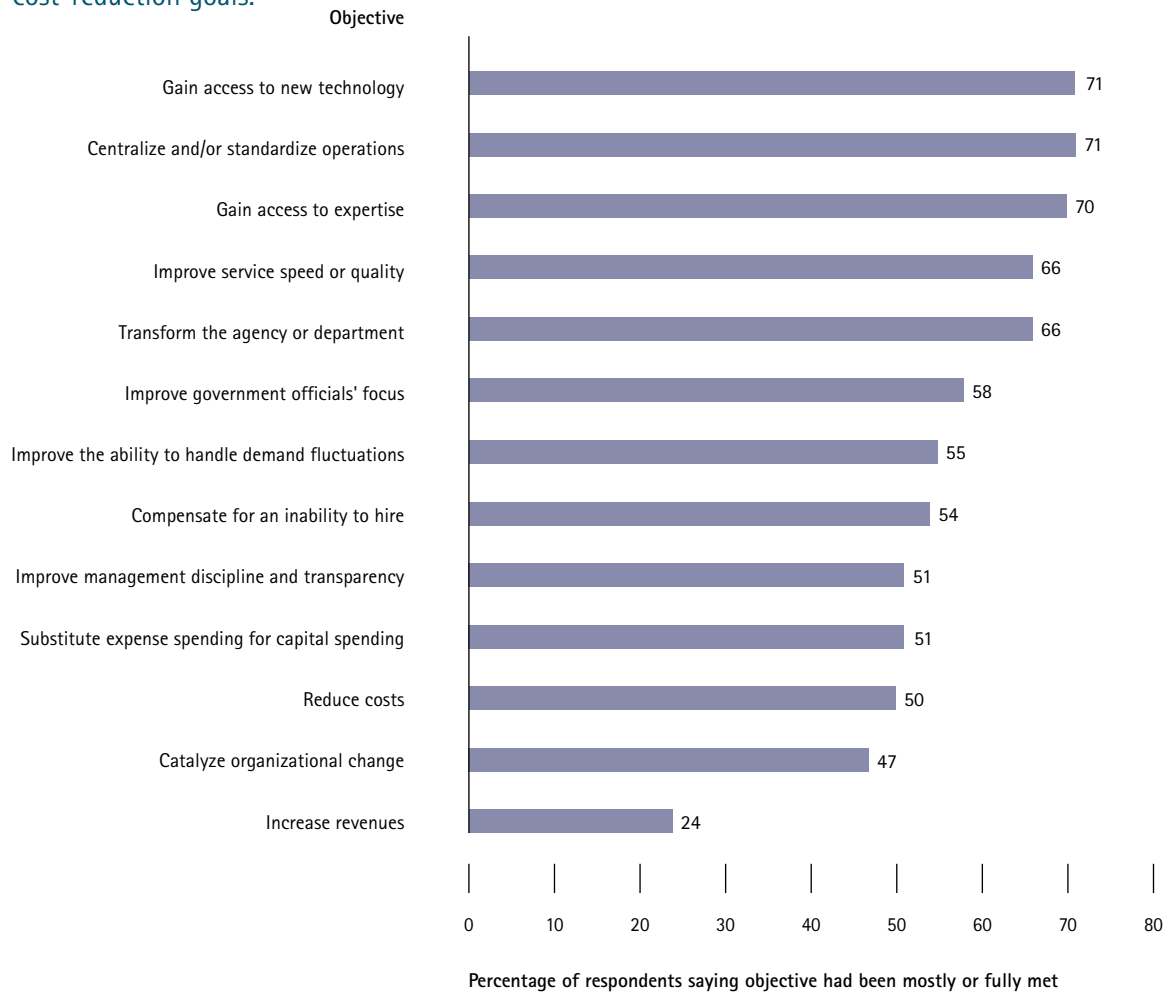
Figure 3. Executives use outsourcing more frequently to add value than to reduce costs.





We found that, increasingly, governments are not just doing more outsourcing, they are aiming for more value-added objectives as well.

Figure 4. Executives achieved their value-adding outsourcing objectives more frequently than cost-reduction goals.



standardize operations” reported the highest percentages of success. In each case, 71 percent stated they had mostly or fully met their objectives in that regard (see Figure 4.) In fact, even executives focusing on the most radical outsourcing objective, “transform the agency or department,” achieved their goal more frequently than those pursuing the lower value-added objective of simple cost reductions.

The logical conclusion is that government executives who have wanted to use outsourcing as a way to add value to their organization have been more successful in meeting their objectives than those who had a more single-dimensional focus such as cutting costs. These executives have used their growing experience in outsourcing to chart a higher value path than conventional outsourcing offers. While organizations may once have used outsourcing merely to wring costs out of non-core activities, many government executives have realized that they also can use outsourcing to help them meet more strategic objectives.

Outsourcing maturity progresses along two trajectories

When we began our research, our goal was to produce a straightforward ranking of outsourcing maturity by country. We soon discovered, however, that outsourcing maturity was a far more fluid concept than we had originally expected, and that ranking national governments in neat order does not accurately describe the landscape. We also discovered that outsourcing maturity could be viewed through different lenses; a country that appeared relatively inexperienced from one perspective may look quite different when viewed from another angle.

The growth in outsourcing is not driven by the same objectives in all cases. National governments’ pursuit of value through outsourcing is taking two significantly different trajectories: the transformational trajectory and the efficiency trajectory. These trajectories are set by the countries’ unique priorities.

The transformational trajectory

The transformational trajectory is driven by bold objectives with high potential value. Countries on this trajectory typically approach outsourcing as a tool to achieve a bold strategic agenda—often

Outsourcing for transformation

The Institute for Social Service in Mexico has used outsourcing to dramatically improve the delivery of health care to government workers. Previously, workers with a health problem had to go to the nearest clinic and wait to be seen. The new outsourced process enables individuals to make appointments ahead of time. While this capability may seem unremarkable to some, it represents a dramatic breakthrough in service for the 10 million individuals affected—representing reductions in wait times from as much as four hours to no more than 15 minutes.

driven by a pressing need to reform due to citizen dissatisfaction or severe budget deficits—in an accelerated time frame. Countries on this transformational trajectory have experience dealing effectively with the inevitable hurdles that arise from more complex and more mature initiatives.

Those countries that have a somewhat lower level of experience with outsourcing, but still hold a transformational agenda, sit at the early stage in the trajectory. On the whole, these countries could be characterized as relatively inexperienced, but we found examples of individual initiatives that had already achieved transformational results, such as Mexico's initiative described in the sidebar above.

The efficiency trajectory

The efficiency trajectory is a path that aims primarily toward cost reduction and productivity. In general, countries on this trajectory focus on technology infrastructure and business applications outsourcing as a way to trim costs and redirect capital to more mission-critical functions. At the more mature end of the spectrum are countries like Singapore and Japan, as well as Hong Kong, where consistent methodologies have led to reported outcomes of great improvements in

process efficiency and cost. We found that this focus on efficiency was consistent across the Asia Pacific region.

A number of countries, such as Brazil, Spain and Italy, could not be clearly classified on either of the trajectories. Brazil, for example, has little experience in what we defined as true outsourcing, although there is a central government agency that operates as a shared services center. It handles the IT needs of all other departments and, in turn, outsources to private-sector suppliers. Italy historically had a similar model, but the governmental IT provider has now been privatized. While the country has developed extensive experience in outsourcing IT, we found little evidence of business process outsourcing.

The trend toward business process outsourcing

One of the most marked differences between the two trajectories is the extent to which a country embraces business process outsourcing. In 42 percent of the outsourcing initiatives we surveyed, executives reported that they had transformed their agency effectively through outsourcing. In the vast majority of these cases—67 percent—they used BPO to accomplish these profound changes. Outsourcing

infrastructure or applications services alone led less frequently to transformational outcomes. As a result, we clearly associate business process outsourcing with the transformational trajectory.

A measure of intent and experience

A government's choice of trajectory is just that, a choice. Despite facing similar forces like crushing fiscal pressure or public dissatisfaction that demand reform, governments have chosen different paths. In addition, some governments have not yet decided how they will wield this powerful tool.

Figure 5 illustrates the position of the 22 countries, plus Hong Kong, in our survey on these two trajectories.

Where countries fall on these trajectories is based on a combination of a number of factors, including the complexity of their objectives, their ability to manage challenging issues such as workforce transition, their mastery of proven management methodologies, the breadth (range of services outsourced) and depth (number of deals) of their outsourcing experience, and their effectiveness to date.

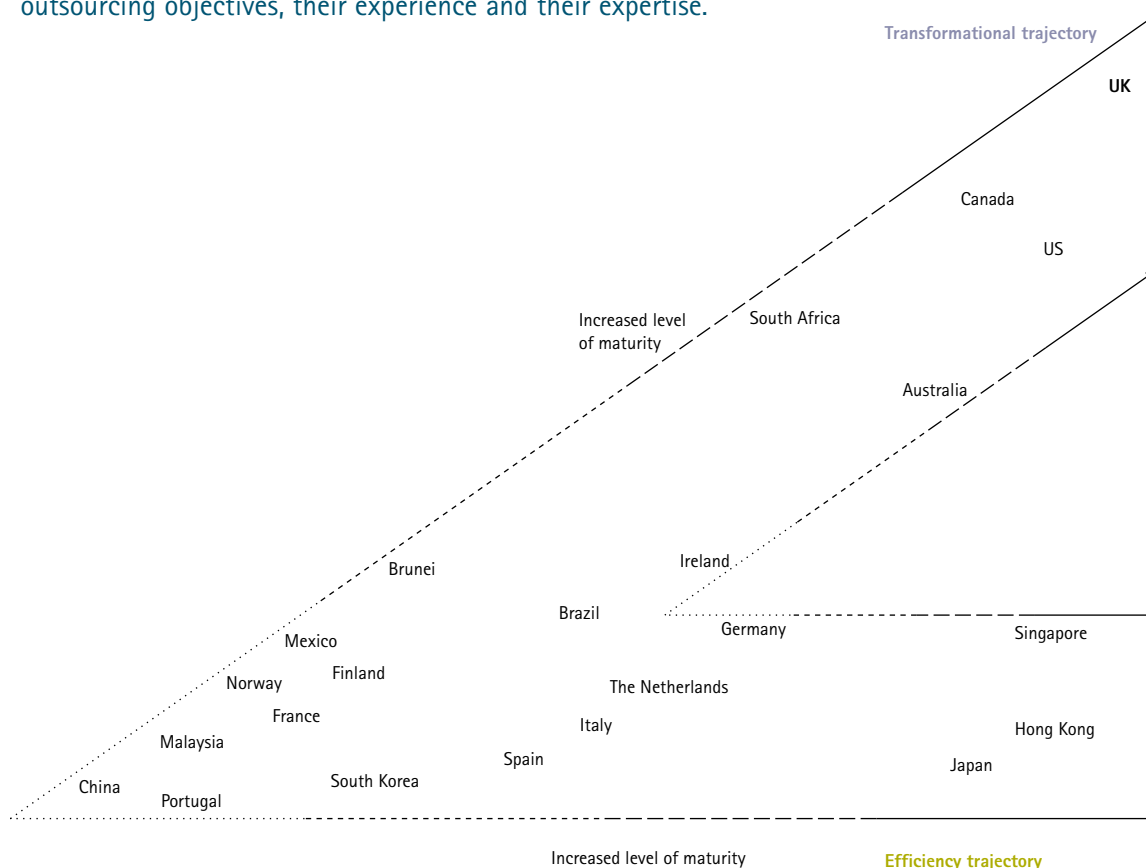
We chose this qualitative approach as the best way of fairly comparing how federal governments around the world are really using outsourcing. While we believe that a transformational trajectory—encompassing a wider range of capabilities—


holds the possibility for countries to realize much higher value from their outsourcing, we recognize the merit of many of the more traditional approaches. Many of these initiatives had no intention of driving significant change in government services, but they have met their efficiency objectives remarkably well. And in many cases, the central governments reported no higher aspirations for their outsourcing initiatives in the future.

Additionally, our placement of a country on a trajectory does not imply that all initiatives within the government of that country have that particular profile. The United Kingdom, for example, falls close to the endpoint of the transformational trajectory. However, many initiatives within the UK government would not be considered transformational. We want to convey that the government has amassed a portfolio of capabilities that includes not only transformational outsourcing, but also more conventional approaches.

Some countries with a highly decentralized governance structure, such as Germany, for example, may appear less outsourcing mature than they would have if we had taken regional- and local-level initiatives into account. Finally, some countries that might be considered less experienced hold examples of truly advanced outsourcing capability.

Figure 5. Countries aim toward one of two outsourcing maturity trajectories, based on their outsourcing objectives, their experience and their expertise.





Leading practices in government outsourcing

As we examined the global landscape of government outsourcing, we discovered that different countries exhibited different strengths. In many cases, several countries' success to date hinged upon their ability to manage one or more elements of an outsourcing initiative particularly well.

We have crystallized these leading practices in the sections that follow, categorizing them according to the six areas of outsourcing in which effective management is critical for success:

- Shaping the relationship to the situation
- Negotiating and contracting effectively
- Managing workforce issues
- Managing the ongoing relationship
- Ensuring strong performance
- Institutionalizing flexibility and innovation

These practices must, however, be tailored to the government's primary purposes for outsourcing.

Shaping the relationship to the situation

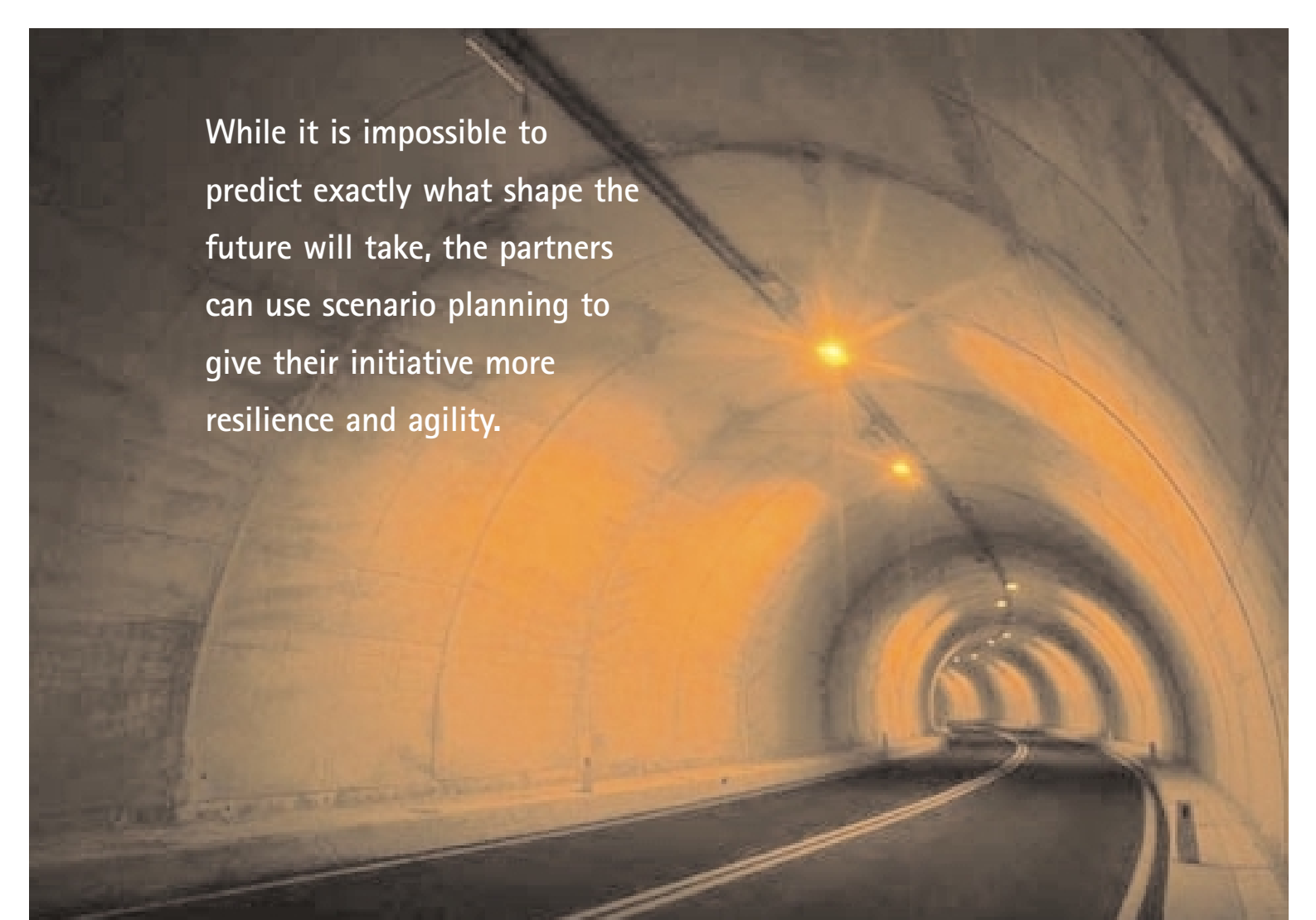
Effective outsourcing starts by establishing clear strategies and goals to guide an agency's efforts. Executives shape the initiative and the relationship that underpins it to meet the agency's specific strategy, situation and needs. Our interviews identified these leading practices related to shaping the outsourcing relationship to the situation:

Provide central guidance, but leave accountability with agency executives.

Top-down mandates from central authorities breed lack of enthusiasm at best and resentment at worst. On the other hand, complete decentralization with no central guidance can leave agencies foundering. Rather than either extreme, agencies and cooperating groups of agencies should be accountable for their own outsourcing decisions, which should be made within a results-oriented regulatory framework with guidance from a central policy.

Drive outsourcing decisions through strategy.

An agency's overarching goals and objectives will direct its outsourcing efforts and provide the measures of its success. Therefore, it must clearly define these goals and objectives before the tendering process even begins. An outsourcing supplier, no matter how deep its resources, should not be given the responsibility to set the strategic direction for a government organization. However, executives can call on the outsourcer to help map out the actions that will achieve the objectives set by its leaders. Collaboration on strategy becomes increasingly important as an agency moves from outsourcing infrastructure toward outsourcing entire processes.



While it is impossible to predict exactly what shape the future will take, the partners can use scenario planning to give their initiative more resilience and agility.

Explore options and learn from others before going to tender.

Before setting their requirements in stone through a formal request for proposals, many successful government agencies use an intense period of information gathering to lay the groundwork for their initiatives: soliciting ideas, investigating innovative approaches and testing the private sector's appetite for different models. Spending the time to gather information up front is a valuable investment. By becoming more educated on the possibilities and more sure of their goals, agencies may find that the other procurement stages take less time. More importantly, however, agency executives expand their understanding of the opportunities for creating value.

Design a business model, not a deal.

The best outsourcing initiatives are those that create value for both sides. This means designing a joint operating model that allows the private-sector firm to make a reasonable profit as it generates benefits for the public sector. Executives should deconstruct their own sources of value, and investigate the business models of their private-sector partners. This analysis positions government executives to explore new ways of working with private firms to make the most of what they can jointly offer.

Negotiating and contracting effectively

Managing *strictly* by the contract is a formula for disaster in outsourcing, but experienced public-sector executives use the process of negotiating the contract to set the tone for the entire relationship with their outsourcing partner. Our interviews yielded the following insights into leading practices in negotiating and contracting effectively:

Take ownership of the negotiation process.

Although contracting specialists can provide useful advice, their incentives often lead them toward adversarial approaches and a focus on cost reduction to the exclusion of other objectives. Effective outsourcing leaders take advice from specialists, but own the negotiating process personally. That way, they can ensure that the objectives and principles that are central to their agenda are also central to the contract and guide the relationship with their provider.

Include values and principles in the contract.

The contract should contain not only specifics about service level agreements and system capabilities, but also guiding principles for the relationship as a whole. These relationship principles are not legally binding, but they represent a very public commitment by both organizations to work together and to ensure each other's success.

Use stakeholder analysis for key decisions.

Crafting an effective outsourcing initiative involves several critical decisions. Leading organizations use stakeholder analysis to guide them in these important choices. They first identify the key stakeholder groups. Then they develop a detailed description of the needs of each group. By assessing each option against these needs, executives can reach a decision that is best for all of the key constituencies.

Plan for the future during the contracting process.

Executives frequently place so much attention on getting an outsourcing deal off the ground that they give little thought to how both partners might need to change what they are doing in the future. As a consequence, many initiatives start off strong, but falter after a few years as changing requirements stress the relationship. Lasting relationships build in contingency plans for expanding or contracting scope and the associated time for readjustment. Finally, they establish procedures that enable disengagement, should conditions change so much that it becomes better to dissolve the relationship. While it is impossible to predict exactly what shape the future will take, the partners can use scenario planning to give their initiative more resilience and agility.

Managing workforce issues

Our research showed that managing workforce issues effectively is a hallmark of outsourcing maturity, particularly for countries on the transformational trajectory. Not surprisingly, we saw few examples of effectively managed workforce transitions. In fact, 75 percent of our survey respondents reported that they transferred no government workers to the provider as part of their outsourcing. Still, some government organizations have learned how to manage this difficult activity effectively. The resounding themes from their successes around workforce management include:

Recognize that workforce management issues are not insurmountable—they just take work.

There is no mystery in handling labor and union issues in outsourcing, but it does take careful attention and hard work. Involve union representatives early and often. Identify the sticking points—fears of job loss, loss of pensions and other benefits—and map out a strategy for dealing with each one. Then communicate aggressively.

Adjust workforce solutions to your situation.

One answer is not right for every workforce situation. Some executives we spoke with worked out a number of different placement alternatives for their employees, dealing with each major category

of employee (long term versus short term, for example) and offering appropriately tailored options for each group. In other cases, a “clean-break” model was the best approach. In this model, the government doesn’t engage in negotiations with providers over the staff. On Friday, they are terminated as government employees and given substantial redundancy payments; on Monday, they can be hired back to work by the outsourced company. This approach greatly simplifies things for the government agency and may be quite attractive to the employees if the economy is vibrant and their skills are in demand.

Set a prudent pace for dealing with workforce transitions.

No matter how you look at it, workforce transitions are disruptive. Executives will want to take enough time to communicate thoroughly with the people who will be affected, to address their concerns and to provide pathways to new roles. Understand, however, that stretching out a painful process does not serve anyone well. Executives should spend time on planning the transfer and on training afterwards, but should not unnecessarily protract a painful process.

Managing the ongoing relationship

Establishing and sustaining a commitment to deliver high-value outcomes through outsourcing means government executives must go beyond contract management to master relationship management. These leading relationship management practices include:

Open the books on both sides.

Sharing information about cost structures can be a powerful way to cement trust in the relationship. It can lead to a strong sense of partnership and “in it together” teamwork. Openness on the part of the vendor also allows the government agency to evaluate claims that the provider is not making an adequate profit.

Leverage procedures appropriately to address sensitive issues.

Clearly establishing a governance structure that defines important methodologies and escalation procedures can introduce both distance and guidance when issues arise. Experienced executives aim for enough methodology to put rigor in important processes and enough flexibility to adjust to the pressing needs of the situation.

Maintain a “whole of business” perspective.

Successful government agencies actively help their providers succeed, even when it isn’t their responsibility. The good deal a government negotiates for

itself needs to be a viable one for the outsourcer as well. It is important for all parties to recognize that the relationship will work only if there is mutual benefit. This carries with it a commitment to evolve the relationship over time, ensuring the value proposition remains flexible enough to maintain mutual attractiveness and benefit.

Use conflict as an opportunity to improve the relationship.

Relationships are never linear; they progress through a series of peaks and troughs. These include occasions of accomplishment and resulting accord. As often, however, they involve points of conflict and tension. In times of tension over expectations and service levels, excellent leaders resist the temptation to adopt an adversarial attitude. Conflicts can start a relationship on a fast downward slide if partners yield to a natural tendency to retreat to their corners. Executives who find ways to arrive at a mutually acceptable resolution can foster long-term trust instead. Successful leaders recognize and harness the potential in conflict points by approaching them as opportunities for growth.

Ensuring strong performance

The starting point for ensuring strong performance in an outsourcing project is to aim for outcomes, and then work with your partner to craft clear, achievable plans to reach them. For most executives, the starting point is the service level agreement (SLA). Well-crafted SLAs are a powerful base when they include both quantitative and qualitative performance measures and are tailored to the specific initiative. Our research pointed out these additional leading practices in ensuring strong performance:

Maintain critical expertise.

Management oversight of the outsourced function cannot be delegated to the provider. If the government agency is to remain accountable for a function, it must maintain the critical expertise to understand how that function should operate.

Tap proven methodologies.

All of the executives we spoke with in Hong Kong, which we found to be highly mature on the efficiency trajectory, spoke of the PRINCE³ (PROjects IN Controlled Environments) methodology as the engine

behind their successful technology infrastructure and applications outsourcing. Proven methodologies help executives monitor each stage of a project completely and keep projects under control even when a large number of parties are involved.

Track qualitative performance indicators as well as quantitative ones.

Every capable outsourcing manager watches operational performance through service level metrics. The most sophisticated ask the provider to self-assess performance and to offer improvement plans for any lapses. Leaders also include qualitative performance tracking on their agenda, most frequently as part of a comprehensive scorecard.

Institutionalizing flexibility and innovation

Achieving high-level outcomes in a changing environment requires institutionalizing innovation as part of the outsourcing process. Government agencies at the far end of the transformational trajectory stimulate new ideas and drive innovation through these leading practices:

Make your innovation plans explicit.

Executives should verbalize their expectations for innovation and quantify how they will know when they are achieving them. Leaders hold regular innovation reviews both to assess their progress and to spur new thoughts. To institutionalize innovation in an outsourcing relationship, executives need a method, not a promise.

Remain externally focused.

Many government executives we interviewed took regular field trips to other government operations to share insights and practices. They also welcomed visitors from abroad in the same spirit. Through this ideas exchange, they learn how to take advantage of innovations that others have pioneered.

Tap the resources of a multinational corporation.

Many government agencies contract with large, multinational corporations as their providers. This enables them to tap into the broader resources of these organizations. To take advantage of this opportunity, executives ask the outsourcing provider what it can bring to the table beyond just technology—in areas such as marketing, research, and extended relationships and alliances.

³ PRINCE (PROjects IN Controlled Environments) is a structured method for effective project management. It is a de facto standard used extensively by the UK government and is widely recognized and used in the private sector, both in the UK and internationally. PRINCE, the method, is in the public domain, offering non-proprietary best-practice guidance on project management. PRINCE® is, however, a registered trademark of the United Kingdom's Office of Government Commerce (OGC).



Conclusion

The innovative practices described here came to the forefront in our research, echoed time and again by outsourcing leaders. No matter what the ultimate outsourcing objectives—increased efficiency or wholesale transformation—we believe these practices will help public-sector executives improve their ability to achieve excellent outcomes. While some of these practices are more applicable in some cases than in others, all of them represent excellent management approaches that can lead to greater outsourcing effectiveness and the higher-value end results that governments increasingly are seeking from their outsourcing initiatives.

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