

**Information Note to  
The Legislative Council Panel on Public Service**

**Information on contracting out government services**

**Background**

At the meeting held on 20 May 2005, the Administration was requested to consider providing the following information:

- (i) Amount of savings achieved through government outsourcing programmes in 2004-05 in terms of administration cost and staff cost respectively; and
  - (ii) Total number of staff employed by government contractors under all the government outsourcing programmes currently in force.
2. The Administration also undertook to provide the following information:
- (i) Copies of the “Serving the Community by using the Private Sector – A General Guide to Outsourcing” published by the Efficiency Unit (EU) in 2003; and
  - (ii) Findings of the outsourcing surveys conducted in 2000 and 2002, with the same details of the survey conducted in 2004 as set out in paragraph 7 of the paper provided by the Administration (LC Paper No. CB(1)1460/04-05(01)).

**The Administration’s Response**

3. The primary objectives of outsourcing public services to the private sector are to achieve value for money and ensure quality service delivery. Cost cutting is not a major consideration when departments take forward such exercises. The Administration does not have accurate statistics on the amounts of savings achieved as a result of outsourcing over the years as this is not one of the measured deliverables for outsourcing contracts. It would be particularly difficult to derive this information for outsourcing contracts that have been in place for many years and for contracts for which

the services outsourced have never been provided in-house. The departments were asked to estimate the savings derived from outsourcing as part of the last biennial outsourcing survey conducted in August 2004. At that time for activities previously provided in-house, the average saving arising from outsourcing was estimated to be about 25% of the expenditure under in-house provision.

4. The Administration does not maintain statistics on the number of staff employed by contractors undertaking government outsourcing contracts, and there are practical difficulties to compile such information due to the wide range of services involved. Departments generally follow outsourcing best practices, which include establishing service levels using output specifications rather than input specifications. The focus is on the quality and value for money, not the number of staff a contractor employs to perform the task. We have considered asking departments to estimate the number of staff involved in contracts but we do not consider this to be either practical nor of any real value in terms of the provision of reliable information so have decided not to proceed.

5. The Efficiency Unit intends to conduct the next biennial outsourcing survey in 2006. We will consider whether we can include questions about cost savings and the number of staff employed on outsourcing contracts, to provide a ‘snapshot’ of the position at the time of the survey.

6. Ten copies of the booklet “A General Guide to Outsourcing” published by the Efficiency Unit in 2003 have been sent to the LegCo Secretariat for distribution to Members. The guide is also available at the Efficiency Unit’s website at [http://www.info.gov.hk/eu/english/research/files/a\\_general\\_guide\\_to\\_outsourcing.pdf](http://www.info.gov.hk/eu/english/research/files/a_general_guide_to_outsourcing.pdf)

7. Key findings of the three outsourcing surveys conducted in 2000, 2002 and 2004 are provided in the Annex to this paper.

## Key Findings of Results of Outsourcing Surveys Conducted in 2000, 2002 and 2004

### Background

The EU conducted the third biennial outsourcing survey in 2004 following two similar exercises conducted in 2000 and 2002. This outsourcing survey was aimed at updating our database on government outsourcing as well as enhancing our understanding of the outsourcing practices and concerns of departments. The survey results provide a "snapshot" of the government outsourcing activities as at August 2004.

2. The first survey conducted in 2000 was a modest exercise, with many questions not asked of departments until the 2002 and 2004 surveys. As a result comparisons between 2000 and 2004 are limited at best. This paper includes comparisons where the data is available.

### Outsourcing Pattern

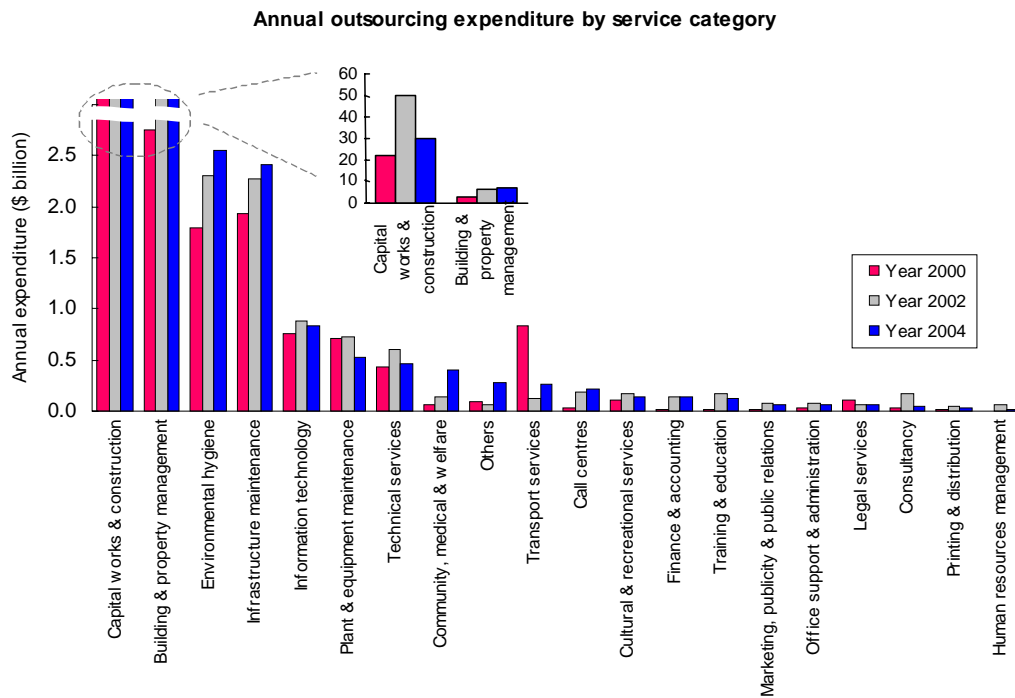
3. A comparison of the number of contracts, total contract value and annual outsourcing expenditure is shown below. The decrease in total contract value and annual outsourcing expenditure in 2004 was largely attributed to the volume of public works projects changing over the two year period between surveys.

<b>Year of survey</b>	<b>2000</b>	<b>2002</b>	<b>2004</b>
Total number of contracts	4389	4853	4512
Total contract value	Not asked	\$238 billion	\$214 billion
Annual outsourcing expenditure	\$32 billion <sup>Note</sup>	\$66 billion	\$46 billion

4. The annual outsourcing expenditure pattern by service type in 2004 is similar to that of the past years. A wide spectrum of government services have been outsourced, with capital works and construction, building and property management, environmental hygiene, and infrastructure maintenance contracts continuing as the top four in terms of annual outsourcing expenditure.

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<sup>Note</sup> Some of the works departments that outsource work did not respond to the survey.



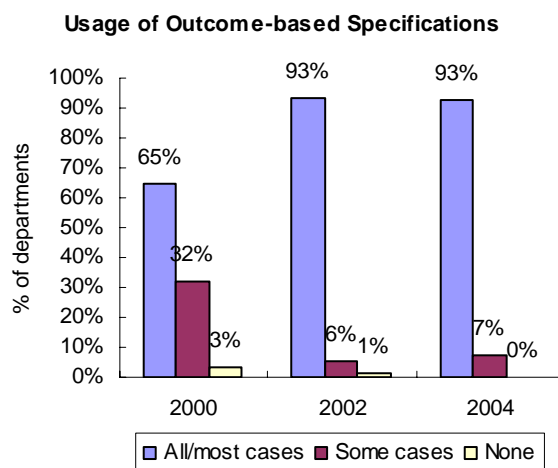
## Contract Sizes

5. The average annual expenditure per non-works contract continued to grow showing a trend of "bundling" smaller tasks into one bigger contract. This helps reduce the tender preparation effort and facilitate contract management.

Year of survey	2000	2002	2004
Average annual expenditure per non-works contract	\$2.1 million	\$3.6 million	\$3.9 million

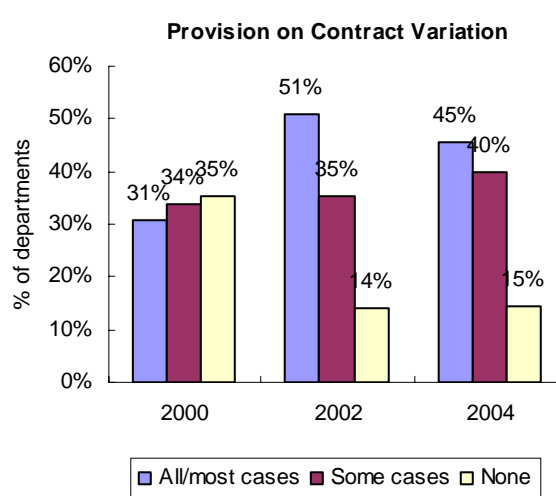
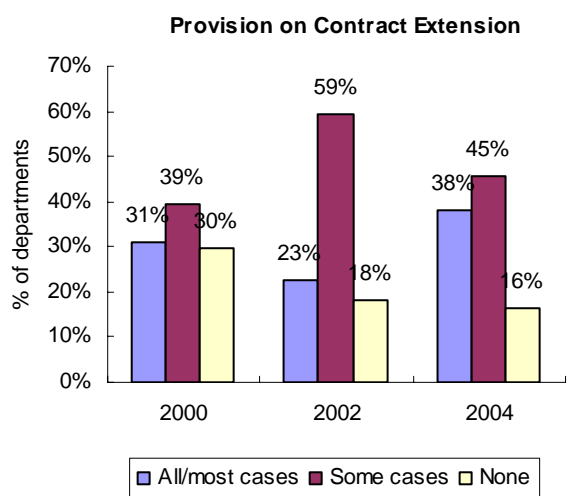
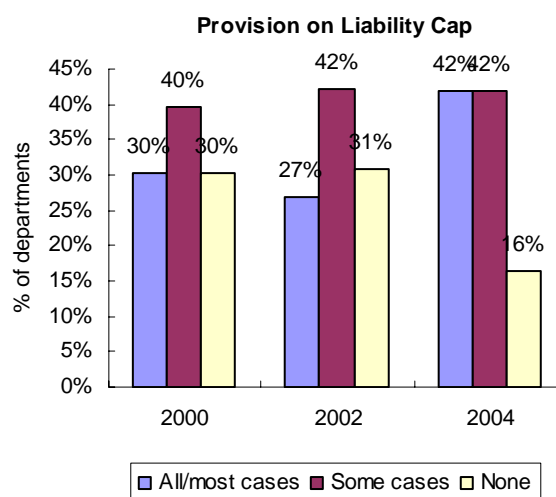
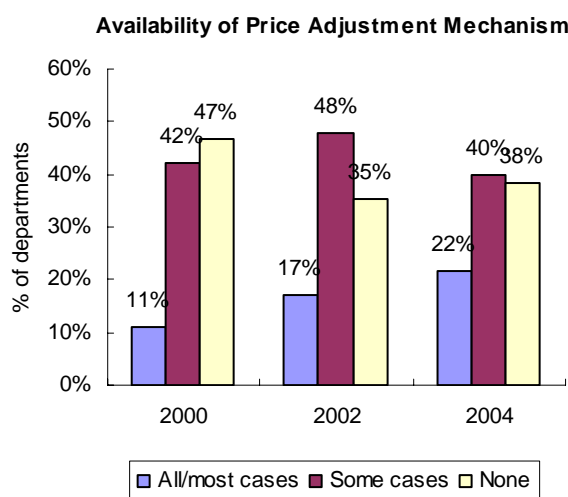
## Service Specifications

6. Departments are seeing the benefits of outcome-based specifications that give service providers greater flexibility in service delivery and encourage innovative solutions.



## Contract Provisions

7. The following charts compare the availability of various contract provisions in the past surveys.



## Outsourcing Achievements

8. Departments usually outsource for pragmatic reasons such as acquiring services unavailable in-house, the wish to focus on core services and the need to access skills, rather than for achieving cost savings. Compared with the in-house modes of delivery, average savings of 25% were reported in 2004 which is similar to that of 23% reported in 2002.

9. Whilst there are occasional disappointments, most departments reported that they were generally satisfied with their outsourcing outcomes in recent years. The percentages of outsourcing objectives being fully met are 59% in 2004, 58% in 2002 and 38% in 2000.

### **Future Outsourcing**

10. A half-day seminar on the "Outsourcing Survey 2004 - Separating Fact from Fiction" was held on 21 January 2005, for directorates and senior professional officers. It provided an overview of current government outsourcing, recent trends and likely future directions.

11. EU will continue to promote the understanding and use of outsourcing as well as other forms of private sector involvement. In addition to providing and updating published guides, we shall continue to conduct seminars regularly for civil servants, and assist departments in conducting feasibility and business case studies on specific projects. We are also able to assist departments in the preparation of procurement documents (including draft contracts, service level agreements and bid marking schemes). We plan to conduct the next biennial outsourcing survey in 2006.

Efficiency Unit  
June 2005

# Serving the Community

*By Using the Private Sector*

*A general guide to outsourcing*

October 2003  
(Second Edition)



The Efficiency Unit welcomes comments from readers and users of this Outsourcing Guide. Comments may be addressed to:

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# Foreword

The Government continues to be committed to providing a wide range of high quality services to the community it serves. It must do this at the same time as it constrains the size of the civil service; returns to its traditional ‘small government’; and moves towards the elimination of the budget deficit.

Outsourcing by the Government has already proven very successful over recent years. There are many examples of projects achieving efficiency and productivity gains, cost reductions and the introduction of innovative techniques and technologies. The private sector has also benefited. By moving tasks into the business sector, we can provide employment and business opportunities that can be developed and expanded in ways that are simply not possible within the public sector.

Much has already been done, and I applaud those responsible. But much more can, and must be done. I urge my colleagues in the civil service, as well as the business community, to actively identify and implement appropriate projects with renewed urgency.

This Guide provides sound, tried and tested advice on how to outsource services with confidence.

**Donald Tsang**

Chief Secretary for Administration

# Contents

	<i>Page</i>
<b>Introduction: Ensuring Value for Money</b>	<b>1</b>
<b>Using this Guide</b>	<b>2</b>
<b>Chapter 1 Outsourcing in the Civil Service</b>	<b>3</b>
1.1 Involving the private sector	
1.2 Identifying reasons for outsourcing	
1.3 Identifying issues to be managed	
1.4 Managing the process	
1.5 Setting up support processes	
1.6 Setting the timetable	
<b>Chapter 2 Phase A: Developing the Business Case</b>	<b>11</b>
A.1 Scope the service	
A.2 Establish the required future levels of service	
A.3 Identify the costs	
A.4 Identify and analyse potential solutions	
A.5 Document the business case and service acquisition plan	
<b>Chapter 3 Phase B: Tendering and Selection of the Service Provider</b>	<b>22</b>
B.1 Create tender documents and set evaluation criteria	
B.2 Manage the tender process	
B.3 Evaluate tender responses	
B.4 Conduct due diligence checks	
B.5 Negotiate the contract	
<b>Chapter 4 Phase C: Managing the Contract</b>	<b>36</b>
C.1 Prepare for the transition and handover	
C.2 Monitor service delivery and manage the relationship	
C.3 Administer the contract	
C.4 Monitor the savings achieved	
C.5 Conduct review and renewal process	
<b>Chapter 5 Support Processes and Assistance</b>	<b>44</b>
5.1 Planning and control	
5.2 Managing people	
5.3 Managing quality	
5.4 Assistance available	
<b>Appendices</b>	<b>49</b>

# Introduction

## Ensuring Value for Money

Over the past few years, the government has used outsourcing widely to deliver high quality and cost-efficient services and projects. As at December 2002, there were over 4,800 government outsourcing contracts with a total contract value of nearly \$200 billion and an annual expenditure of \$65 billion. Given the extensive use of outsourcing it is imperative that departments focus on ensuring that they achieve value for money.

- ♦ **Contract size.** Given that the effort and costs involved in processing each outsourcing contract are similar regardless of the size of the contract - for both the government and the private sector - it makes sense to ensure that contracts are big enough to justify the effort. To fully benefit from economies of scale, departments should avoid artificially constraining the size of contracts. Related services such as building management and cleansing services can be consolidated or bundled and undertaken by a single service provider. Bundling can even be used for individually discrete tasks, such as conveyancing, through the use of term contracts.
- ♦ **Cross-departmental co-operation.** There are frequent instances where two or more departments are responsible for the provision of, or are the recipients of similar services. Co-operation between departments in outsourcing these services can often achieve cost savings and service delivery improvements that would not be achievable by individual departments acting alone.
- ♦ **Contract duration.** Long-term contracts encourage investment in equipment, technology and people, because costs and returns on investment can be spread over longer time periods.
- ♦ **Outcome-based specifications.** Service specifications should be, as far as possible, outcome-based. This encourages service providers to propose innovative solutions which focus on the outcomes needed rather than inputs provided, and also gives contractors greater flexibility to respond to changing circumstances.
- ♦ **Appropriate levels of service.** In preparing service level specifications, departments should avoid the temptation to require the contractor to do more, or to deliver a higher standard, than the department had when the function was carried out in-house. Such “gold-plating” raises costs unnecessarily and distorts the value comparison.
- ♦ **Optimal risk allocation.** Departments should optimise - not maximise - risk transfer to the outsourced service provider. A department should avoid transferring those risks to the service provider that the provider is not best placed to manage. Otherwise, all tender bids will be inflated unnecessarily. In general, the private sector is best at managing operational and life-cycle risks.
- ♦ **Competition.** Much of the benefits of outsourcing arises out of the competition involved in the process, not just the use of the private sector per se. Making sensible use of competition to procure outsourced services is essential if real gains are to be achieved.
- ♦ **Level playing field.** In conducting cost benefit analyses, the full cost/benefit to the government (not to the client department only) should be considered, otherwise the assessment is distorted. For example, if a department was considering outsourcing its vehicle fleet, the analysis should reflect that the contractor’s payment of vehicle taxes, duty on fuel, annual licence fees and so on will flow to the government offsetting the cost of the contract to the department. The private company will also pay tax on its profits, but this may be more uncertain and also complex to calculate.
- ♦ **Use incentives, not penalties.** Make use of incentives to encourage good performance and continuous improvements, rather than penalties. One party to a contract cannot penalise the other. Attempts to do so will not be upheld by the courts.

*Obtaining value for money should be a key objective in every outsourcing exercise*

- ♦ **Do not always select the lowest priced tender.** Beware unfeasibly low bids that may not be sustainable or cannot deliver sufficient quality. One appropriate consequence of the “two-envelope system” of tender evaluation is that the best combination of technical and financial proposals is not always the cheapest tender.
- ♦ **Ensure that projected savings are realised.** The full benefits of outsourcing an existing service will arise only if the projected savings in in-house costs are realised. This includes not only staff but also, for example, the accommodation that the staff had occupied.
- ♦ **Common goals and understanding.** It is essential for the contractor and the client department to understand and share the objectives of the outsourced project or programme. The client department must continue to bear in mind, throughout the procurement process and contract management phase, the need to communicate clearly and effectively.
- ♦ **Quality management.** If the management of an outsourced facility requires that particular skills and expertise is required to ensure that the facility is managed to the standard required, then this may be stated explicitly in the procurement documentation. It is perfectly acceptable to state that particular qualifications (or their equivalent) and a stated number of years experience at a particular level are required for key management positions.
- ♦ **Dispute resolution.** Departments need to pay careful, ongoing attention to contracts to ensure that potential problems are identified early and nipped in the bud. If disputes are not resolved early and, for instance, end up subject to arbitration, the costs involved can be substantial and service delivery may be disrupted.
- ♦ **Review existing contracts before re-use.** There is an understandable tendency for officers to re-use existing contracts without critically examining whether the department’s current requirements and best practices are adequately reflected. Over time, this results in contracts that are badly out of date.

## Using this Guide

The Guide provides information and guidance for outsourcing decision-makers within the civil service and discusses steps that should be considered at each phase of the outsourcing process. It has been developed to meet the needs of managers and supporting staff involved in outsourcing. This Guide is also made available to the private sector so that they can better understand the procedures that are being followed.

Throughout the Guide the term department is used generically for all types of government organisations. Appendix 1 provides a glossary of terms and abbreviations.

Readers of the Guide may not need to consult every part. It is organised around the discrete phases that should form part of a fully implemented outsourcing projects. Each phase is colour coded: Red = Phase A; Yellow = Phase B; and Green = Phase C.

Amendments to the Guide will be posted on the EU website (<http://www.info.gov.hk/eu/>) and in the Central Cyber Government Office (CCGO) website under Public Sector Reform/PSR Information Centre (<http://host1.ccgo.hksarg/cso/eu/psric/>). Please check for amendments before making detailed use of the Guide.

## Chapter 1 Outsourcing in the Civil Service

This chapter describes the place and purpose of outsourcing within the government's use of the private sector to provide public services. It then provides an overview of outsourcing issues, processes and timelines.

Tasks	Actions
1.1 Involving the private sector	<ul style="list-style-type: none"> <li>♦ Identify the appropriate model</li> </ul>
1.2 Identifying reasons for outsourcing	<ul style="list-style-type: none"> <li>♦ Concentrate on priorities</li> <li>♦ Improve service quality</li> <li>♦ Increase resource flexibility</li> <li>♦ Access skills</li> <li>♦ Access technology</li> <li>♦ Manage costs</li> </ul>
1.3 Identifying issues to be managed	<ul style="list-style-type: none"> <li>♦ Privacy and confidentiality</li> <li>♦ Knowledge of government</li> <li>♦ Disengagement</li> <li>♦ Political environment</li> <li>♦ Internal and external consultation</li> </ul>
1.4 Managing the process	<ul style="list-style-type: none"> <li>♦ Developing the business case</li> <li>♦ Tendering and selection</li> <li>♦ Managing the contract</li> </ul>
1.5 Setting up support processes	
1.6 Setting the timetable	

### 1.1 Involving the private sector

The government is committed to providing the best services it can for the community. Its commitment to enhancing public sector productivity and keeping down the public sector's share of the Gross Domestic Product means that departments must examine new ways of providing services other than through the appointment of more civil servants.

Private sector involvement (PSI) is being encouraged within the civil service as a means to improve the efficiency, volume and quality of services needed. The main forms of PSI are:

- ♦ Purchaser/provider contracts
  - Contracting in
  - Contracting out/outsourcing
  - Grants and subventions

*Outsourcing is an arrangement where a government department contracts with an external service provider for a continuous period for the provision of services specified and paid for by the department*

- ♦ Public private partnerships (PPPs)
  - Creating wider markets
  - Private finance initiatives (PFIs)
  - Joint ventures
  - Partnership companies
  - Partnership investments
  - Franchises
- ♦ Privatisation
  - Asset sales or transfers
  - Sales of shares in state enterprises
  - Management buy outs (MBOs)
- ♦ Private sector provision
  - Market provision of services
  - Withdrawal of public services



These are explained in more detail in “*Serving the Community by Using the Private Sector*”, available from the CCGO website under Public Sector Reform/PSR Information Centre and the EU website (<http://www.info.gov.hk/eu/>).

Each model of PSI offers risks and benefits. Outsourcing, one of the key forms of PSI, is highly relevant in the Hong Kong context. It supports the pursuit of the government’s policy of “minimum intervention, maximum support”.

#### Reasons for outsourcing:

- ♦ *Concentrate on priorities*
- ♦ *Improve service quality*
- ♦ *Increase resource flexibility*
- ♦ *Access skills*
- ♦ *Access technology*
- ♦ *Manage costs*

## 1.2 Identifying reasons for outsourcing

In pursuing the outsourcing option, the first step is to determine whether this represents the best model for the service under consideration. In Hong Kong, government departments have contracted out many activities including capital development (infrastructure and building) and administrative and maintenance functions (building and property management, cleaning, security, plant and equipment maintenance). Other areas where outsourcing is emerging as a more common choice include the environment, hygiene, training and development and welfare services.

Successful outsourcing allows the civil service to focus in-house resources on tackling priorities. In general these priorities will be policy, regulatory and statutory service delivery functions. However, priorities may differ from time to time and department to department, just as they do from country to country, and no function should be treated as automatically immune from regular consideration as to its potential for outsourcing.

Outsourcing is not an end in itself. Its successful adoption will involve departments in important decisions about the business they are in and the best mechanism for delivering their services to the community. Outsourcing is a management tool and should be approached in that manner.

Even though another entity operates the function or performs the service, departments remain fully responsible for providing the outsourced services. They retain control over strategic decisions such as the services to be performed and the outputs and outcomes to be achieved.

Departments outsource services for a number of reasons. Aging infrastructure, poorly maintained equipment, inappropriately skilled staff or outdated work practices are not uncommon in government departments. They may wish to:

**Concentrate on priorities.** When a department concentrates on carrying out its priorities, it can use its financial, human and management resources more effectively and efficiently. Outsourcing some functions provides departments with the flexibility to redirect resources to activities critical to their mission. Under outsourcing, management's role shifts from primarily managing resources and technology to managing relationships and contracts, and satisfying the needs of customers. Management, however, remains accountable for the quality and cost of service delivery.

Departments should be cautious of being restricted by definitions of "core" services. International experience shows that most services other than the taking of policy decisions have been outsourced in other jurisdictions.

**Improve service quality.** In an era of increasing specialisation and rapid advances in technology, many departments find that the quality of service provided in-house is not keeping pace with best practice. Outsourcing can be an effective tool to improve customer service. Private sector service providers may have more flexible, innovative and effective ways of delivering services and ensuring the services reach the people they are meant for. Examples of this might include offering longer or more flexible service hours built around client requirements and providing access to services via technology.

**Increase resource flexibility.** Maintaining the level of equipment and staff necessary to cover peak loads can leave a department with under-utilised resources during off-peak periods. Conversely, a department may find it difficult to maintain resources at a level sufficient to meet demand at peak periods, leading to poorer customer service. Outsourcing functions subject to peaks and troughs in usage can provide a department with the flexibility to respond rapidly to changing demands.

**Access skills.** Departments may experience a shortage of skilled and experienced personnel brought about by retirements, resignations, caps on recruitment or an inability to recruit into the civil service. Remaining employees may not always have the specialised skills or training to keep pace with the rapidly evolving technology.

In general, departments will source those skills necessary to support core functions through recruitment and use outsourcing to access skills that they find difficult to recruit and retain.

When a department is contemplating providing new services, outsourcing can ease the process of building the skills and resources required to respond to these new initiatives. In some cases, outsourcing to an external service provider may be the only practical way to access the skills necessary to properly deliver services.

Departments also benefit from having their staff work with the service provider's specialists. To ensure a department's interests are well served, contract managers will need to keep their own knowledge up-to-date.

**Access technology.** Departments also look to outsourcing to keep up with the accelerating changes in technology. Service providers often have more funds or expertise to acquire and maintain new computing/telecommunications resources than government departments. They are also able to implement new technology better and more quickly because their

*Departments should focus on their priorities so that they can perform their missions more efficiently and effectively*

*More effective services should flow from outsourcing*

*Outsourcing can assist in matching resources to fluctuating requirements*

*Some skills may only be available via outsourcing*

*Technology may be more readily available via outsourcing*



*Cost control may benefit from outsourcing*

*There may be issues affecting the outsourcing decision that seem unique to government - but they are not unsolvable*

- ◆ *Legal issues*
- ◆ *Privacy and confidentiality*
- ◆ *Knowledge of government*
- ◆ *Disengagement*
- ◆ *Political environment*
- ◆ *Internal and external consultation*

core business forces them to focus on continuous technology refreshment. They need to reinvest to survive.

**Manage costs.** Budget realities have a key impact on deciding which functions to perform in-house and which to outsource. Outsourcing can reduce both fixed and recurrent costs. Research indicates that savings can range between 10% and 25% per annum. However in instances such as accessing superior services in information technology (IT) systems, applications and software development, the costs may be similar or higher.

Another important benefit of outsourcing is being able to forecast costs. The uncertainty caused by compounding rapid changes in service requirements with technological change could lead to cost overruns and unpredictable cash flows. A fixed price contract simplifies budget planning and cost management for departments.

### 1.3 Identifying issues to be managed

In deliberating whether to pursue outsourcing, departments should first consider the following:

**Legal issues.** The government has extensive constitutional and common law powers to enter into outsourcing contracts. However, these powers may be constrained by specific legislation. For example, an ordinance might require that a particular function be carried out by a public officer or by a specific departmental officer. Departments must examine possible legal constraints on intended outsourcing proposals at an early stage. The Department of Justice can advise if the legislation in question is unclear, and whether a proposed outsourcing would be ‘ultra vires’.

**Privacy and confidentiality.** Departments may maintain records of individuals’ private or confidential information. Some outsourcing could lead to this information becoming available to the service provider’s employees. Steps should be taken to apply the same level of privacy protection as when the information was held by the departments. This may require all those with access to the information to sign confidentiality agreements.

**Knowledge of government.** When a service is delivered by civil servants, it is expected that they have a very close knowledge and understanding of government requirements. It is sometimes perceived that an external service provider could not have the necessary depth of knowledge and understanding. The reality is that those delivering the service, whilst not direct employees of the government, could have the knowledge and understanding to carry out the activities required. It is the responsibility of the outsourcing department to define precisely the knowledge required.

**Disengagement.** In entering into an outsourcing contract with a service provider, there may be concerns about the ability of the government to terminate the contract and revert to the previous internal service delivery arrangements or engage another suitable service provider. One of the tasks that should be addressed in every outsourcing project is the impact of the service provider not being able to perform the service. An integral component of the outsourcing process must be to identify and set up plans to minimise and mitigate this risk. Arrangements for disengagement will be less complicated if this risk is taken into account at an early stage.



**Political environment.** The possibility of an outsourcing project becoming politically sensitive must be addressed during the planning process. Areas of sensitivity may include the impact of changes on external clients or the community more generally. A department considering outsourcing options should examine how stakeholders will be affected by a shift to outsourcing arrangements, what their reactions might be and how to build appropriate communication into the outsourcing process.

**Internal and external consultation.** For most outsourcing projects, the human implications require close attention from the outset. It is sensible to ensure that all internal stakeholders, particularly staff, are aware of the project, the project timetable, and the impact the project may have on them or those they represent. Close liaison and co-operation with staff are more likely to lead to better outcomes than the adoption of a non-consultative approach.

During the planning process, a programme should be developed to ensure the staff are kept informed. This should contain mechanisms for regular and open communication throughout the outsourcing project. If the proposed outsourcing is likely to affect staff that belong to a grade managed by another department it is important to involve the responsible grade management early in the planning process.

Where the service delivery impacts upon external stakeholders, departments should consider the timing and extent of consultation with District Councils, advisory bodies etc.

## 1.4 Managing the process

The outsourcing process consists of three phases, with supporting processes common to each phase. Figure 1.1 on the following page shows the total process in overview.

Before the process commences the department will complete two actions. First, it will make an assessment whether it is in principle possible and desirable to use the private sector to deliver the service. Second, in order to pursue this in-principle position, the department will allocate responsibility for investigating the options by appointing a team to manage the business case development.

**Phase A - Developing the business case.** This is the pre-outsourcing decision phase directed by senior management to identify potential candidates for outsourcing. Outsourcing is one of the options that should be considered here. Other options may include other PSI alternatives or internal improvement and reorganisation solutions.

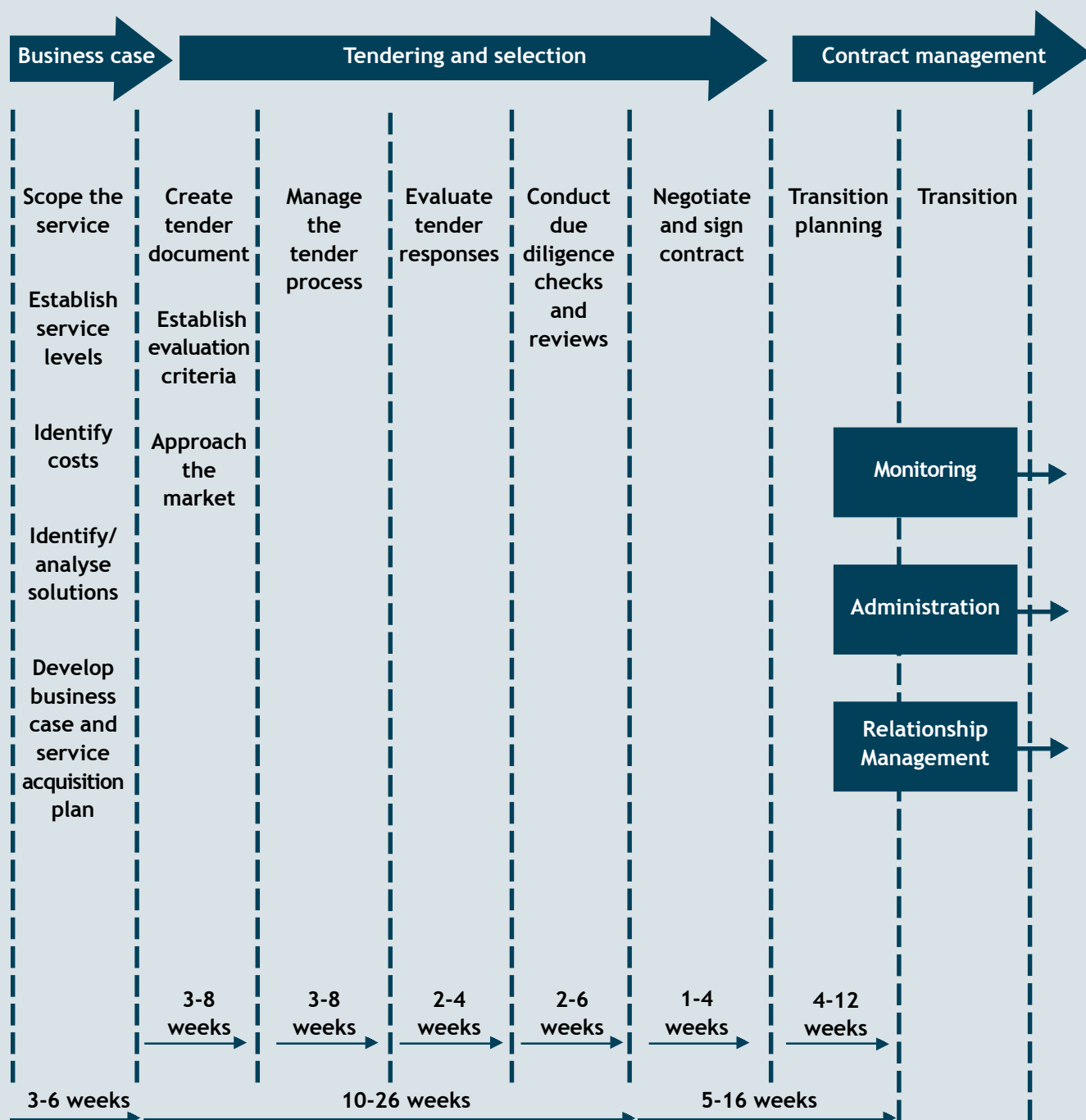
**Phase B - Tendering and selection of the service provider.** If the decision is to proceed with outsourcing, this phase examines the steps involved in defining the scope of services, approaching the service provider market and managing the tenderer selection. It includes documenting requirements, establishing a preliminary service level agreement (SLA) and evaluating responses from service providers. Departments should be able to provide potential service providers with an indication of service levels expected so that the service providers will be able to price accordingly.

**Phase C - Managing the contract.** The outsourcing contract is finalised and there is a planned transition to the outsourcing arrangements. Procedures for monitoring the contract are set in place and the department works with the service provider to build an open and sustainable relationship focussed on the quality of the services delivered.

Figure 1.1: Outsourcing process overview



Figure 1.2: Indicative time line for an end-to-end outsourcing project



*Support processes extend across the three phases of outsourcing and include project management tasks to support the outsourcing project*

*A well executed outsourcing arrangement takes time to achieve*

## 1.5 Setting up support processes

The support processes ensure that the outsourcing process and the resulting contract are an ongoing success. These processes address the key areas of planning and control, managing quality and managing people. In investigating and subsequently implementing outsourcing, the first step for a department is to appoint a suitable project team to take the project forward. Without a good team many outsourcing projects take longer to achieve, are more contentious and fail to achieve the full benefits expected. Chapter 5 of this Guide provides more detail on the setting up of support processes.

## 1.6 Setting the timetable

Many failures in outsourcing arise from insufficient time and resources being applied to the key steps of:

- ♦ Service level specification
- ♦ Tender document preparation
- ♦ Tendering
- ♦ Selection
- ♦ Contract negotiation
- ♦ Contract finalisation
- ♦ Transition to new service arrangements
- ♦ Contract management.

There is no prescribed time for an outsourcing project. It will depend on the department's readiness and skills, and the complexity of the services to be outsourced. An example of a schedule for the outsourcing process is provided on the previous page. This time line is indicative only - achieving this will require good planning and the time scale of any outsourcing project will depend on the complexity of the case and on other issues facing the department at the time.

## Chapter 2 Phase A: Developing the Business Case

This is the pre-outsourcing decision phase where a department makes a strategic decision about how a service should be delivered. Outsourcing is one of the options within the government's PSI framework that should be considered. The main tasks of this phase are summarised below.

Tasks / Actions	Focus / Responsibility / Deliverable
<b>A.1 Scope the service</b> <ol style="list-style-type: none"> <li>1 Consider the service's relationship to the department's overall strategy and direction</li> <li>2 Consider the impact of the service on other areas of the department</li> <li>3 Prepare a statement of current requirements</li> <li>4 Make the first stop/go decision</li> </ol>	<b>Senior management focus</b> Determine the scope and potential for outsourcing of the service <b>Responsibility</b> Outsourcing project team <b>Deliverable</b> Scoping report
<b>A.2 Establish the required future levels of service</b> <ol style="list-style-type: none"> <li>1 Define the future services and the parties' responsibilities</li> <li>2 Determine the required service levels</li> </ol>	<b>Senior management focus</b> Determine a service standard that is reasonable when compared to the current standard, and identify improvements that may be available to the department <b>Responsibility</b> Senior management and other stakeholders <b>Deliverable</b> Preliminary SLA
<b>A.3 Identify the costs</b> <ol style="list-style-type: none"> <li>1 Conduct a preliminary analysis of internal costs</li> <li>2 Benchmark internal costs</li> <li>3 Estimate the external and internal costs of outsourcing</li> <li>4 Compare outsourcing costs with benchmark costs</li> </ol>	<b>Senior management focus</b> Consider all the costs <b>Responsibility</b> Outsourcing project team <b>Deliverable</b> Internal costing model
<b>A.4 Identify and analyse potential solutions</b> <ol style="list-style-type: none"> <li>1 Identify internal and external options</li> <li>2 Evaluate the market</li> <li>3 Conduct a cost/benefit analysis of the options identified</li> </ol>	<b>Senior management focus</b> Examine whether the solutions take into account the risk to service delivery, long-term strategy, impact on clients, integration and internal capability <b>Responsibility</b> Outsourcing project team <b>Deliverable</b> Analysis and evaluation of solutions
<b>A.5 Document the business case and service acquisition plan</b> <ol style="list-style-type: none"> <li>1 Document the business case together with risk analysis</li> <li>2 Prepare detailed service acquisition plan</li> </ol>	<b>Senior management focus</b> Determine if a viable business case exists to proceed with outsourcing the service <b>Responsibility</b> Outsourcing project manager <b>Deliverable</b> Recommendation supporting or rejecting outsourcing as an option (business case report)

**Task A.1 Actions**

- 1 Consider the service's relationship to the department's overall strategy and direction**
- 2 Consider the impact of the service on other areas of the department**
- 3 Prepare the statement of current requirements**
- 4 Make the first stop/go decision**

**A.1 Scope the service**

When examining the viability of outsourcing, the department should compare internal and external options and define the parameters, including the scope and cost. The cost and benefits of these options are compared against each other, as well as among identified service candidates. From this, the most viable alternative is identified, a priority list of outsourcing is drawn up, and a business case is prepared for those services the department thinks are the most likely candidates to be outsourced.

In order to determine whether a service should be outsourced, the department needs to know what the service is, how it is delivered and what it costs. From this, decisions can be made about future service requirements. At the end of these tasks - if the merits of the different alternatives are clear cut - it may be possible to decide whether to go forward or not with an outsourcing solution without any further analysis.

**A.1.1 Consider the service's relationship to the department's overall strategy and direction.** This action consists of reviewing the business direction being undertaken by the department, its strategic position and objectives for the future.

For example, in outsourcing IT management and servicing, the department needs to consider how the use of technology in the delivery of services will evolve, the impact of this on future service direction and whether this is likely to change over time. These issues will focus attention on the government's service-wide Digital 21 Strategy for Hong Kong and the role of technology in the department's medium term business strategy. These key considerations will affect the form of any alternative delivery arrangements considered and the final development of the business case.

This can be carried out by the staff currently providing the service or by a third party. They should consider the environment in which the service area operates, how it relates to the other areas of the department, and the impact of government policy or regulations on outsourcing this service area.

For example, a department outsourcing its records management function will need to consider the various classifications of its records to determine suitability for outsourcing. Many of its records may be suitable for storage offsite using a service provider. However, information and documents involving classified material may need to be kept within the department's control. The level of control required will affect the department's decision on whether outsourcing is viable.

**A.1.2 Consider the impact of the service on other areas of the department.** The department needs to consider whether there are synergies between related service areas that could be taken advantage of through outsourcing.

For example, accounts receivable functions and debt collection are closely related. When looking at outsourcing one of these functions, it is a good idea to consider outsourcing the other function. The systems are closely related and a service provider may have access to advanced technology that will enable the implementation of a better process for both functions.

The impact of changes in the delivery of the service also needs to be considered in terms of the risks that these changes present; and how they will be managed to achieve the department's objectives. A formal process of risk analysis should be carried out during the business case preparation (see section A.5).

**A.1.3 Prepare the statement of current requirements.** The statement of current requirements describes the existing service and how it has been provided. The following must be documented:

- ♦ What the service is and who the clients of the service are
- ♦ The required outcomes (the current service level)
- ♦ Relationships between the in-house service team and other units/functional areas, either inside the department or in another organisation

For example, finance and administration units generally have an organisational relationship with procurement units. Each existing organisational arrangement or process that links these functions needs to be examined. The examination should include the technology used to connect the different functions; descriptions of where interrelated tasks or processes begin and end; and an overview of how each unit is involved in the process. This will determine the scope of the service performed and whether any of the interrelated units could perform some or all of the services provided.

- ♦ Skills analysis of the incumbent staff (identifying what they do and the gaps between their current skills and the skills needed in the future)
- ♦ An inventory and description of third party contractual obligations (existing contracts, both internal and external, may form part of the outsourced arrangements and need to be phased out or maintained within the new structure)
- ♦ Disaster recovery and service continuity requirements, such as business process improvements. This is especially necessary for services with a direct impact on the public
- ♦ Other opportunities for improvement such as business process re-engineering (the realisation of these opportunities could produce better results than outsourcing in some cases)

For example, a unit may be able to re-engineer its accounts payable processes to improve them rather than outsourcing the service. It could also identify opportunities to improve staff productivity and skills through training. These may be required to bring service levels in line with best practice.

It is advisable to involve staff from the service unit being considered for outsourcing, as they are often best placed to provide an accurate and realistic picture of the current requirements.

**A.1.4 Make the first stop/go decision.** This step involves a preliminary, high-level assessment of the feasibility of outsourcing. It should be made by departmental senior management based on strong evidence that outsourcing is either:

- ♦ A feasible way forward to meet the department's objectives, or
- ♦ Premature at this stage, although desirable in principle.

Cases where the reasons to pursue outsourcing are compelling might include situations where:

- ♦ The department wishes to take on new functions
- ♦ Resources are required to meet workload fluctuations on a seasonal or other cyclical basis
- ♦ The department intends to expand an existing function

*Departments need to know what they want to get from outsourcing. Defining current and future needs is critical to achieving this*



- ♦ Key expertise, leading edge skills or technology that is required is lacking in the civil service
- ♦ There is an active and competitive market of service providers whose performance of the service is demonstrably superior to the department's.

A decision to proceed no further at this early point must be supported by clear and appropriate criteria such as:

- ♦ Urgent improvements are required to processes that extend across the department, including the function being considered, before an outsourcing option can be realistically considered
- ♦ Privacy/security issues require that only civil servants can handle key, integral elements of the service
- ♦ Existing legislation affecting the service requires amendment to allow non-civil service involvement.

It is possible that at this very early point in analysis the department may have enough information to proceed to an alternative solution to outsourcing. This may be an alternative PSI arrangement; an in-house improvement solution; or a decision to discontinue the service in its entirety.

### Task A.2 Actions

#### 1 Define the future services and the parties' responsibilities

#### 2 Determine the required service levels

## A.2 Establish the required future levels of service

Preparing the business case requires developing a preliminary SLA, which describes the service or set of services that are to be supplied to government users or the community. It also defines the standard to which these services will be delivered in order to satisfy the department's objectives for the service. The preliminary SLA will enable the department to compare the current service with other delivery options identified during the business case analysis. It will also be used to prepare the statement of requirements for future services in the tender documentation if the department proceeds with an outsourcing option.

**A.2.1 Define the future services and the parties' responsibilities.** It is likely that the services the department provides in the future will differ from those currently provided. Drawing on the statement of current requirements already prepared during the service scoping stage, a revised statement of requirements should be prepared that reflects and spells out the department's future needs. This will normally form the basis of the SLA.

In defining the future services, it is necessary to consider the term over which the services are to be provided. This will depend on the type of service and risk profile. A department should avoid being locked into a high-risk arrangement for a long period. Nonetheless, the investment costs for some services may be such that a longer term is required to encourage good outsourcing partners to come forward.

Both the department and the service provider will have responsibilities within the scope of the SLA. Each party's responsibilities are determined by analysing the entire service scope and allocating responsibility for each element of the service to either party. Broadly, the service provider is responsible for day-to-day service operations while the department monitors the provider's performance.

The following is an example of each party's responsibilities that may be documented in the SLA.



The department will be responsible for:

- ♦ Specifying the service requirements
- ♦ Advising the service provider of operational requirements
- ♦ Ensuring that users (internal and external) are aware of the scope of the agreed services and the related procedures, particularly as they relate to support services
- ♦ Monitoring adherence to agreed policies and procedures relevant to providing the service
- ♦ Advising the service provider of changes to the service requirements and facilities likely to have an impact on current and future use of the service
- ♦ Managing the relationship to ensure issues are resolved quickly
- ♦ Consulting the service provider on all relevant contracts being considered between the department and third party contractors that may have an impact on the service provider's service delivery
- ♦ Helping the service provider deliver the service through briefings, and good and timely feedback on performance.

The service provider will be responsible for:

- ♦ Providing the agreed services
- ♦ Managing the service and suggesting improvements
- ♦ Responding to service requirements articulated by the department and changes to facilities likely to have an impact on current and future use of the service
- ♦ Managing the relationship to ensure issues are resolved quickly
- ♦ Consulting with and seeking the department's agreement to any proposed arrangements for all relevant third party contracts that may have an impact on the service provider's delivery of the services
- ♦ Obtaining written confirmation on estimates and quotations before undertaking any chargeable activity that will affect the price of the contract or the delivery of the services
- ♦ Providing timely and accurate reports on service performance.

**A.2.2 Determine the required service levels.** The department will need to look at each of the service elements to be outsourced; determine the standard required of each; and decide how it will be measured. Service standards define the level of service that the department will expect from the service provider. They are defined by point of delivery, availability, reliability, response time, resolution time and measurement period:

- ♦ **Point of delivery** is generally described under one of the following categories:
  - Location, which is the geographic location, building and/or departmental point at which delivery takes place (the address where the services are physically delivered); and/or
  - Medium, which defines the place/device to or from which the service is delivered. This could be a mobile phone receiving signals or a computer network.
- ♦ **Availability** is the amount of the time that the service is actually available. This is defined as a percentage of the measurement period(s) chosen for reporting purposes.

*Service level standards must be measurable. They will cover:*

- ♦ *Point of delivery*
- ♦ *Availability*
- ♦ *Reliability*
- ♦ *Response time*
- ♦ *Resolution time*
- ♦ *Measurement period*

For example, in an IT environment a service may be described as requiring a computer system availability requirement of 99.9% on a 24-hour x 7-day basis. For a security service the service may need to be available 100% of the time - 24 hours a day, 7 days a week.

- ♦ **Reliability** concerns the maximum acceptable number of individual faults over a measurement period. The service definition will have to make clear what constitutes acceptable or minimum service quality.

For example, the number of acceptable faults in an IT system over a period of a month may be: 1 fault classified as urgent; and 5 faults classified as high priority. For a rubbish collection contract, reliability may be defined as the percentage of rubbish bins that must be emptied within a specified period of time.

- ♦ **Response time** is generally measured by the time taken by the service provider to detect and respond to the occurrence of a fault and/or user request, by providing the required service support.

For example, a response time for a fault classified as urgent in an IT system may be 5 minutes from the fault occurring; for a fault classified as high priority it may be 10 minutes. A cleaning service may need to be on call to clean up spillage or other accidents. In a high use building, the response time to this will be more critical than in a low use building. The cleaners should be required to respond within a specified time from the accident being reported. For a home meals delivery service, the response time to a missed delivery for a diabetic client may be defined as urgent and the response time for rectifying this would be specified in the SLA.

- ♦ **Resolution time** can be defined as the acceptable time for resolving the fault. It is measured from the moment the fault occurred to the moment the fault is resolved.

For example, a fault classified as an urgent priority may be required to be resolved within 1 hour of the fault occurring. A fault classified as a high priority may require resolution within 2 hours of the fault occurring, and so on. For a home meals delivery service, a diabetic client should be provided with a standard meal within 30 minutes from the time of lodging a complaint of missed delivery.

- ♦ **Measurement period** usually refers to the period of time over which the service availability, reliability, response times and resolution times will be measured and reported.

For example, one month is generally considered an adequate measurement period for an IT-related service level.

The information derived for each of the measurement categories will be documented in an SLA format, as illustrated in Appendix 2. The actual format used will vary in the degree of complexity and details required, and by the nature of the service. Some SLAs may be expressed as a table of quantitative measures on a single page; others may run to many pages of description with qualitative and quantitative measures; and some may provide visual evidence standards for the service being outsourced. The issue is not the format but that the required service levels are adequately described so that the department and the service provider can objectively measure performance.

In addition to the service standards the SLA will define responsibility for measurement and frequency of reporting:

- ♦ **Responsibility for measurement** identifies the party responsible for measuring the performance (generally, the service provider). The department will also want to confirm this independently through quality assurance reviews, but at less regular intervals than the reporting by the service provider (see section C.2).
- ♦ **Reporting frequency and method** varies according to the service. A high transaction-based service may require weekly reporting while a low transaction-based service may require monthly reporting. This is generally provided in some form of report, provision of data or exception report.

Examples of SLA terms are provided at Appendix 2.

### A.3 Identify the costs

The department needs to determine what it costs to provide the service in-house. This data will be compared against the costs of the internal and external options identified to carry out the service in the future.

**A.3.1 Conduct a preliminary analysis of internal costs.** This covers the service's current full costs including:

#### Direct costs

- ♦ Current operational costs (including total employment costs, materials, utilities, servicing of equipment, site and ancillary services such as security, cleaning, courier services and specialist printing) together with an estimate of the likely additional costs if the scope of the future services differ from the current services
- ♦ Hardware, software and equipment used in providing the service
- ♦ Capital used exclusively for the service.

#### Indirect costs

- ♦ Services provided by other departments but not charged for
- ♦ Capital and equipment that is not used exclusively for the provision of a service (calculate a proportional share attributable to the service)
- ♦ Overheads that are spread across the whole department (calculate a proportional share attributable to the service).

**A.3.2 Benchmark internal costs.** Non-recurrent costs will be “one-off” while recurrent costs will need to be projected forward in time. The time period for the cost projection will be the term of the possible outsourcing contract. The term will vary subject to the type of service, risk profile and likely investment requirements for any service provider. Three to five years are common contract terms and there are many instances where a longer period is appropriate. Typically, an outsourcing contract is longer than a conventional procurement contract because the service provider's level of involvement with the department is at a more strategic level.

For example, a contract to outsource data processing can have a shorter term than a contract to outsource a strategic sourcing and procurement function. The data processing contract is transaction-based, which involves less system integration and resourcing on both sides. It will take less time for the service provider to achieve the targeted results. Conversely, the strategic sourcing and procurement contract will require considerable system integration, resourcing and financial investment from the service provider.

#### Task A.3 Actions

- 1 **Conduct a preliminary analysis of internal costs**
- 2 **Benchmark internal costs**
- 3 **Estimate the external and internal costs of outsourcing**
- 4 **Compare outsourcing costs with benchmark costs**

The forward projection over the proposed term of the contract will give the department an indicative budget for the service and enable it to compare fully its internal costs with the prices submitted by tenderers. This becomes the “benchmark” cost.

In making the forward estimate of the cost of delivering the current service the department will need to consider if the service is one in which service levels and/or technology are likely to undergo considerable change over the period under consideration. The costs of any technology and equipment upgrades, changes in the provisions of service levels, or changes in the terms and conditions of staff delivering the service (i.e. salary increases or other benefit changes) need to be factored into the forward projection. The use of sensitivity analysis to show the impact of possible cost or service changes is a useful tool.

**A.3.3 Estimate the external and internal costs of outsourcing.** The most direct cost the department will face is the contract price. As a full picture of the service provider’s costs or prices will not be available before tenders have been received, data derived from sources such as colleagues in the civil service who have outsourced similar functions, organisations that advise on outsourcing, or from searching the Internet may be a good reference.

Departments need to consider any local conditions, changes in the economic environment or the market for the service that may make any price data sourced through the above mechanisms outdated or inappropriate.

Apart from the contract price, there are other important costs to be included in an estimate of the cost of outsourcing the service. These include:

- ♦ Cost of tendering the service (e.g. cost of engaging external advisers)
- ♦ Transition costs - when the department is handing over the delivery of the service to the new service provider
- ♦ Contract management costs (including staff cost and related training and development costs)
- ♦ Operating costs of any retained elements of the service or restructured organisation (e.g. salaries, recruitment, training)
- ♦ Cost of reversing the process and bringing the function back in-house.

In order to ensure a level playing field in comparing the cost of outsourcing with in-house provision, the effects of taxation should be taken into account.

For example, departments are not subject to a range of vehicle related taxes that an outsourcing contractor would be.

In estimating contract management costs the department will have to consider how the staffing of the contract management function will be achieved. This will include all staff required to manage and monitor the contract during its term. This may be achieved through redeployment of existing staff of the department or may require recruitment of additional and specialised staff if outsourcing represents a significant expansion on the existing service.

This estimation of all these costs will enable a more comprehensive comparison of the various options, including outsourcing or retaining in-house. The use of sensitivity analysis in modelling the potential costs of outsourcing under different circumstances will help the department consider the many “what if” questions that arise at this point in the process.

Benchmark Internal Costs	Costs of Outsourcing
<ul style="list-style-type: none"> <li>♦ Staff costs of those directly involved in providing the service</li> <li>♦ Other operational costs such as materials, supplies and services</li> <li>♦ Capital, equipment and accommodation exclusively used for the service</li> <li>♦ Support services provided by other staff within the department or from other departments</li> <li>♦ Proportional share of the capital, equipment and accommodation in use attributable to the service</li> <li>♦ Overheads</li> </ul>	<ul style="list-style-type: none"> <li>♦ Contract price for the outsourcing service</li> <li>♦ Staff and operating costs of retained elements of the service</li> <li>♦ Cost of tendering the service, e.g. cost involved in tender evaluation and selection</li> <li>♦ Transition costs, e.g. planning for transition and handover arrangement</li> <li>♦ Contract management cost, e.g. performance monitoring and related administration work</li> <li>♦ Cost of reversing the process, e.g. contingency plan</li> <li>♦ Overheads</li> </ul>

**A.3.4 Compare outsourcing costs with benchmark costs.** Compare the benchmark internal costs with the likely costs of outsourcing over the term of the contracting period. Cost comparisons should assume the provision of the same levels of service. An example of the cost elements to be covered is as follows:

The types of costs incurred will vary in different options under different scenarios. Departments should model these costs for the effect of changes in service levels, changes in technology, equipment upgrades, staff transition, and changes in the terms and conditions of staff over the life of the contract.

## A.4 Identify and analyse potential solutions

The objective of this exercise is to identify internal or external options to provide the service. The department can compare these options with the current service performance, using the costs and service level data collected in the scoping and cost studies. The outcome of this comparison will indicate whether outsourcing is a viable option or whether another option - internal or external - should be considered.

**A.4.1 Identify internal and external options.** Besides providing a profile of the current service, the service scoping study may identify possible improvements to the service as well as alternatives to outsourcing. Each solution identified should be included for consideration on the basis of its assessed potential for satisfying the objectives of the change. The range of available solutions involving the private sector were listed in section 1.1 of this Guide. Both external and internal solutions may include:

- ♦ Implementing a shared services model (common corporate services across the department, or departments, are bundled into one central area)
- ♦ Bundling related groups of services (this may make processes more efficient and also cut costs)
- ♦ Investing in new technology
- ♦ Updating skills (this may involve training, redeploying or recruiting staff)

### Task A.4 Actions

- 1 Identify internal and external options**
- 2 Evaluate the market**
- 3 Conduct a cost/benefit analysis of the options identified**

- ♦ Restructuring or re-engineering the service (to improve processes and reduce costs)
- ♦ Reviewing and improving internal service levels (e.g. setting realistic service levels).

**A.4.2 Evaluate the market.** Evaluating the market is an important step in determining the viability of the outsourcing option. If there is a competitive market with many service providers, the outsourcing solution is strengthened. If the market is weak with a limited number of service providers, the department needs to take this into account in its risk assessment. Sometimes there is little or no capability in the local market because the government is the current de facto monopoly supplier. In these circumstances the department must consider whether the necessary skills can be imported or otherwise supplied.

Evaluating the market involves:

- ♦ Identifying potential service providers and their capabilities
- ♦ Evaluating the options offered by the industry
- ♦ Researching market prices to confirm earlier estimates (see section A.3.3).

**A.4.3 Conduct a cost/benefit analysis of the options identified.** The department needs to conduct a cost/benefit analysis on all the options identified by making reference to the cost elements at section A.3.4.

Apart from analysing the tangible costs and projected savings, the following factors should also be taken into account for evaluation:

- ♦ Review the fit between the objectives for change and all the options identified

For example, if an essential objective is to produce a target level of service availability then all options that cannot meet this objective will be discounted from further consideration.

- ♦ Review the fit between the options identified and the department's strategic direction
- ♦ Consider the potential intangible benefits (e.g. flexibility to respond to changing needs and reliability of performance)
- ♦ Identify the key risks and how they will be managed
- ♦ Consider the impact on the staff (e.g. their likely response to the changed arrangements, any requirement for internal transfers, redeployment and/or retraining)
- ♦ Consider the effect on the service area and on units aligned with it
- ♦ Consider the requirement for asset transfers or disposal
- ♦ Consider the economic impact of business activities (e.g. profit taxes, duties and government fees to be paid by a private service provider)
- ♦ Review the public relations impact.

Armed with an estimate of the costs, benefits and risks of each option, the department will be able to compare these and recommend the best option to deliver its service.

## A.5 Document the business case and service acquisition plan

The business case should include sufficient information for senior management to decide whether the recommended option satisfies the objectives for change. It will also provide an approach to acquiring the services from the external market.

*An often neglected part of evaluating an outsourcing option lies in examining the lessons learned by other organisations - by talking to colleagues in the civil service or industry networks*

### Task A.5 Actions

- 1 Document the business case with risk analysis
- 2 Prepare detailed service acquisition plan



**A.5.1 Document the business case with risk analysis.** The business case should state clearly which option best supports the objectives for change and provide sufficient supporting data. Appendix 3 provides an indication of the matters that may be covered in the business case preparation. The hierarchy of analysis requires that the objectives of the department in pursuing outsourcing are clear and that outsourcing will satisfy these objectives; the cost/benefit of the preferred option is demonstrated; and the risks are adequately assessed and catered for in the recommended approach.

The department may need to discuss the proposals with others such as the relevant policy bureau and the Civil Service Bureau (if surplus staff will result). It should also prepare a communication strategy for stakeholders such as its staff, service clients and the community.

The risk analysis element of the business case deserves special attention. Risks are inherent in both internal and outsourced service delivery. The department must undertake an objective assessment of the risks involved both in pursuing outsourcing and maintaining the service in-house; identify how likely the risk is and how manageable it will be; and consider the necessary contingency planning that will be required to ensure the management of the risks. The business case itself should include a preliminary risk management strategy for any risks identified with the preferred course of action. Further details on structured processes for risk management are provided in Appendix 4 Risk Management and Appendix 5 Transition Planning.

**A.5.2 Prepare detailed service acquisition plan.** A detailed acquisition plan should be developed to complement the business case - that is, how the department will go about securing a service provider. It is important that the plan describes the various options and provides substantive reasons for a recommendation to proceed with the tendering method.

The government has four ways of approaching the market through tenders. These are:

- ♦ **Open tendering**, where any interested service provider may choose to submit a tender
- ♦ **Selective tendering**, where all registered service providers with the relevant qualifications are invited to submit their tender
- ♦ **Pre-qualified tendering**, where tender invitations are sent by letter to those service providers whose pre-qualification has been approved on the advice of the relevant tender board
- ♦ **Single or restricted tendering**, where tender invitations are sent to only one or a small number of service providers approved by the Secretary for Financial Services and the Treasury or the Director of Government Logistics. This procedure is only used when circumstances do not permit open tendering (e.g. due to extreme urgency or security, or for proprietary products).

The service acquisition plan needs to be more comprehensive than merely selecting the tendering mechanism. It should also involve:

- ♦ Consideration of the processes to be adopted in managing tendering
- ♦ Preparation of a project plan to map out milestones, deliverables, resources and timing associated with the tendering and selection process.

The appointment of an external or independent reviewer (sometimes known as a probity auditor) to oversee the implementation of the proposed acquisition plan can also be considered as an element of the strategy.

## Chapter 3 Phase B: Tendering and Selection of the Service Provider

Having made the decision to outsource, the department moves into the phase of tendering for and selecting the service provider. The process by which the service provider is selected will influence the ongoing relationship. Fairness, merit and thoroughness are the precepts that should guide this phase. The Stores and Procurement Regulations (SPR) set out the allowed actions in tendering and selection. This Guide has been prepared to fit within the SPR framework. It does not supplant the SPR and departments must familiarise themselves with the SPR before commencing tendering and selection. A list of regulations/circulars/guides related to tendering is at Appendix 6.

Tasks / Actions	Focus / Responsibility / Deliverable
<b>B.1 Create tender documents and set evaluation criteria</b> 1 Finalise the statement of requirements 2 Develop the financial assessment model 3 Develop the conditions of tender and draft the contract 4 Establish the evaluation team 5 Establish the evaluation criteria and weightings	<b>Senior management focus</b> Consider and approve criteria <b>Responsibility</b> Project manager, supported by the evaluation team <b>Deliverable</b> Tender documents, draft contract, selection criteria, criteria weightings and marking scheme
<b>B.2 Manage the tender process</b> 1 Establish the tender framework 2 Finalise the list of tenderers and make the tender documents available 3 Conduct a briefing for tenderers 4 Receive tender submissions	<b>Senior management focus</b> Approve process <b>Responsibility</b> Project manager <b>Deliverable</b> An ethically managed tender process
<b>B.3 Evaluate tender responses</b> 1 Evaluate tender compliance 2 Evaluate tenders in detail 3 Financial vetting 4 View tenderer presentations and conduct site visits 5 Recommend service provider	<b>Senior management focus</b> Consider and approve start of negotiations with recommended service provider <b>Responsibility</b> Evaluation team <b>Deliverable</b> Tender evaluation document and recommendation



Tasks / Actions	Focus / Responsibility / Deliverable
<b>B.4 Conduct due diligence checks</b> <ol style="list-style-type: none"> <li>1 Conduct due diligence review of the service provider</li> <li>2 Facilitate due diligence review by the service provider</li> </ol>	<b>Senior management focus</b> Accept results of due diligence investigations and approve/disapprove recommendation(s) <b>Responsibility</b> Evaluation team <b>Deliverable</b> Due diligence information, with a recommendation of whether outsourcing is still viable
<b>B.5 Negotiate the contract</b> <ol style="list-style-type: none"> <li>1 Set the negotiation framework</li> <li>2 Establish the negotiating team</li> <li>3 Negotiate a value for money contract</li> <li>4 Obtain clearance to finalise the contract</li> </ol>	<b>Senior management focus</b> Consider and approve contract <b>Responsibility</b> Negotiating team and senior management <b>Deliverable</b> Signed contract

## B.1 Create tender documents and set evaluation criteria

Preparation of elements of the tender documentation can be complex. It requires knowledge of both the service area and of contract preparation. If the department does not have staff with the right skills for this stage, it is advisable to obtain specialist advice for documenting the requirement, financial modelling and developing the contract.

The tendering method and some components of the documentation will have been created during the business case phase. The method selected will dictate the structure of the documents.

The typical document structure of an invitation to tender (ITT) will include the following elements:

- ♦ Covering letter
- ♦ Tender form (GF 231)
- ♦ Terms of tender
- ♦ Statement of requirements or tender specification
- ♦ Conditions of contract
- ♦ Offer to be bound

Some examples of tender documents, contracts in different service areas are provided in the CCGO website under Public Sector Reform/Private Sector Involvement/PSI Guides, References and Links - "Tender Documents/Contracts in Use".

**B.1.1 Finalise the statement of requirements.** The department's requirements are defined in a statement of requirements document, which sets out clearly the mandatory and desirable requirements. The department's needs must be clear so that service providers

### Task B.1 Actions

- 1 *Finalise the statement of requirements*
- 2 *Develop the financial assessment model*
- 3 *Develop the conditions of tender and draft the contract*
- 4 *Establish the evaluation team*
- 5 *Establish the evaluation criteria and weightings*

*Tender documents  
should focus on  
outputs not  
methods*

will know what provisions they must fulfil and where they may have discretion to add value. Preparation of a precise and well thought out statement of requirements will assist the subsequent assessment of compliance.

The document should state the requirements in terms of “what” the required outputs/ outcomes are rather than “how” the work is to be performed. A statement of requirements that prescribes the delivery method may result in viable alternative methods being discounted too early in the process.

The preliminary SLA developed in Phase A will be the basis of this document and should be reviewed and amended as necessary. It can then be incorporated into the final statement of requirements.

The document should include the following:

- ♦ **Description of environment.** This may include the whole department, interacting units, geographical locations, systems and infrastructure.
- ♦ **Description of requirement.** This describes what the service is and constitutes the main part of the tender specification. It does not prescribe a process, but specifies what output or outcome the department requires. It should only describe processes to the extent that legislation dictates. The table below compares input-based (“how”) and output-based (“what”) requirements.

Comparison of input / output statements for the service level required	
Input-based	Output/Outcome-based
Floor 11 of the building must be cleaned: <ul style="list-style-type: none"> <li>♦ By a minimum of five staff</li> <li>♦ Using Acme detergent and Acme mops</li> <li>♦ Once a day</li> <li>♦ To the standard required</li> <li>♦ Not during business hours</li> </ul>	Floor 11 of the building must be cleaned daily to the standard required and not during business hours
<ul style="list-style-type: none"> <li>♦ The call centre must be staffed 24 hours a day, seven days a week</li> <li>♦ There must be 20 staff available to answer calls at any given time</li> <li>♦ The telephones must be Lucent telephones</li> <li>♦ The staff will wear headsets at all times</li> </ul>	80% of incoming telephone calls must be answered at all times within three rings, with an average call answering time of two rings

Guidelines for preparing service level specifications are at Appendix 7.

- ♦ **Transition and implementation requirements.** The tenderer should be required to submit a draft transition and implementation plan as part of the response to the tender. Handing over the service delivery may take some time to phase in after the contract is signed and the transition and implementation requirements outlined at this point will assist both the selection process and the department’s own transition planning. The main elements listed below for transition planning need to be considered by both the department and the tenderer.

### Matters to be considered in planning for the transition and implementation of the outsourced service arrangement

- ♦ Definition of each party's responsibilities
- ♦ Organisational structure for any residual functions
- ♦ Timetable to implement the arrangements for the residual functions
- ♦ Notification and process of handover
- ♦ Service delivery monitoring mechanisms
- ♦ Approval and audit processes
- ♦ Payment processes
- ♦ Staff redeployment to service provider or other departments
- ♦ Staff job descriptions, employment contracts, recruitment, training
- ♦ Change management strategy
- ♦ Disposal or transfer strategy for assets
- ♦ Expiry, termination and assignment plans for third party contracts

- ♦ **Request for tenderer's conditions or assumptions.** Tenderers should be requested to prepare their response showing how they will meet the service requirements specified by the department. This response must make clear any tenderer assumptions about actions to be completed by the department or other stakeholders, or any other conditions that have a direct bearing on the viability of their proposed solution.

**B.1.2 Develop the financial assessment model.** In preparing the financial aspects of the tender the department needs to determine the best method for pricing the tender and how the financial information submitted by tenderers should be presented to assist comparison.

The pricing model represents decisions by the department on the best way to structure a price (and payment) for the service to be outsourced. There are three common pricing models (outlined below) which are used in different circumstances.

### Commonly used pricing models

Model	Advantage
Fixed price (for full service)	Provides the department with predictable and defined costs
Payment for use	Allows for the size of the requirement to fluctuate - requires some form of unit costing
Incidental costs parameters	<p>Allows for unpredictable costs associated with the provision of the service</p> <p>For example, a property management contract may include a payment for unscheduled repairs up to a certain capped amount and then an approval system for amounts exceeding that cap.</p>

The department should develop a financial assessment model to assist it in the collection and assessment of the financial elements of the tenderers' submissions. This assessment model can be based on the cost model developed during the business case phase. It should specify all relevant categories of costs to be submitted by the tenderers so that the evaluation team can compare the prices submitted by tenderers against each other and against the benchmark cost.

For the full evaluation, the costs may be placed under the following headings:

- ♦ Service provider costs
  - Contract price (and cost elements)
  - Incentives/rewards to the service provider for superior performance as specified in the tender specification.

For example, a bonus payment to be given to the contractor if the outsourcing project can be completed within a particular period of time in advance of the deadline.

- ♦ Department costs
  - Current cost of delivery
  - Contract management costs
  - Transition costs and contract termination cost.

**B.1.3 Develop the conditions of tender and draft the contract.** Tender documents must specify the rules under which the tender process will be conducted. A standard government terms and conditions of tender document (GLD-Terms-2) outlines common clauses that appear in many government tender documents. A complete set of tender documentation includes:

- ♦ **Terms of tender.** The process for submitting a tender
- ♦ **General conditions of contract.** The conditions which must be complied with in executing the contract
- ♦ **Special conditions of contract.** Any conditions specific to the contract
- ♦ **Offer to be bound statement.** To be signed and completed by the tenderer
- ♦ **Tender specifications.** Description of the services to be provided and against which the tenderers' submissions will be evaluated (see section B.1.1).

The draft contract will provide the basis of the final contract to be signed between the department and the successful tenderer, and is issued with the tender documents.

In addition to the material provided in GLD-Terms-2, the department may need to identify additional requirements and contractual outcomes. This is best done with legal advisers and the stakeholders (e.g. the key service users and current internal service providers). Tender documents and contracts should be cleared with the Department of Justice in accordance with SPR.

The structure of an outsourcing contract differs from a standard procurement contract because an outsourcing arrangement is more like a business partnership than a traditional product supplier/buyer relationship. In an outsourcing relationship, the parties should share risks and work together towards shared objectives.

The contract should be drafted taking account of the issues at Appendix 8.

Best practice reveals that good contracts have the following characteristics:

- ♦ **Contracts should be tight.** The foundation of a successful relationship is a well-designed contract. In a tight contract, both parties are clear about what the scope covers as the SLA describes comprehensively the required services and performance levels
- ♦ **Contracts should be flexible.** Contracts should provide a mechanism to allow changing needs to be met. In a standard government contract this is generally covered by a clause that allows for “options exercisable by the procuring entity”. From the department’s stand point, a long-term contract for services should not be iron-clad, as objectives, requirements, processes and technology are constantly changing

For example, flexibility encompasses the ability to easily handle more transactions, change administrative arrangements, replicate the operation in an extra location, modify software or run on upgraded hardware.

- ♦ **Contracts should encourage, rather than penalise.** Contracts should be about conditioning behaviour rather than triggering penalties

For example, when the supplier fails to meet the SLA in cleansing service, the department may choose not to impose negative action (such as not being considered in providing cleansing service to the government for a particular period of time) but, instead, to work with the supplier to prevent this happening again. (Exceptions, of course, would be made in cases where damages arise.)

There is a shift towards a partnering relationship, so the inclusion of formal bonuses, such as gains-sharing, may become more appropriate as the relationship matures. In doing this the department needs to minimise the danger of the service provider focussing on the bonus areas to the detriment of other areas by implementing a bonus system that encourages desired behaviour.

**B.1.4 Establish the evaluation team.** Ensure that key stakeholders are represented. The tender evaluation team should include technical/operational, business, financial and senior management representatives, and outside experts if required. To enhance independence, consider having at least one person external to the department on the team.

**B.1.5 Establish the evaluation criteria and weightings.** The evaluation criteria can be developed by reference to the statement of requirements document. The criteria are generally classified as:

- ♦ **Technical/operational.** This usually makes up the major portion of the evaluation process. It covers the extent to which a tenderer meets the terms of the draft contract including technical and service specifications.
- ♦ **Financial.** This covers both price as well as consideration of the financial viability of the tenderer.

Consideration should be given to the weighting of the evaluation criteria, and use of an appropriate marking scheme. In designing a marking scheme, the following issues should be considered:

- ♦ Classification of evaluation criteria into mandatory and desirable
- ♦ The passing marks under each category of criteria and the overall passing marks
- ♦ The use of objective and measurable evaluation criteria for rating
- ♦ The weights reflect the relative importance of the criteria to the department
- ♦ The scheme is transparent and clear to the tenderers

- ♦ The scheme is flexible enough to differentiate and rank the qualitative competitive edge of compliant bids.

The use of a marking scheme generally requires separate evaluation of price and technical criteria, generally known in the civil service as the “two-envelope” system.

Other evaluation requirements may involve carrying out financial vetting on short-listed tenderers. If this is required it should be specified in the tender documentation. This is discussed in section B.3.3.

After the technical evaluation criteria are identified, they are classified between mandatory and desirable (added value) criteria. The table below illustrates such a division.

Examples of evaluation criteria	
Mandatory criteria	Desirable criteria
Provision of stationery as required within approved delivery times	Intranet-based ordering system that provides an online catalogue for browsing, anticipates monthly ordering amounts, automatically orders these amounts and automates approval procedures for purchases outside of normal discretionary amounts
The service provider must be able to supply vehicles that can carry three adult passengers in addition to the driver	There will be a choice of the colour of the vehicle and the upholstery colours

The department needs to assign numerical weightings for each element of the mandatory and desirable evaluation criteria. The point of the evaluation criteria and a marking scheme is to develop a rigorous and defensible approach to making assessments about the relative merits of the different tenderers. The SPR provide guidelines for adopting a marking scheme for tender evaluation. Appendix 10 provides some additional advice on evaluation criteria and scoring.

Unless the use of a standard marking scheme for the type of contract has previously been authorised by the relevant tender board, marking schemes must be submitted to the relevant tender board for approval before the tender is issued. An overall pass mark and/or minimum scores for individual attributes may be proposed.

## B.2 Manage the tender process

The department will generally advertise an outsourcing project through an ITT.

When the range of potential solutions cannot be readily ascertained or the service provider market is not well known, ITT may be preceded by a request for an Expression of Interest (EOI).

The EOI can be used either to establish the availability of providers capable of meeting the department’s needs (ahead of the subsequent use of an open ITT) or to create a list of providers to whom a subsequent selective tender is issued. Use of the EOI process is likely to result in a more clearly defined ITT document.

### Task B.2 Actions

- 1 Establish the tender framework
- 2 Finalise the list of tenderers and make the tender documents available
- 3 Conduct a briefing for tenderers
- 4 Receive tender submissions

**B.2.1 Establish the tender framework.** Tender management demands the use of best practice principles. The following should be followed throughout the process:

- ♦ Keep the process transparent and open.

For example, note and file all relevant communications and ensure all potential tenderers have equal access to the same information.

- ♦ Minimise opportunities for unethical behaviour.

For example, channel all communications through a designated officer.

- ♦ Design a process that is independently conducted, competitive and anti-monopolistic. To limit the opportunity or appearance of bias, the identity of tenderers may be withheld from the evaluation team. Nonetheless, all evaluation team members will need to declare any possible conflicts of interest.
- ♦ Maintain appropriate confidentiality of tender submissions. It is important to be aware that some of the information submitted by tenderers constitute their intellectual property as a trade secret; they cannot be used by the department without the tenderer's prior approval. If departments are in any doubt concerning intellectual property rights embodied in tenders they should consult the Intellectual Property Department.
- ♦ The department's right to negotiate should be included in the terms of tender.

**B.2.2 Finalise the list of tenderers and make the tender documents available.** Once the tender documents are finalised, the department needs to make the tender documents available using the service acquisition process determined during the business case phase (see section A.5.2) and in accordance with the SPR. Where the department physically provides hard copies of the tender documentation to tenderers it should check that the documents have been received. If the tender is advertised electronically this receipt process is not required. Electronic issuance of tender documentation should request contact information from all organisations downloading the documentation in order to provide follow-up information as necessary.

The same method of communication should be used to ensure that all relevant and additional information arising during the tender process can be forwarded to potential tenderers. For example, where one prospective tenderer seeks and is provided with additional information that should be made available to all tenderers.

**B.2.3 Conduct a briefing for tenderers.** If the department intends to hold a briefing for tenderers, this should be mentioned in the ITT and in the tender documentation, identifying time and location. Issues typically covered in a tender briefing session include:

- ♦ Scope and scale of services to be outsourced
- ♦ Current volumes and operational statistics
- ♦ Service and technical requirements
- ♦ Transfer or sale of asset
- ♦ Staffing issues
- ♦ Performance measurement.

**B.2.4 Receive tender submissions.** Departments should ensure that tenderers have adequate time to prepare a quality submission. Where outsourcing contracts are large and commit the parties to a long-term relationship, a longer tender submission period is

*Openness, transparency and ethical dealing are the hallmarks of a good tender process*



better. The generally applied minimum in the civil service is 3 weeks, although up to 40 days is required for contracts covered by the World Trade Organization Agreement on Government Procurement.

The department should issue a receipt to tenderers when submissions are received. The closing date and time should be strictly adhered to and unsolicited revisions to submissions received after the closing date and time should not be accepted.

#### Task B.3 Actions

- 1 *Evaluate tender compliance*
- 2 *Evaluate tenders in detail*
- 3 *Financial vetting*
- 4 *View tenderer presentations and conduct site visits*
- 5 *Recommend service provider(s)*

### B.3 Evaluate tender responses

The evaluation of an outsourcing tender can be broken up into two broad categories:

- ♦ **Technical/operational.** The department evaluates the technical/operational aspects based on the criteria drawn up and issued with the tender. It also compares the tenderers' responses to the draft contract issued in the tender documentation to determine the viability of entering into an acceptable contract with the tenderer.
- ♦ **Financial.** The department compares the prices submitted with the current costs identified in the business case phase. The analysis should be kept separate from the technical/operational evaluation, to prevent bias based on price.

The ultimate aim of the evaluation process is to select the best service provider to manage and deliver the service. Value for money is important in selection. A system using the combined technical and financial scores may produce a higher score for a tender that is not offering the lowest price. Nonetheless, the contract should be awarded to the highest scoring tender. For this reason, the marking scheme chosen should accurately reflect the relative importance of price and quality in the selection criteria.

The evaluation process will also include financial vetting of the short-listed companies. The purpose is to confirm that the tenderer has sufficient resources to satisfy the department's needs and will provide the necessary insurance and indemnities that the department will require in order to enter into the contract.

**B.3.1 Evaluate tender compliance.** Prior to a detailed evaluation, the department may need to produce a shortlist of tenderers, eliminating the tenderers who are unable to satisfy the mandatory requirements and/or fully comply with the tender process. The department should make all reasonable efforts not to exclude viable service providers.

For example, when a section of the response has not been received and this may be an administrative oversight rather than an inability to provide the service, departments should make efforts to ensure that administrative and process errors are corrected. However, this should not be used to allow tenderers to change their tender.

In evaluating basic compliance the department may find itself left with a limited number of complying tenders. The department will need to make a decision whether it wishes to continue with the evaluation process or recommence the tender. A wider level of competition may provide the department with better choices in respect of quality and price and assist in minimising some of the risks. If the department wishes to recommence the tender process, it would be advisable to consult with the relevant tender board. The department needs to re-examine the tender documentation to see if there is something in the contract or specification that is reducing the possibility of complying bidders.

Generally, if none of the tenders is complying, departments should cancel the tender process and re-tender with revised specifications, terms and conditions, where applicable.



However, if a department decides to proceed with a non-conforming tender this is allowed for in the SPR and the tender report must clearly specify what deviations exist and the reasons for proceeding with the tender despite this.

**B.3.2 Evaluate tenders in detail.** Following the compliance evaluation, the department will evaluate the tenderers using the evaluation model set up prior to issuing the tender. If using the two-envelope process departments should evaluate the technical envelope first.

- ♦ **Operational/technical capability.** Rate the responses submitted against the predetermined criteria and, if using a marking scheme, provide a score for each.
- ♦ **Financial capability.** This covers the tender price of the tenderer. Only after completion of the technical evaluation should the financial envelopes be opened.

First, make an assessment of the relative prices of the tenderers. Input the prices submitted into the financial evaluation model and perform a comparison with the internal costs defined in the business case. Use of a financial evaluation model will help the department make an assessment about the reliability and relative value of pricing information that may be presented by tenderers in different ways.

During the evaluation process there may be cases where the evaluation team requires the clarification of information relating to a tender. If any member of the evaluation team identifies a need for clarification then that person should document this need, including the reasons and the potential effect on other tenderers. The member should then request the nominated evaluation team member to seek clarification.

The clarification notice must be forwarded to the tenderer in writing and must set a reasonable time frame for provision of an answer. The response should be in writing and within the specified time.

**B.3.3 Financial vetting.** Financial vetting is generally conducted on the short-listed tenderers. It occurs at this time as it is one of the last points in the formal evaluation process to confirm whether the tenderers are capable of fulfilling contract requirements. This is mandatory for any service contracts in excess of limits set in SPR.

Mandatory financial vetting must include:

- ♦ Audited accounts for the past 3 years
- ♦ Projected profit and loss statements for the period of the contract.

Departments should assure themselves about:

- ♦ Past and projected earnings performance
- ♦ Balance sheet strength
- ♦ Degree of tenderer's financial commitment to deliver the service according to the contract terms.

Other useful information that will assist in assessing a company's viability includes:

- ♦ Company structure and shareholdings
- ♦ Management details (quality assurance accreditation, insurance coverage, human resource capability)
- ♦ Past or present legal actions against the company
- ♦ Past performance on government tenders.

*Do not open financial envelope until technical evaluation has been completed*

*Copy correspondence to one tenderer to all other tenderers*

It is also advisable to perform reference checks on tenderers. This should be conducted by contacting each of the referees supplied and asking a set of questions determined by the evaluation team.

**B.3.4 View tenderer presentations and conduct site visits.** The evaluation team will benefit from having tenderers present their cases, introduce their management teams and clarify issues.

Site visits would also help the evaluation team assess intangible issues such as values and organisational compatibility between the department and the tenderers and meet the staff actually doing the work, in addition to the tenderers' senior management and sales teams.

**B.3.5 Recommend service provider.** Finally, all elements of the evaluation criteria are taken into account to determine a list of recommended tenderers in order of merit. If a marking scheme is being used the raw and weighted scores would be finalised at this point.

The preferred service provider should now be apparent and a report on the tendering process is prepared for the department's senior management and the relevant tender board that addresses the following:

- ♦ Recommended scope of services
- ♦ Market reaction to and interest in the scope
- ♦ Anticipated costs
- ♦ Cost/benefit and risk assessment
- ♦ Ranking of all short-listed tenderers
- ♦ A recommendation to negotiate the terms of the contract with a number of short-listed tenderers or a recommended tenderer.

The SPR provides a template for preparation of a recommendation to the relevant tender board.

## B.4 Conduct due diligence checks

A due diligence check goes to a greater depth than the viability study conducted during the tender evaluation. Both the department and the service provider need to thoroughly examine the viability of entering into a contractual relationship.

The due diligence will vary for each outsourcing contract. Put simply:

- ♦ The department is assuring itself that the potential service provider has the capacity and assets it claims to have
- ♦ The service provider is making sure it fully understands what is required and that it is capable of delivering it in the terms specified.

The department will need to conduct an audit on the service provider's premises, equipment and key personnel to check the reliability of a service provider's statements about its ability to meet the terms of the contract. This will involve examining the service provider's processes and conducting a skills analysis on its key staff members.

### Task B.4 Actions

- 1 *Conduct due diligence review of the service provider*
- 2 *Facilitate due diligence review by the service provider*

**B.4.1 Conduct due diligence review of the service provider.** In general, the department will:

- ♦ Confirm the credentials of the service provider and its key staff, including referee checks
- ♦ Confirm the financial position of the service provider
- ♦ Obtain any bank or corporate guarantees required under the contract
- ♦ View and record any required documentation, e.g. insurance policies
- ♦ Identify and resolve any intellectual property arrangements
- ♦ Review the physical or intellectual property assets promised by the service provider for the delivery of the service
- ♦ Conduct final review of the impact of ordinances/regulations, policies and administrative arrangements relating to the service
- ♦ Review the service provider's proposed approach to carrying out the procedures including any technical or operational documentation, if necessary
- ♦ Review the service provider's procedures on ethical business practice, and confirm the existence and quality of its company code of ethics and staff code of conduct

For example, the codes should cover acceptance of advantages and entertainment; declarations and avoidance of conflict of interest; and non-disclosure of confidential information.

- ♦ Review any taxation matters that may be applicable.

**B.4.2 Facilitate due diligence review by the service provider.** The service provider will probably wish to:

- ♦ Determine that the performance levels set by the department are realistic and achievable
- ♦ Perform an asset audit in cases where departmental assets are to be transferred to the service provider. This should include a statement of the condition of each asset and its location, developing an asset disposal strategy if required
- ♦ Confirm the credentials and identifying the department's key staff (in particular, contract management staff)
- ♦ Review the inventory of all existing contracts, leases and licences and ensure that all third parties have been advised of the new service arrangements by the department
- ♦ Clarify arrangements for operational interaction between the service provider and the department at a variety of levels, and with clients and other stakeholders as appropriate.

## B.5 Negotiate the contract

The department will need authorisation from the tender board to begin negotiations on the contract and finalise the contract provisions. The right of the department to negotiate will have been stated to the tenderers in the tender documentation (refer to the SPR).

A value for money outsourcing arrangement does not rest merely on price. Think about risk, innovation and flexibility - for both parties to the contract. Keep this in mind during contract negotiations.

**B.5.1 Set the negotiation framework.** The department needs to set terms for negotiations at this point. This is a framework around which the contract negotiations will be conducted, and will feature the following:

*The viability of outsourcing the service should be examined at all milestones during the process. It is particularly important at this point - before formal negotiations and any commitments to the service provider begin*

### Task B.5 Actions

- 1 Set the negotiation framework
- 2 Establish the negotiating team
- 3 Negotiate a value-for-money contract
- 4 Obtain clearance to finalise the contract

- ♦ **Agree the timetable for negotiations.** Set a time scale for completion of the negotiations.
- ♦ **Confirm that the contract will deliver the outsourcing objectives.** This needs to be done at this stage as it is one of the last opportunities to review the deal to ensure it will deliver the expected benefits.
- ♦ **Determine the most important negotiation points and a position on each.**
- ♦ **Prepare an agenda for the negotiations.**
- ♦ **Determine the key risks and the approach to be taken.** Prohibited negotiating behaviours are outlined in the SPR. They include technical transfusion, auction techniques and competitive disclosure (see glossary at Appendix 1).
- ♦ **Do not introduce new issues or revisit agreed matters.** The parties should not admit new issues into negotiations (i.e. issues not previously raised in bids nor signalled in setting up the negotiation framework). In addition the parties should agree not to reintroduce issues already agreed in the negotiations.
- ♦ **Recording of agreed matters.** Keep a record of all matters agreed during the negotiations so they may be recorded in contract drafts. Accordingly, this must be recorded in meeting notes and agreed at the end of each meeting.
- ♦ **Ensure that all ordinances and regulatory constraints are reflected in the final contract.** As the department drafts the tender documents, all amendments will be managed by it.
- ♦ **Version control of altered documents.** The altered versions must be issued sequentially and in compliance with any departmental document naming conventions.
- ♦ **Agree dispute escalation and resolution process.** In case negotiations reach an impasse, there should be an agreed process for overcoming this. This typically will involve escalating matters to more senior management for resolution. Accordingly, the parties need to ensure that appropriate senior managers will be available throughout the course of the negotiations.

**B.5.2 Establish the negotiating team.** The composition of the negotiating team may differ from the evaluation team as different areas of specialist knowledge are required. For example, legal advisers might be essential for this part of the process. The team should involve key stakeholders from the department who are decision-makers able to legally bind the department (at the Directorate level). Most importantly the negotiations should be led by an experienced negotiator. For tenders administered by the Government Logistics Department (GLD) on behalf of another department, normally the GLD will lead the negotiating team.

Both negotiating teams should comprise members with the authority to decide on behalf of their organisations and to commit their organisations to the terms and conditions agreed. The department's negotiating team will need to seek direction from the relevant tender board on the limits within which the negotiations and commitments can be made. Depending upon these, the negotiations may be on a "without prejudice" basis and subject to the ratification of the relevant tender board.

**B.5.3 Negotiate a value for money contract.** It is important to bear in mind throughout the contract negotiations that the ultimate outcome is to set the terms and parameters for a strategic partnership rather than simply the procurement of a service. The finished contract will be the foundation of this relationship and should reflect that.

The best value for money will be achieved by setting common objectives, sharing risk, encouraging innovation and maintaining flexibility. In such a contract, the terms and conditions will not be heavily biased in favour of the department.

For example, many companies work on a shorter payment period than departments. Reaching a mutually acceptable time period between invoicing and payment could solve short-term cash flow problems for the service provider and earn the department a discount.

Price should not be the only influence. Factors such as agreed arrangements for responsibility and management of the contract are important as these dictate how the relationship will work.

For example, a fair dispute resolution process will encourage the parties away from litigation when there is a dispute. The appointment of a mutually acceptable mediator to work with the parties to achieve resolution on issues of dispute will be less expensive than recourse to legal action, and will do more to preserving the relationship and the continuous delivery of the services. This is important as disengagement from the relationship will be expensive and may involve a disruption to service continuity.

The result of the contract negotiations should be a final version of the contract. This will be drafted to reflect everything that the parties have agreed. Both parties should have sufficient time to review the final copy and obtain the necessary internal approvals to formalise the contract. It is not always possible to ensure every detail is finalised prior to finalising the contract. Unresolved matters should be kept to a minimum.

For example, the details of the reporting can be finalised after the contract is signed. In general, issues that are unlikely to cause a breakdown in the relationship between the parties can be resolved after the contract is signed.

In addition, the contract may be conditional on a number of matters being successfully resolved.

For example, the contract may be conditional on the successful transition into the new service. Accordingly, if the service is not successfully transitioned across to the service provider then the department would have the right to terminate the contract.

**B.5.4 Obtain clearance to finalise the contract.** The department will need to obtain the relevant tender board's approval for the final negotiated contract. It should develop a final submission summarising the reasons for recommending the service provider, assessing the degree of risk in entering into this arrangement and confirming that the contract represents value for money. The SPR provides a standard tender report format for departments to use.

The contract should be signed by a department officer with the appropriate level of expenditure discretion, as per the SPR. After the contract is signed, the unsuccessful tenderers must be formally notified in writing. Requested debriefings should be given.

## Chapter 4 Phase C: Managing the Contract

The outsourcing contract is signed and the department and the service provider make the transition to the outsourced arrangements. This phase also covers arrangements for service-level monitoring throughout the contract and the decision, towards the end of the contract, whether to extend or renew the outsourcing arrangement. The department needs to manage the relationship with the service provider at a senior management level. Good outsourcing results depend upon good contract management.

Tasks / Actions	Focus / Responsibility / Deliverable
<b>C.1 Prepare for the transition and handover</b> <ol style="list-style-type: none"> <li>1 Finalise the implementation plan</li> <li>2 Move staff to new arrangements</li> <li>3 Transfer assets and third party contracts</li> </ol>	<b>Senior management focus</b> Approve and monitor transition arrangements <b>Responsibility</b> <ul style="list-style-type: none"> <li>♦ Service provider submits plan</li> <li>♦ Project team and contract manager</li> </ul> <b>Deliverable</b> Outsourcing arrangement ready to start. Staff and assets moved to new arrangement where relevant
<b>C.2 Monitor service delivery and manage the relationship</b> <ol style="list-style-type: none"> <li>1 Monitor service delivery</li> <li>2 Conduct quality assurance reviews</li> <li>3 Review the performance of service levels</li> <li>4 Enforce performance against service levels</li> </ol>	<b>Senior management focus</b> Determine if service provider's performance is satisfactory and in accordance with agreed service levels <b>Responsibility</b> <ul style="list-style-type: none"> <li>♦ Senior management from service provider</li> <li>♦ Senior management from department, supported by operational team and contract management team</li> </ul> <b>Deliverable</b> Processes in place to monitor and evaluate contract performance
<b>C.3 Administer the contract</b>	<b>Senior management focus</b> Determine if contract is carried out in accordance with agreed terms and conditions <b>Responsibility</b> <ul style="list-style-type: none"> <li>♦ Service provider's operational team</li> <li>♦ Department contract management team</li> </ul> <b>Deliverable</b> Regulatory processes are implemented in accordance with policy/legal requirements

Tasks / Actions	Focus / Responsibility / Deliverable
C.4 Monitor the savings achieved	<p><b>Senior management focus</b> Determine if projected savings are delivered as scheduled and any remedial actions are required</p> <p><b>Responsibility</b> Department contract management team</p> <p><b>Deliverable</b> Documentation of the savings forecast and realised, with reasons for any deviation</p>
C.5 Conduct review and renewal process	<p><b>Senior management focus</b> Determine if a business case exists to proceed with recommendation for contract renewal</p> <p><b>Responsibility</b> Senior management, supported by the operational and contract management teams</p> <p><b>Deliverable</b> Recommendation to senior management whether contract should be renewed, re-negotiated, re-tendered or brought back “in-house”</p>

## C.1 Prepare for the transition and handover

In the transition stage, the contract is subject to a number of criteria being fulfilled. These will include confirming transition plans, confirming financial arrangements and establishment of securities or bonds. Arrangements for monitoring and administering the contract will be set up at this point. Appendix 5 provides more information on achieving the transition.

**C.1.1 Finalise the implementation plan.** This stage covers the transition to the selected service provider. Timetables, responsibilities and deadlines for the implementation and transition should be finalised.

Broadly, the implementation plan covers transition for staff if any, establishing mechanisms to monitor service delivery, transfer of assets where applicable, and phase-in of the new service provider. The implementation plan will also cover the management of the risks that will be faced at the point of service commencement by the new service provider. A contingency plan needs to be in place in the event of any service failure during handover.

The formal handover may take some time to phase in after the contract is signed and implementation begins. This might be the case where the outsourced service:

- ♦ Is to be provided over a wide geographical area
- ♦ Is complex
- ♦ Requires a large amount of information to be exchanged.

### Task C.1 Actions

- 1 *Finalise the implementation plan*
- 2 *Move staff to new arrangements*
- 3 *Transfer assets and third party contracts*



After completion of the implementation plan, an independent review of the transition and implementation may be conducted. This would be particularly helpful if the department plans to outsource other functions.

Finalising the ongoing staffing and structure of contract management generally occurs during the transition process. At this point the department should have determined who will be responsible for the contract management at a senior level and the size and form of the team that will support this role. Appendix 11 provides further information on the key roles required in contract management.

There is no formula for deriving the number of staff required to support contract management. International comparisons indicate that best practice in contract management resourcing averages at approximately 3% of the contract price. This is not a hard and fast rule. Contract management arrangements (and costs) will depend on the size and complexity of the contract(s) to be managed and whether the department manages all contracts through a centralised contract management unit or by individually designated staff on a contract-by-contract basis.

**C.1.2 Move staff to new arrangements.** Resolving issues relating to existing staff affected by the outsourcing or any new staff required to manage the outsourcing is an important part of the broader transition to the outsourcing arrangements.

Planning for this activity will have commenced during the business case phase. Human resources issues may now take priority as the manner in which redeployment and transition of staff are handled can affect the morale of the entire organisation.

Issues of staff transition include the following:

- ♦ Planning to phase down departmental staff input into the service to be outsourced
- ♦ Finalisation of organisational arrangements for, and staffing of, any functions retained by the department or associated with outsourcing the service
- ♦ Establishment of the ongoing contract management function that is to be adopted (including any recruitment of specialist skills)
- ♦ Staff redeployment, secondment, and training.

**C.1.3 Transfer assets and third party contracts.** Any requirement for the transfer of assets and/or third party contracts as part of outsourcing should have been thoroughly considered during the development of the business case and subsequent preparation of the tender documentation to take the outsourcing to the market.

The final transition plan for this stage may include:

- ♦ Definition of each party's responsibilities
- ♦ Change management strategy
- ♦ Management of assets (disposal or transfer)
- ♦ Expiry, termination and assignment of third party contracts
- ♦ Preparation of notification of handover
- ♦ Implementation of approval processes.



## C.2 Monitor service delivery and manage the relationship

Management of the relationship between the parties affected by the outsourcing contract is crucial. Departments should resource this appropriately to ensure success.

The three key parties to any outsourcing are:

- ♦ **Department.** Its primary responsibility is to monitor whether the service provider delivers the outputs and outcomes in accordance with the contract. The department does not become involved in the daily operational issues unless the delivery of the service is threatened. The department also manages the expectations of users and collects their feedback on how the services are performed.
- ♦ **Service provider.** Its primary responsibility is to fulfil its legal obligations by delivering the service to the users in accordance with the contract. As a secondary responsibility, the service provider must report to the department on its service delivery. This reporting aids both parties in continually re-examining the success and viability of the outsourcing relationship.
- ♦ **Users.** If the users of the service are department staff, their responsibility is to use the service so that it generates value for the department. As a secondary responsibility, they should provide feedback and communicate issues to both the service provider and the department's contract managers. Where the users are members of the public or the business community the department should establish mechanisms for seeking user feedback on the service delivery.

All three parties should manage their responsibilities following best practice principles for the outsourcing contract to be successful. These include:

- ♦ **Promoting the change.** The service provider and the department must work together to communicate the nature of the change and the services available to government staff and/or the community.

For example, the department needs to communicate the agreed service level standards to the users so that they understand the limits of the department's relationship with the service provider and what they as users can expect.

- ♦ **Managing expectations.** Both the service provider and the department must manage expectations. This principle also applies to the relationship between the department and the service provider. The department must explain to the service provider how the department works and how to work effectively within its environment.

For example, the service provider should know the likely turnaround time to obtain approval from senior management of the department so that it may manage its own supply chain and resources effectively.

If the department manages the service provider's expectations the relationship between the parties will be preserved and the service provider will be able to manage the supply of the service more effectively.

- ♦ **Knowing the business.** The service provider must know the department's business and future strategy for the outsourced service. It must understand exactly what the department wants and needs.
- ♦ **Communicating user needs.** The users and the department must let the service provider know - formally or informally - their needs and any issues that come up.

### Task C.2 Actions

- 1 *Monitor service delivery*
- 2 *Conduct quality assurance reviews*
- 3 *Review the performance of service levels*
- 4 *Enforce performance against service levels*

- ♦ **Keeping to defined roles.** The department should not be involved in the day-to-day delivery of the service. Under an outsourcing contract, its role is to manage the service delivery relationship, not the services themselves. It should become involved only when service standards are not achieved or are threatened.

Correspondingly, the service provider should act within the scope of its service specifications. Any change in the scope of its role must be through formally managed contract variations. Otherwise, the service provider may find itself performing tasks outside its scope for no recompense, which may adversely affect its ability to deliver the services originally contracted. Formal contract variation is required even for those instances where the parties agree informally to substitute different activities for the same contract price. Remember, many outsourcing contracts are long term and contractor or departmental staff who make informal agreements may not be there for the life of the contract.

- ♦ **Achieving and maintaining a partnership.** The parties continuously need to work together to achieve both commercial reality and public accountability.

For example, for the arrangement to be viable, the department needs be sure that the service will be provided transparently and ethically, while recognising that the service provider has to retain a commercial focus and operate profitably.

- ♦ **Processing of payments must be accurate, timely and auditable.** The service provider must produce accurate reporting that meets the department's needs. All invoices must be accurate, clear and auditable. The department should budget accordingly, and audit and process invoices promptly. If this practice is not followed, both parties will spend time correcting matters, thus souring the relationship.
- ♦ **Innovating and improving.** The parties should work together to innovate and continuously improve the service quality, and to find more effective ways to satisfy user needs.
- ♦ **Good faith.** Both parties need to enforce the contracted terms of the relationship diplomatically. The outsourcing contract requires considerable commitment in resources and time to work effectively. The parties need to keep in mind that a possible disengagement from a contract is costly and may involve damaging publicity.

**C.2.1 Monitor service delivery.** Monitoring service delivery is vital to successful contract management. The department will use this data to determine whether to grant contracted rewards to the service provider for exceeding service levels or to take remedial actions for under-performance.

The information will also help the department decide its future actions when the contract finishes.

There should also be a mechanism to monitor complaints and feedback from the users and the public. This should be built into the formal reporting requirement by the service provider. The department may also institute separate arrangements to check user satisfaction.

User satisfaction may be one of the key measures for determining performance in the delivery of the contract. If it is part of the formal reporting measures in the SLA, a sound methodology must be agreed before the contract is finalised. This may range from simple measures such as the number of complaints registered or a more formal survey administered to a statistically valid sample of users. If user satisfaction is not a required performance measure the department may use less formal measures to get user feedback. Whatever method is used, a baseline level of user satisfaction prior to the transfer of the service should be established to provide valid comparisons.

*Successful outsourcing requires rigorous contract monitoring. Make sure this is in place at the point of transition*

During the transition period the department should test the arrangements it has put in place for monitoring service delivery. Some issues to be considered at this time include:

- ♦ The form and detail of reports
- ♦ The frequency of reporting
- ♦ Ensuring the department receives the right information to exercise its ongoing accountability for the service.

Reporting frequency for contract monitoring purposes varies. A service with high transactions, e.g. an e-procurement portal, may require weekly reports while one with low transactions, e.g. property management outsourcing, may only require monthly reports.

Reporting frequency may also vary with the stage of the outsourcing relationship. During the transition and implementation stages, daily or weekly reports are advisable. Once the implementation phase is completed, the department should not need to monitor the progress as closely.

The department must analyse the service level compliance reports provided by the service provider against the agreed service levels in the contract. This must be done with every report submitted. Every non-performance issue should be recorded, reported appropriately and resolved quickly.

In addition, opportunities for improvement to the performance of the contract should be recorded and presented for discussion between the service provider and the department during review meetings for monitoring contract performance or during less formal contacts between the project staff and the department.

**C.2.2 Conduct quality assurance reviews.** Regular quality assurance reviews should be conducted on the service provider. The purpose is to satisfy the department that the results reported by the service provider are genuine and can be relied upon. It is an independent check in the performance monitoring process and should tie into any performance reporting.

In addition, the department should confirm that any statutory requirements are being satisfied.

The review, generally conducted by internal audit staff and key internal customers, may be held every six months, with a formal report issued prior to a review meeting with the service provider. The frequency of the review will depend on the size of the contract, the risks of non-compliance, the track record of the service provider and the development of the working relationship between the department and the service provider.

**C.2.3 Review the performance of service levels.** The department should conduct formal and regular review meetings at a senior level. These may be held as regularly as necessary. Quarterly or half yearly is often the case. Review meetings should:

- ♦ Review the strategy and plans
- ♦ Assess actual performance against agreed service levels and against the final cost/benefit analysis
- ♦ Conduct benchmark reviews against other similar arrangements, using actual performance data

*In reviewing performance, create an open communication channel, where both parties act in partnership to achieve continuous improvement objectives and address areas of concern*

- ◆ Endorse negotiations for any contract variations
- ◆ Approve budget projections.

In addition to this senior level review, a team at the operational level will need to monitor the contract more closely. The frequency and agenda of their review meetings will change throughout the life of the contract. This may be several times a week throughout the transition and initial operational stages. Afterwards, it may meet weekly, fortnightly or monthly to address issues as they arise. The review meetings should look for improvement opportunities and identify any additional or unnecessary requirements.

**C.2.4 Enforce performance against service levels.** If the service is not delivered in accordance with agreed service levels, the immediate step will be to resolve the issues directly with the service provider.

As a general rule, if the department is unhappy with the performance of the service provider it is important that it raises this as early as possible. Both parties to the contract should work together to raise the service to the expected level or to resolve any misunderstanding or over-expectation. If a service problem exists, it is common for an agreed action plan addressing the problems to be prepared and for the service provider to commit to measurable improvements within a specified period of time.

The department may refer to measures set out in the contract for non-delivery of service, such as withholding incentives or issue of default notices. Unsettled disputes may be resolved through arbitration, if this has been provided for in the contract.

As a last resort, the parties may need to consider disengaging from the outsourcing relationship. It will take much time and expense to disengage from the contract. Therefore, in deciding what actions to take, the department must consider their effect on the relationship between the parties. Outside advisers can be very valuable as independent mediators. A commonly used dispute escalation process is attached as Appendix 9.

### C.3 Administer the contract

In carrying out the contract administration function, the department is responsible for documenting any contract variations and for re-issuing the altered contract to relevant stakeholders. This process must be consistent with the existing requirements of the SPR.

In addition, the department will need to ensure that regulatory obligations are satisfied, such as audit and access, privacy, and other Hong Kong regulatory considerations.

Lastly, the department must ensure that the payment of contract fees is processed smoothly, and that payments are made for services delivered.

### C.4 Monitor the savings achieved

To ensure that the outsourcing arrangement does provide value for money, the department needs to monitor closely the savings achieved against the projected savings. A template for the review of benefits from outsourcing is provided at Appendix 12 and departments are advised to take the following actions:

- ◆ Document the estimated savings based on the cost and benefit analysis conducted when developing the business case for outsourcing

#### *Contract enforcement may follow four levels of escalation:*

- ◆ *Discuss at project/contract manager level*
- ◆ *Escalate to department head and service provider CEO*
- ◆ *Refer to agreed external arbitration process*
- ◆ *Terminate the contract*
- ◆ *Track and communicate variations in the contract*
- ◆ *Pay on time*
- ◆ *Match payments to performance*
- ◆ *Document the benefits achieved against the estimated savings*
- ◆ *Explain if deviation exists*
- ◆ *Take remedial measures*

- ♦ Classify the savings between recurrent and one-off, and between realisable and notional. Detailed breakdowns will vary from case to case
- ♦ Update the estimated savings when the contract prices and other terms are finalised
- ♦ Record in the template the actual savings achieved in different phases/years of the outsourcing contract, say every six months throughout the contract period depending on the contract length and the time schedule for realisation of the benefits and after the termination/renewal of contract
- ♦ Record reasons for any deviation from the estimated savings
- ♦ Explore remedial measures to achieve the targeted savings.

Apart from tangible benefits, the realisation of intangible benefits such as the extent of improved quality and provision of additional value-added services should also be monitored and documented.

Proper documentation of the savings forecast/realised is important as it provides essential information on the success or otherwise of the exercise, and will help management to make informed decisions on future exercises. It also provides ready information for departments to answer enquiries.

### C.5 Conduct review and renewal process

This part of the process has considerable overlap with the business case phase as it involves re-examining the viability and cost/benefit of the outsourcing arrangement. The format and approach of the return-to-market when an outsourcing contract finishes will depend on the results of this strategic review.

Issues to examine when reviewing the success of outsourcing include:

- ♦ Has value for money been achieved?
- ♦ Has outsourcing delivered the anticipated benefits?
- ♦ Has the department's strategy for service delivery changed?
- ♦ Have there been any changes in government policy or law which may require a change in service scope for the next contract?
- ♦ If the outsourcing arrangement is to be continued, do any alterations need to be made?
- ♦ Could this arrangement be bundled with other existing or new outsourcing activities or rolled out to other service areas?
- ♦ Can the scope of the requirements be altered (perhaps to get better value for money, better quality services, or cover more services)?

The outcome of a thorough review should be an estimate of the costs, benefits and risks of each option identified and a recommendation of the best option for the department to take.

Once this decision has been made, the department will need to prepare and present a business case with a recommendation. If the decision is made to proceed with another outsourcing contract, then the process returns to the tendering and selection phase of the outsourcing cycle.

*Now is the time to reflect on the outsourcing experience*

- ♦ *How can the outsourcing be improved?*
- ♦ *Do you wish to continue?*

## Chapter 5 Support Processes and Assistance

The support processes that extend across the three phases of an outsourcing project ensure that the business process is defensible and that the resulting contract is an ongoing success. It addresses planning and control; managing people; and managing quality as well as available assistance.

Tasks / Actions	Focus / Responsibility / Deliverable
<b>5.1 Planning and control</b> <ol style="list-style-type: none"> <li>1 Establish a project team</li> <li>2 Establish financial management</li> </ol>	<b>Senior management focus</b> <ul style="list-style-type: none"> <li>♦ Appoint project manager</li> <li>♦ Approve financial model</li> </ul> <b>Responsibility</b> Project manager <b>Deliverable</b> <ul style="list-style-type: none"> <li>♦ Project team established</li> <li>♦ Financial management strategy established</li> </ul>
<b>5.2 Managing people</b> <ol style="list-style-type: none"> <li>1 Manage organisational change</li> <li>2 Manage department staff</li> </ol>	<b>Senior management focus</b> <ul style="list-style-type: none"> <li>♦ Maintain project sponsorship</li> <li>♦ Communicate regularly</li> </ul> <b>Responsibility</b> <ul style="list-style-type: none"> <li>♦ Project manager</li> <li>♦ HR manager</li> </ul> <b>Deliverable</b> <ul style="list-style-type: none"> <li>♦ Organisational change managed</li> <li>♦ Department staff managed effectively</li> </ul>
<b>5.3 Managing quality</b> <ol style="list-style-type: none"> <li>1 Establish risk management</li> <li>2 Establish change control and issue management</li> </ol>	<b>Senior management focus</b> <ul style="list-style-type: none"> <li>♦ Approve risk management plan</li> <li>♦ Approve transition plan</li> </ul> <b>Responsibility</b> <ul style="list-style-type: none"> <li>♦ Project manager in conjunction with service area</li> </ul> <b>Deliverable</b> <ul style="list-style-type: none"> <li>♦ Risks managed</li> <li>♦ Strategy and procedures for change control and issue management prepared</li> </ul>
<b>5.4 Assistance available</b> <ol style="list-style-type: none"> <li>1 The EU's role in government outsourcing</li> <li>2 The EU Help Desk</li> <li>3 Other private sector involvement options</li> </ol>	



## 5.1 Planning and control

### 5.1.1 Establish a project team

A project team should be appointed to support the different stages of the outsourcing project. This should cover the following skills:

- ♦ Business
- ♦ Technical/Operational
- ♦ Change Management
- ♦ Legal
- ♦ Financial

Not all of these skills will be required at every stage of the process. Depending on the size of the project, many of the roles may be assumed by one person or several. Appendix 11 looks at the composition and roles of an outsourcing project team.

Some members of the department's outsourcing project team may not work directly for the department. Consultants, for example, may provide:

- ♦ Support services, such as facilitation of business case processes and the development of service levels
- ♦ Specialised knowledge or expertise, e.g. a financial analyst may be used to produce a financial model for the performance of the services.

Special project management focus will be required to minimise the risks associated with reliance on an "outside party" for performance of key project-related tasks. The department must assure itself that appropriate knowledge transfer takes place and that it is able to manage after the departure of the consultant.

### 5.1.2 Establish financial management

This involves ensuring that the outsourcing project reflects the overall financial strategy of the department and that it continues to do so throughout the life of the project. This is achieved by regularly reporting to senior management on the progress, scope and cost of the project.

## 5.2 Managing people

### 5.2.1 Manage organisational change

Staff generally experience or anticipate sudden and dramatic changes in their work environment when their departments implement outsourcing projects. As a result staff may resist strongly. Understanding the level of change a project will cause is the key factor in determining the level of emphasis to place on human and organisational factors before and during implementation.

Successful implementation of the changes associated with outsourcing projects requires careful planning, teamwork, commitment, and structure.

#### *Task 5.1 Actions*

- 1 Establish a project team*
- 2 Establish financial management*

#### *Task 5.2 Actions*

- 1 Manage organisational change*
- 2 Manage department staff*

Strong project sponsorship is essential. While a project should have one sponsor who initiates and effectively owns the project, there may also be several secondary (or sustaining) sponsors, each filling a different role in the change management process. The project manager must understand the criteria for effective sponsorship and must actively cultivate such sponsorship for the project.

For example, a procurement outsourcing project may have the Assistant Director (Finance) as a major sponsor. Other sponsors may be key users of the service and other parties with a vested interest. Branches that require the services of the procurement unit on a regular basis will be important interests to manage.

### 5.2.2 Manage department staff

Human resources issues should be given priority throughout the project. Much of the success of the transition and implementation will depend on the willing participation of staff affected by the outsourcing of a service.

The following issues should be considered:

- ♦ Communication strategy
- ♦ Consideration and finalisation of future postings
- ♦ Staff briefings
- ♦ Staff consultation/advice on transfer and selection issues
- ♦ Provident fund requirements
- ♦ Surplus staff management
- ♦ Handling resignations, redeployments, secondments and transfers to the service provider.

## 5.3 Managing quality

Quality management is continuous throughout the life of the project. The approach is defined and the procedures are put in place as part of the planning process. Quality in any project is achieved when all deliverables are produced:

- ♦ According to specifications and standards
- ♦ Meeting users' needs and expectations
- ♦ On time
- ♦ Within budget
- ♦ In a manner that is perceived by the department as successful.

### 5.3.1 Establish risk management

The objective of a risk management process is to minimise the impact of unplanned incidents on the project and on the department by identifying and addressing potential risks before negative consequences occur.

After potential risks are identified, the exposure is determined in terms of time and cost. Risk management is therefore concerned not only with identifying risks, but also with reducing risks to an acceptable level.

#### Task 5.3 Actions

- 1 *Establish risk management*
- 2 *Establish change control and issue management*



Potential project-level risks should be identified during the initial planning effort and updated during the different phases of outsourcing. An ongoing risk management process should then be carried out formally as part of the detailed work planning process. The risks identified must be monitored conscientiously and acted upon speedily. A process for risk management is discussed in Appendix 4.

### 5.3.2 Establish change control and issue management

All outsourcing projects are subject to change throughout the outsourcing life cycle. Insufficient recognition of changes and/or ineffective management of changes are among the most common reasons for project failure.

Structured and comprehensive procedures for managing both changes and issues reduce project risks and are therefore essential components of any project management. Changes to a signed-off or important output required from the project should go through a structured change control process.

The primary objective of change control and issue resolution is to establish a standard method to document, analyse, approve, and communicate changes and issue resolutions.

## 5.4 Assistance available

### 5.4.1 EU's role in government outsourcing

As described in section 1.1 of this Guide, outsourcing is one of many forms of private sector involvement being encouraged within the civil service. The EU has an important role in developing this programme.

The EU offers departments a wide range of services and know-how. It can conduct:

- ♦ Cross-departmental project studies
- ♦ Feasibility and business case studies
- ♦ Re-engineering/performance improvement services to facilitate outsourcing decisions
- ♦ Project planning, scoping studies, and implementation planning
- ♦ Tender evaluation criteria development
- ♦ Due diligence checks
- ♦ Establishment of contract administration and relationship management regimes
- ♦ Training courses, seminars, experience sharing sessions, brain storming sessions, etc
- ♦ Help desk services.

Examples of EU assistance include:

- ♦ Development of service level agreements, tender documentation, and a performance monitoring system for Radio Television Hong Kong to outsource the maintenance of electrical and mechanical equipment and installations
- ♦ Development of a business case including a market testing for Rating and Valuation Department to outsource the valuation of 10 000 New Territories village houses in order to clear a backlog
- ♦ Development of a business case for the Agriculture, Fisheries and Conservation Department to outsource the operation and management of a Wetland Park.

### *Assistance available*

- 1** *EU's role in government outsourcing*
- 2** *The EU Help Desk*
- 3** *Other private sector involvement options*

*“To promote these endeavours we will set up a help desk to assist departments in undertaking outsourcing.”*

*Donald Tsang,  
2000-01 budget speech*

#### 5.4.2 The EU Help Desk

The EU is ready to assist departments to implement new outsourcing arrangements or to improve the effectiveness of existing ones. The objectives of the Help Desk are to:

- ♦ Alleviate the difficulties of both departments undertaking outsourcing projects and staff involved in the management of outsourcing contracts
- ♦ Achieve better contracting outcomes through the application of appropriate methodologies and processes
- ♦ Help departments through the spread of good outsourcing practices; reducing project time lines and cost as departments draw on precedents and better information.

The EU Help Desk will:

- ♦ Answer ad hoc queries about the outsourcing processes through a telephone hotline and an e-mail address
- ♦ Forward requests for more in-depth assistance to the appropriate EU officer
- ♦ Update supplementary information onto the EU website and the PSR Information Centre at the CCGO website
- ♦ Maintain a list of external outsourcing consultancy firms and service providers of common services
- ♦ Document examples of best practice, success cases and lessons learnt from local and overseas outsourcing arrangements
- ♦ Maintain a knowledge base on outsourcing related information, e.g. sample contracts and training materials.

Departments are welcome to visit the EU website (<http://www.info.gov.hk/eu/>) and the PSR Information Centre in CCGO (<http://host1.ccgohksarg/cso/eu/psric/>) to access information on outsourcing and contact the EU Help Desk on **2165 7255** or at [helpdesk@eu.gov.hk](mailto:helpdesk@eu.gov.hk) for further details.

#### 5.4.3 Other private sector involvement options

Apart from outsourcing, there are other forms of private sector involvement which may better provide the solutions to the challenges faced by departments. The EU is able to advise departments on the common options, and their advantages and disadvantages. The EU has recently issued *“An Introductory Guide to Public Private Partnerships (PPP)”* to provide a quick reference for departments to better understand this innovative arrangement with the private sector. A copy of the PPP Guide is available on the EU website and the PSR Information Centre in the CCGO.

Departments wishing to explore other private sector involvement options are invited to contact the EU Help Desk on **2165 7255** or [helpdesk@eu.gov.hk](mailto:helpdesk@eu.gov.hk).



## APPENDICES

Appendix 1	Abbreviations and Glossary of Terms
Appendix 2	Examples of Service Level Agreement Terms
Appendix 3	Business Case Template
Appendix 4	Risk Management
Appendix 5	Transition Planning
Appendix 6	Regulations/Circulars/Guides Related to Tendering
Appendix 7	Guidelines for Service Level Specifications
Appendix 8	Issues for Drafting a Contract
Appendix 9	Dispute Resolution
Appendix 10	Tender Evaluation
Appendix 11	Project Team Roles
Appendix 12	Outsourcing Benefit Analysis Template

## Appendix 1      Abbreviations and Glossary of Terms

### Abbreviations

CCGO	Central Cyber Government Office
EOI	Expression of Interest
EU	Efficiency Unit
GLD	Government Logistics Department
HR	Human resources
IT	Information technology
ITT	Invitation to Tender
PSI	Private Sector Involvement
PSR	Public Sector Reform
SAR	Special Administrative Region
SLA	Service level agreement
SPR	Stores and Procurement Regulations

### Glossary of Terms

<b>Auction techniques (Note: prohibited by SPR)</b>	<p>These are techniques designed to pressurise a tenderer into moving a price up or down and include:</p> <ul style="list-style-type: none"> <li>♦ Indicating to a tenderer the price it must meet to stay in the running</li> <li>♦ Conditional treatment based on linking other procurements outside those covered by the tender under consideration</li> <li>♦ Advising of price relative to other tenderers (although indication that a price is too high or unrealistic is allowed)</li> <li>♦ Furnishing information about the prices of other tenderers.</li> </ul>
<b>Benchmark costs</b>	<p>These are the full internal costs the department is expected to pay over the term of the contract for delivery of the services. They are established and used during the business case phase to determine whether outsourcing is financially viable for the department. The structure of the benchmark costs is also used to form the basis of the financial model that is issued with the tender. Lastly, the benchmark costs will be used as a comparison with prices submitted by the tenderers to determine whether outsourcing is still a competitive option from a cost perspective.</p>
<b>Competitive disclosure (Note: prohibited by SPR)</b>	<p>This is when the negotiator/contracting department discloses information to one tenderer that supplements the ITT and is not revealed to all other tenderers at the same time.</p>

<b>Conditions of tender document</b>	This document specifies the rules of the tender process. It will typically contain obligations on both parties. It covers issues from when and how the tender will be submitted to confidentiality provisions.
<b>Contract management</b>	The management of the outsourcing contract on behalf of the department. It may be performed by a specialised contract management unit in the department or by the area of the department that has outsourced the service. Its primary functions are monitoring and enforcing service levels and managing the overall relationship between the service provider and the department.
<b>Contracting out</b>	See outsourcing.
<b>Disaster recovery</b>	The processes put in place by a department to ensure that the services will continue uninterrupted in the event of an event occurring which disrupts or threatens to disrupt the performance of the service. For example, in the case of a mission critical computer system, maintaining backup systems offsite.
<b>Due diligence check</b>	A detailed investigation which may be conducted by one or both parties to an outsourcing tender. In a due diligence check, both parties thoroughly examine the viability of entering into the outsourcing relationship. There is no legal definition of due diligence. However, it is generally understood to mean the extent to which a prudent person would carry out investigations on behalf of the party they represent in determining whether a contract they intend to enter into is sound and that all reasonable checks have been carried out to verify information provided by the other party.
<b>Evaluation criteria</b>	The criteria used to evaluate service provider responses to an EOI or ITT.
<b>Expression of Interest (EOI)</b>	A document that the department will issue requesting information from prospective tenderers on the services they can provide and/or on the solutions available for satisfying the requirement. It is often used as a first step in the tendering process. An advertisement in the newspaper or an internet medium are good ways of issuing this. It is typically used in situations where the requirement cannot be adequately defined through lack of information on available solutions or when the market of service providers is not known.
<b>Force majeure event</b>	An event which disrupts the performance of one or both of the parties' obligations under the contract and which could not reasonably have been avoided by the parties. Examples of this include typhoons, floods, fires and unavoidable industrial action.
<b>Invitation to Tender (ITT)</b>	A document that the department will issue to tenderers. The document will request that the tenderers reply to a precisely defined requirement in a prescribed format. It is typically comprised of a statement of requirements, a conditions of tender document, a draft contract and a format for the tender response.
<b>Outsourcing</b>	An arrangement where a government department contracts with an external service provider for a continuous period for the provision of services specified and paid for by the department.

<b>Probity audit</b>	The overview of the outsourcing process to ensure that it follows relevant procedures/regulations, is equitable and that the proper outcome is reached. This is particularly important for the civil service as public scrutiny of the expenditure of public funds used for outsourcing purposes is likely to be high.
<b>Relationship management</b>	The management of the outsourcing contract relationship between the service provider and the department.
<b>Residual organisation</b>	The part of the department charged with managing the outsourcing contract. This organisation's primary functions are monitoring and enforcing service levels and managing the overall relationship between the service provider and the department. It may be a unit established solely for this purpose or it may be carried out by the part of the department from which the service has been outsourced.
<b>Service continuity</b>	The performance of the service in accordance with its defined service levels. The performance of the service must continue throughout the outsourcing process and beyond the transition and implementation phases regardless of the circumstances.
<b>Service levels</b>	Service levels are the standards of service with which the service provider must comply. They must be clear and measurable.
<b>Service level agreement (SLA)</b>	Defines a service or set of services that a service provider will supply to departments and the standard to which these will be delivered, how they will be measured, who will measure them, who will report on them and how frequently they will be reported upon.
<b>Service provider</b>	The organisation that will be providing the outsourced services to the department.
<b>Statement of requirements</b>	The documented scope of the service that the department requires from the outsourcing arrangement.
<b>Technical transfusion (Note: prohibited by SPR)</b>	The disclosure of technical information or intellectual property relating to a proposal that results in improvement of a competing proposal.

## Appendix 2 Examples of Service Level Agreement Terms

Outsourced Services Service Levels	Telephone Enquiry Services	Web Services to Public
Point of delivery	Call Centre 2888 1234	Public domain of the Web
Availability (how accessible the service is to a user)	<ul style="list-style-type: none"> <li>Monday to Friday 9:00 to 17:00</li> <li>Saturday 9:00 to 12:00</li> <li>99% of the time</li> </ul>	<ul style="list-style-type: none"> <li>24 hours per day</li> <li>7 days per week</li> <li>99.5% of the time</li> </ul>
Reliability (accuracy/failure of the service)	Accuracy of response > 99.5%	Maximum of 5 failures with total outages of 3 hours within a year
Response (time to respond to a user request)	<ul style="list-style-type: none"> <li>90% calls answered within 20 seconds</li> <li>Enquiry resolved within - 10 minutes (simple) 2 working days (complicated)</li> </ul>	Not applicable
Resolution (time to correct problem/fault)	<ul style="list-style-type: none"> <li>Urgent problem &lt; 1 hour</li> <li>Less urgent problem &lt;1 week</li> </ul>	Duration of any single outage < 1 hour
Measurement period	Monthly	Monthly
Responsibility for measurement	Service provider	Service provider
Reporting frequency and method	<ul style="list-style-type: none"> <li>Report on exception basis or on request</li> <li>System records</li> </ul>	<ul style="list-style-type: none"> <li>Monthly status report</li> <li>System records</li> </ul>

## Appendix 3 Business Case Template

The following is a template to assist departments with the preparation of the business case for the specific outsourcing project. The template is provided as a guide only as each outsourcing project has its own requirements.

<b>Executive summary</b>	Comment on the outsourcing project, various options, risks, critical issues, broad financial data and recommendations. Remember the scoping study is likely to be used in high-level decision making and that any document created as part of this phase, including the business case itself, may become a public document.
<b>Introduction</b>	An introduction to the outsourcing project, background information, reasons for developing the business case and the outline project plan.
<b>Current position</b>	Outline the current service arrangements, including standards, levels of service, stakeholder commentary etc.
<b>Issues identification</b>	Identify all the issues associated with existing service arrangements, including real opportunities for value for money improvement and how those issues may be dealt with.
<b>Industry review</b>	Review the state of the actual or prospective market for these specific services, including industry players, technology and other strategic developments.
<b>Assessment and management of risks</b>	Identify and characterise potential risks and outline a risk management plan.
<b>Options analysis</b>	Discuss the advantages and disadvantages of the genuine options available.
<b>Financial analysis and impacts</b>	Outline current costs as well as alternative options. Complete net present value (or other comparative financial) analysis, including sensitivity analysis. Remember that, at the business case stage, the existing costs and prospective contract costs are unlikely to be known with certainty. It is unwise to raise expectations of significant changes in cost arising from outsourcing unless these can be reliably substantiated.
<b>Qualitative analysis</b>	Outline the non-financial factors that need to be considered in the selection of the chosen option.
<b>Innovations</b>	Identify particular innovations included in the proposals. These are inherently risky in that by definition there are uncertainties in comparison with the prevailing arrangements for service delivery.
<b>Employee impact</b>	Assess the impact of any changed method in service delivery on departmental employees.
<b>Summary and recommendations</b>	Draw conclusions and detailed recommendations for the appropriate course of action.
<b>Appendices</b>	<ul style="list-style-type: none"> <li>♦ Cost benefit analysis</li> <li>♦ Financial impact statement</li> <li>♦ Key statistical and performance data</li> <li>♦ Outline SLA for the specific services</li> <li>♦ Other information required for a decision</li> </ul>



## Appendix 4 Risk Management

All activities are subject to risk whether outsourced or delivered in-house. Part of the assessment of an outsourcing option will be whether it assists with managing or mitigating risks involved in in-house delivery and whether any risks involved in outsourcing are in turn able to be managed or mitigated. Essentially, there are three types of risk present in an outsourced activity.

- ♦ **Inherent risks.** These are the risks that are present irrespective of the method of service delivery, whether in-house or external.
- ♦ **Planned risks.** These are risks that can be anticipated, estimated and planned for. In outsourcing risk is best allocated to the party that stands to gain economically from controlling it. But remember, risk allocation will increase or decrease the contract price depending on who bears the risks.
- ♦ **Contract risks.** Outsourcing is perceived as risky because some control is ceded to the service provider. The distancing of the department from day-to-day management of the service may heighten the perception of risk. However, outsourcing also offers opportunities for risk reduction because the formal analysis of the service during the process ensures that risks are identified and appropriate management responses are considered and implemented.

*(Note: There may be specific risks that arise from the transition from an internal service to outsourcing. These are addressed in Appendix 5: Transition Planning)*

In essence, a risk is anything which has the potential to prevent the department from achieving its objectives. The key aspects of a department's approach to risk management during outsourcing should be:

- ♦ A structured approach that formally identifies and analyses risks
- ♦ Involving departmental management in the process to achieve ownership of the risk management process and to promote a risk aware culture
- ♦ Considering the key risks in the areas of the department involved in outsourcing.

For each risk the following should be identified:

- (a) Describe the risk and its symptoms
- (b) Describe the consequences
- (c) Establish an impact rating
- (d) Establish a likelihood rating.

*(Note: A simple way of presenting this analysis is the worksheet provided at the end of this appendix.)*

Next an action plan should be prepared:

- (e) Identify existing risk mitigation controls
- (f) Determine response to each risk
- (g) Determine monitoring process.

### (a) Describe the risk and its symptoms

Drawing on expert opinion, experience and published guidance as available, the department should list the various risks (inherent, planned and contractual) together with a description of the symptoms by which these risks will be recognised.

### (b) Describe the consequences

For each risk the potential consequences should be described so as to provide the basis on which to assess the impact and the likelihood of occurrence. Consequences can be described using a value (e.g. days lost in

project implementation) or a physical measure (e.g. close-down of service due to weather conditions). Consequences may be financial or non-financial.

### (c) Establish an impact rating

The following ratings and qualitative descriptions can be used to assist in measuring the impact of consequences:

Catastrophic	:	A disaster with potential to lead to collapse of the service	5
Major	:	A critical event which can be endured with proper management	4
Moderate	:	A significant event which can be managed under normal circumstances	3
Minor	:	An event, the consequences of which can be absorbed but management effort is required to minimise the impact	2
Insignificant	:	An event, the impact of which can be readily absorbed through normal activity	1

Consequence factor	Insignificant ①	Minor ②	Moderate ③	Major ④	Catastrophic ⑤
Financial loss impact	-	\$x million	\$x million	\$x million	-
Service impact	Insignificant impact on the service	Minor impact on the service	Moderate impact on the service and related services	Major impact on (include loss of) relevant service	Significant damage to department
Outsourcing project delay	Days delay	Weeks without compromising the department	Ability to complete before busy period compromised	Project not likely to complete before 200X	Project abandoned

### (d) Establish a likelihood rating

The department should make a realistic assessment of the likelihood rating (i.e. how likely it is that the department will actually be exposed to each risk). Consideration will be given to:

- ♦ The anticipated frequency of the event occurring
- ♦ The working environment
- ♦ The procedures and skills currently in place
- ♦ Staff commitment, morale and attitude
- ♦ History of previous events.

The likelihood ratings and descriptions usually used are:

Almost certain	:	The event is expected to occur in most circumstances	5
Likely	:	The event will probably occur in most circumstances	4
Moderate	:	The event will probably occur at some time	3
Unlikely	:	The event could occur at some time	2
Rare	:	The event may occur only in exceptional circumstances	1

### (e) Identify existing risk mitigation controls

For each specific risk the department should consider whether controls are currently in place and identify the positive and negative control considerations in determining the control effectiveness. An assessment of the efficacy of any existing risk controls should be made.

### (f) Determine response to each risk

The department must next consider the risks unaddressed, or remaining despite existing controls, and decide whether they are acceptable in the context of the department and service objectives. The objective is not to eliminate all risks but rather to ensure that any residual level of risk is maintained at an acceptable level in a cost effective manner. The department may then adopt the following responses:

- ♦ **Accept the risks.** Management may decide that the level of residual risk is acceptable after considering factors such as:
  - The adequacy of current controls
  - The quality and quantity of information about the controls
  - The likelihood and consequences of the risk occurring
  - The cost of additional controls.
- ♦ **Develop risk mitigation through expert advice.** Management may decide that expert advice is required to assist in reviewing the controls associated with the risk. This could include experts internal or external to the department who are more familiar with best practice in a particular area. Experts can provide the benchmark data that can be used to measure against.
- ♦ **Develop risk mitigation through self assessment.** Self assessment promotes the philosophy that it is the people who work in the area who should be involved in the planning, implementing and monitoring of the controls in their area of responsibility. Management may decide that it is appropriate for people in their area to more closely assess their controls. Self assessment is best carried out in a workshop situation involving key staff, where existing or required controls are thoroughly scrutinised and developed.

Whatever the responses adopted, the course of action determined should be documented by the outsourcing project manager for inclusion in the business case. Specifically the management action plan must document:

- ♦ Brief details of the course of action
- ♦ Implementation/completion date
- ♦ Responsible manager.

### (g) Determine monitoring process

Monitoring of the risk management programme on an ongoing basis will commonly be delegated to the senior manager with responsibility for managing the outsourcing contract. In some instances a department may delegate this task to a senior manager not connected to the project thus providing an “outsider” viewpoint in ensuring that risks to the department are monitored and kept to a minimum.

Risk Assessment Worksheet

RISK DESCRIPTION/CAUSES		CONSEQUENCES		MATRIX					
				IMPACT					
				5					
				4					
				3					
				2					
				1					
				LIKELIHOOD	1	2	3	4	5
				IMPACT					
				5					
				4					
				3					
				2					
				1					
				LIKELIHOOD	1	2	3	4	5
				IMPACT					
				5					
4									
3									
2									
1									
LIKELIHOOD	1	2	3	4	5				
IMPACT									
5									
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2									
1									
LIKELIHOOD	1	2	3	4	5				
IMPACT									
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IMPACT									
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1									
LIKELIHOOD	1	2	3	4	5				
IMPACT									
5									
4									
3									
2									
1									
LIKELIHOOD	1	2	3	4	5				
IMPACT									
5									
4									
3									
2									
1									
LIKELIHOOD	1	2	3	4	5				

Instructions for completion:

- 1. Describe risk and its causes
- 2. Describe consequences
- 3. Complete matrix
  - (a) circle impact rating
  - (b) circle likelihood rating
  - (c) tick matrix where the two ratings cross
- 4.
  - (a) If tick is in green area, risk is probably acceptable no further action required.
  - (b) If tick is in amber area, ensure that risk management plans are in place.
  - (c) If tick is in red area, risk may be unacceptable and basis of contract may need to be reconsidered.

## Appendix 5 Transition Planning

The preparation of a transition plan for the transfer of service delivery responsibility from the department to the service provider is a necessary control step. Both the department and the service provider need transition planning. Normally the service provider is expected to provide an indicative transition plan as part of the tender. Following selection the department and the service provider should work together to integrate their respective transition plans.

The main focus of the transition plan is on activities that need to be undertaken by the service provider to assume full control of the service being outsourced in a manner that does not affect service continuity. However, during this phase the department is still actively involved in delivery, so the department's approval of the approach taken and its commitment to actions is essential.

The following is an outline of the elements of transition planning from the perspective of the department and the service provider. This should be used as a guide and may not be suitable for all outsourcing projects. Each project needs to consider the particular transition requirements that it involves.

### Department transition planning

- ♦ **Establish a transition management committee.** This may be a time to transfer some responsibilities from the department Project Manager to the Contract Administrator (see Appendix 11). In many instances the two roles are undertaken by the same person. Such an approach has some good points, but does tend to place a high level of reliance on one individual. It may be useful to mirror the service provider's approach to continuity and transition.
- ♦ **Prepare a project plan for this transition phase.** Highlight critical tasks within the transition management plan. These should contain details of responsibilities and time frames. There will be significant roles for both the department's and the service provider's representatives. The ongoing refinement of the plan is a part of the ITT, due diligence and contract formation processes.
- ♦ **Conduct transition management meetings** and other processes to manage the transition.
- ♦ **Prepare correspondence** to be sent to the service provider and announce decision to affected staff. Also advise other stakeholders.
- ♦ **Prepare complementary human resource management plans.** The plans need to address the situation of the department's staff and of any service provider's assisting the transition (including sub-contractors).
- ♦ **Prepare a communication strategy.** The communication strategy is to ensure a smooth transition to new service arrangements and lay the foundation for processes of continuous improvement throughout the term of the contract.
- ♦ **Identify and prepare assets** to be transferred to the service provider, if relevant. Ensure that appropriate leases or licences are also transferred. Dispose of surplus assets and equipment as required.
- ♦ **Finalise with the service provider the department's requirements** for the delivery of services, particularly the interfaces at operational and client service levels:
  - Confirm the prevailing legislative and administrative arrangements that govern the provision of services
  - Finalise relevant policy and procedural requirements for the delivery of services
  - Review and authorise the service provider's procedures, covering arrangements for normal operations, for specific emergencies and for specific disasters.
- ♦ **Establish contract management systems and reporting arrangements.** Review the transition process 3 months or so after the services commence so that:
  - Lessons are properly learned and applied to the ongoing contract operation and management
  - The next outsourcing project benefits from this experience.

## Service provider transition planning

The overall transition plan is broken down into components. Broadly these can consist of the following:

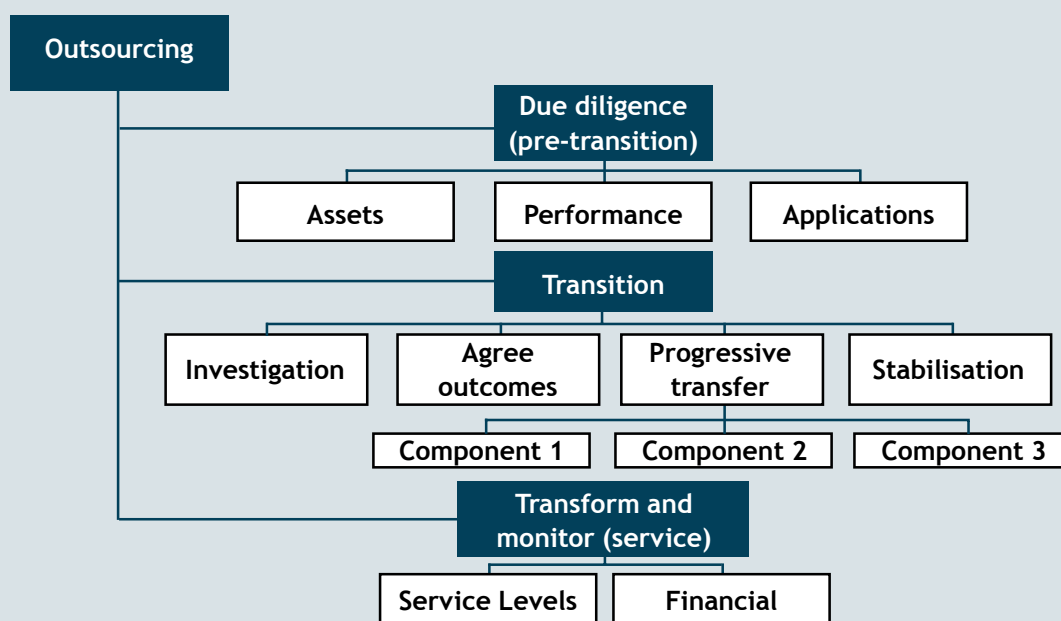
- ♦ **Due diligence check.** Ideally the due diligence check should be performed in advance of the transition as it assists the service provider and the department to decide whether they wish to enter into the outsourcing arrangement. However, it is often conducted at this stage as a contractual condition which must be satisfied
- ♦ **Transition of the service** (including any asset transfers - both third party contracts and/or physical assets). This is the core of the service provider's transition plan. It will describe how the service provider will take over a pre-existing service from the department or how it will start up a new service. For a pre-existing service, the plan will elaborate how service continuity will be maintained
- ♦ **Human resources** issue resolution and transition
- ♦ **Service level** monitoring arrangements and financial arrangements.

Each component can be broken down into sub-components. This will depend on the complexity of the service to be transferred, the accuracy of any existing service records, organisation of the service and relevant government policies.

The transition plan must be adequately communicated to all interested parties throughout the process. A formal programme of communication is generally set up for outsourcing arrangements. This is to ensure that the process continues to have credibility. It is also an important part in ensuring that department staff morale is maintained and that staff are willing to assist with the transition.

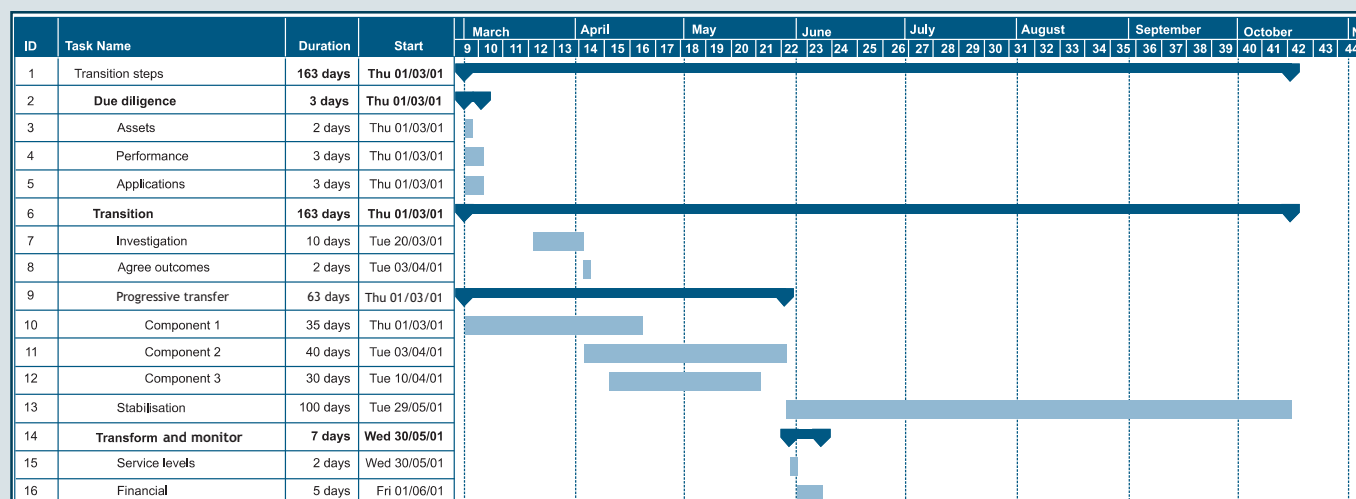
The elements of a transition plan will differ from project to project, along with the time commitments required. It is important to customise the elements according to individual demands of the project. An indicative breakdown of activities is indicated in the figure below.

**Figure A5.1: Indicative transition activities**



The activities are further developed in the project schedule, which provides the sequence and time aspects of the project for the service provider. It will also show the interconnecting contingencies between transition activities. A high-level transition schedule is presented in the following figure.

**Figure A5.2: Indicative high-level transition plan**



## Transition risk assessment

This process provides a framework for ensuring that the potential risks of the transition process are addressed. It is a critical part of transition planning for both the service provider and the department. The risk assessment process entails looking at each transition activity and identifying its associated risks and how they can be managed to ensure a smooth transition and limit adverse impacts on service continuity.

An indicative risk assessment plan is illustrated in Table A5.1 on the next page. The assessment shows the risk event, the service provider's response strategy, the symptoms that would indicate an occurrence of the event, and a summary of the risk response plan. Each identified risk event is also assessed for impact, probability of occurrence and the difficulty in detecting the event. These are then given a high, medium or low rating, so as to prioritise the need for a response. As with risk management for the outsourcing as a whole (see Appendix A4), responses will mainly focus on high impact/high probability risks.

**Table A5.1: Example of transition risk assessment plan**

Transition Risk Assessment Plan						
Risk Event	Risk Symptoms	Impact	Probability	Detection Difficulty	Service Provider Response Strategy	Planned Response
Department project management experience level is unknown	Lack of responsiveness or planning	L	L	M	Mitigate	Provide leadership and allow additional delay and lag time
Unclear delineation of roles for service provider and the department in monitoring and reporting	Undefined responsibilities impact upon SLA measurement during contract negotiation	M	M	L	Mitigate	Tight control during requirements definition and tight monitoring of schedule
Possible misinterpretation by department of the phases in the transition from current provider to service provider	Department interprets complete project plan as transition, without distinguishing the different elements of due diligence check (pre-transition), stabilisation (making the transition) and transformation (full and successful handover) as additional activities	L	M	L	Mitigate	Provide presentation of project plan to Department. Identify and agree department requirement for transfer of responsibility, commencement of SLA measurement, and delivery of value-added services

The meaning of the risk rating in each category is shown in the following table.

**Table A5.2: Transition risk rating**

Transition Risk Rating			
	High	Medium	Low
Impact	Risk will change scope of project schedule, resources or objective	Risk will require project re-planning, but not change project objective	Risk can be handled through minor changes to project execution
Probability	Risk event is very likely to occur	Risk will require project re-planning, but not change project objective	Risk can be avoided/ minimised through minor changes to project execution
Detection difficulty	Risk is hard to detect or impossible to forecast	Risk may remain undetected for some time	Risk is easily detected

Every risk identified will need to be considered and a response prepared in developing the overall transition plan. The risks identified in the transition planning need to be catered for both in selecting the appropriate skill base for the transition team and in implementing the transition plan.



## Appendix 6 Regulations/Circulars/Guides Related to Tendering

Some government regulations, guides and circulars related to tendering activities are listed below for reference (the list may not be exhaustive):

- ♦ **Stores and Procurement Regulations**
  - Chapter 2 Procurement of Stores and Services
  - Chapter 3 Tender Procedures
  - Chapter 4 Consultants Selection Procedures
  - Chapter 5 Contract Administration
- ♦ **A Guide to Procurement by the Government of the HKSAR**
- ♦ **Standard Terms and Conditions used for Tender for Services (GLD-Terms-2)**
- ♦ **Financial Circulars**
  - FC 10/1997 - WTO Agreement on Government Procurement
  - FC 11/1997 - Access to Tender Information
  - FC 11/1999 - Ground Rules for Special Consideration of Private Sector Initiatives
  - FC 3/2001 - Tendering Arrangements for Service Contracts
  - FC 4/2001 - Disclosure of Information for Firms Bidding in Different Capacities for the Same Consultancy Assignment
  - FC 5/2001 - Guidelines for Trading Funds Bidding for Government Contracts
  - FC 2/2003 - Initiating Works-related Tendering and Consultant Selection Procedures Before Funding is Secured

*(The above materials are accessible through the PSR Information Centre in the CCGO website.)*

## Appendix 7 Guidelines for Service Level Specifications

Users are advised to prepare service level specifications by addressing the following:

- ♦ Tender Objective
- ♦ Scope of Work
- ♦ Work Volume Information
- ♦ Key Stakeholders' Roles and Responsibilities
- ♦ Work Statements
- ♦ Performance Measures and Performance Targets
- ♦ Performance Assessment Plan
- ♦ Management Plan, Work Plan, Contingency Plan and Quality Assurance Plan
- ♦ Positive Incentives or Bonus Scheme
- ♦ Remedial Actions for Non-performance.

In preparing the specifications, users should:

- ♦ State both the mandatory and desirable requirements clearly, concisely, logically and unambiguously
- ♦ Focus on performance results rather than how the work is to be performed
- ♦ Provide adequate information for tenderers to decide and cost the service they will offer
- ♦ Specify measurable performance outcomes for assessing the contractor's performance
- ♦ Avoid over-specifying requirements
- ♦ Include only the essential characteristics of the requirement.

All requirements should be:

- ♦ Specific
- ♦ Measurable
- ♦ Achievable
- ♦ Relevant
- ♦ Transparent

## Appendix 8 Issues for Drafting a Contract

The contract should be drafted with special consideration to the following:

<b>The term</b>	This will depend on the type of service and risk profile. Clearly departments should avoid being locked into a high-risk arrangement for a long period. In Hong Kong, however, the tendency has been to be over cautious and miss opportunities to achieve value for money as a result of unreasonably restricting the length of contracts. Longer terms are often required to encourage the necessary investments in equipment and staff to produce quality services.
<b>Risk management</b>	<p>The risks of entering into an outsourcing arrangement should be mitigated as far as possible.</p> <p>For example, many organisations require service providers to hold and maintain appropriate public liability insurance policies for the duration of the contract. The service provider may be asked to provide evidence of this periodically.</p>
<b>Transfer of assets and employees</b>	<p>This is rare in existing outsourcing examples in Hong Kong. However, it is a feature of much international experience.</p> <p>For example, in IT outsourcing it is common for assets and staff to transfer to the service provider. It is possible that some staff may like the option to transfer to the service provider. Where this is the case appropriate arrangements will have to be established.</p>
<b>Intellectual property ownership</b>	<p>Both the department and the tenderer may have intellectual property rights that need to be protected.</p> <p>For example, the parties will need to work out an arrangement, such as licensing, if a software program critical to the service is owned by the department.</p>
<b>Business continuity</b>	Ensuring the continuation of the service throughout transition, outsourcing and any subsequent changes in contractual arrangements.
<b>Service levels</b>	Outlined in Chapter 2
<b>Incentive or bonus scheme</b>	To encourage good performance exceeding the required service levels and provide remedial measures for non-performance.
<b>Mechanism to vary payment and price formulae</b>	A well thought out, practical mechanism should be incorporated in the contract that will enable flexible responses to changing circumstances.
<b>Force majeure terms</b>	<p>These set out the procedures to be followed if service delivery is disrupted due to circumstances outside either party's control.</p> <p>For example, a typhoon may prevent the property management service provider from accessing a building to clean it.</p>
<b>Dispute resolution procedures</b>	See Appendix 9

<b>Integrity requirements</b>	Tenderers should be made aware that the government intends to deal only with service providers committed to ethical business practices. Evidence should be sought that the company has, and promulgates to its staff, a company code of ethics and a staff code of conduct.
<b>Performance guarantee or a financial undertaking</b>	The department may consider seeking a performance guarantee from any parent company of a service provider or, if there is not a parent company, an undertaking to provide a sequestered account at a fixed sum to which the department will have unrestricted access in the case of service failure requiring the contracting of another service provider.
<b>Security</b>	Conditions should be included covering access to, and protection of, confidential information.
<b>Transition-in-service</b>	An obligation should be imposed on the service provider to provide a detailed transition plan.
<b>Step-in rights</b>	The department requires a legal right to step in and resume the service in the event of serious default, or to replace the existing service provider.
<b>Termination and transition to a new service provider</b>	<p>In drafting the contract, both parties need to establish the rules to be applied should any situation require the early termination of the contract. This element of the contract should also cover the process to be adopted should the department choose another service provider at the end of the contract. Establishing any rules of transition between an existing and another service provider must be built into the contract with the existing service provider.</p> <p>For example, issues for the contractor are most likely to relate to cash flow. Issues for the department are about the need to ensure that disengagement from the contract does not adversely affect service continuity. Generally the department will need to cover the time it will take to go to market again, select a service provider, hand over and install the new service provider.</p>
<b>Value-added services</b>	Tenderers may be able to provide value-added services. Tenders normally contain a standard clause advising that alternative proposals which improve the offer (e.g. fully conforming to the mandatory requirements but containing desirable features in addition to those specified in the tender documents) may be submitted and will be considered by departments in their evaluation of tenders.

## Appendix 9 Dispute Resolution

The following is an outline of a dispute resolution process commonly used in outsourcing contracts. It is illustrative of the conciliatory nature of outsourcing contracts. Arbitration is a last resort, rather than the first measure taken. This is to protect the relationship between the parties, as much as is possible, during the resolution of any dispute.

The department and the service provider agree to work jointly to resolve disputes in an amicable and efficient manner for the benefit of both parties. The dispute resolution process specified in this section shall be regularly and jointly reviewed to ensure its relevance and acceptability to both parties. The resolution process shall provide for the escalation of disputes where this is found to be either necessary or expedient.

The service provider is responsible for the establishment and maintenance of a register of disputes. This register need not be dedicated to disputes, but may coincide with and be part of other action registers, such as that used by the service provider's service centre to log issues and problems.

Dispute resolution is through an escalation process. There are four levels of escalation:

- ♦ The individual representatives of the department and the service provider between whom the dispute may be construed to exist
- ♦ The department's Project Manager and the service provider's Project Manager associated with the foregoing representatives
- ♦ The department's Contract Manager and the service provider's Account Manager
- ♦ The Head of Department and the service provider's Managing Director.

Any dispute arising in connection with the outsourcing contract which cannot be settled by negotiation between the parties or their representatives should be submitted to arbitration in accordance with the relevant local rules of arbitration.

## Appendix 10 Tender Evaluation

A tender evaluation template is a standard form for an evaluation team to use when evaluating the technical/operational aspects of a tender. It is to be used for recording the scores given to each tenderer as each tender is evaluated. It should be developed prior to the issue of the tender as part of the tender documentation. The primary source will be the statement of requirements, which will provide an overview of the mandatory and desirable criteria.

Each score on the evaluation sheet should be supported by as many relevant comments as possible. This is so the evaluation team can support the scores they have given each tender with evidence of how the score was reached. There is generally no space allowed on the evaluation sheet for supporting comments. This is because the comments are typically not submitted with the evaluation scores, but may be produced later if required.

The total score for an evaluation will be combined with the financial evaluation results to produce an overall score for each tenderer.

### Evaluation plan

Basically the evaluation consists of three elements:

- ♦ The evaluation criteria
- ♦ Weighting for each criterion
- ♦ The scoring protocol.

The overall evaluation criteria must be agreed prior to issuing the EOI/ITT. Other elements of the plan must be agreed prior to opening the responses - such as the weighting for the evaluation criteria. A few elements may be resolved during the course of the evaluation - such as the convention for scoring particular submissions. However, the intention should be to resolve as many issues and reduce subjectivity in scoring as far as possible before commencing the evaluation.

### Outline of evaluation criteria

The setting of evaluation criteria is a critical component of the EOI and ITT requirements. Each outsourcing project is different and outsourcing project managers should use the following only as a guide to frame the criteria for each project.

The following provides an example list of criteria for an EOI.

*EOI - Whom are you prepared to receive proposals from in terms of capability and experience?*

No.	Criteria	Weight	Raw Score	Weighted Score
1	Demonstrated understanding of legislative and administrative framework in the service area of the department			
2	Demonstrated ability to work within the environment of the department and its clients			
3	Previous experience or demonstrated ability to meet the service needs			
4	Management philosophy as it relates to staffing, personnel management and training			
5	Approach to the provision of the services			
6	Approach to quality management - quality assurance certification			
7	Philosophy and approach towards innovation in providing and/or managing the specific services			
8	Financial capacity			
9	Any other factors that the evaluation team consider relevant, whether or not those factors or criteria have been identified in the EOI document			
	<b>TOTAL</b>			

The following provides an example of criteria for the three aspects of evaluation of an ITT: technical, financial and combined.

*ITT Technical - Who will provide the best service?*

Aspect	Criteria	Hurdle	Weight	Raw Score	Weighted Score
<b>Technical</b>	Proposal meets service specification	yes/no			
	Tenderer technically capable	yes/no			
	Tenderer complies with relevant regulations	yes/no			
	Tenderer's personnel adequately qualified	yes/no			
	Tenderer's facilities appropriate	yes/no			
<b>Capability</b>	Proposal demonstrates understanding of the outsourcing objective	yes/no			
	Tenderer's experience and reputation in the industry	yes/no			
	Tenderer's track record as contractor	yes/no			
<b>Quality</b>	Use of best practice in the service approach	yes/no			
	Feasible innovations offered	yes/no			
	Arrangement to ensure good customer service	yes/no			
<b>Transition</b>	Proposal for handling transition	yes/no			
<b>Others</b>	Management team and structure	yes/no			
	Complaints management	yes/no			
<b>Comments</b>					
<b>Additional offers</b>					
<b>Total Scores</b>					



*ITT Financial - Who's price and financial arrangements are best?*

Criteria	Hurdle	Weight	Raw Score	Weighted Score
Proposed contract payment arrangement	yes/no			
Potential costs savings	yes/no			
Transition costs	yes/no			
Net present value	yes/no			
Financial viability	yes/no			
<b>Total</b>				

*ITT Combined - Which is the best deal?*

Overall Evaluation	Weight	Weighted bid score	Overall weighted score
Technical score			
Financial score			
<b>Total</b>			

## Weighting

When the evaluation criteria are established they should be “weighted”. That is, each of the criteria should be assigned a weight that will reflect its relative importance in the selection decision. The score for each of the criteria are multiplied by these weights to provide the weighted score which is then summed to provide the total score for each tender.

To aid in evaluation tenderers should be encouraged to address the evaluation criteria directly and succinctly. In particular they should be discouraged from including extraneous marketing material.

## Scoring protocol

The process of assigning a score to each response for each evaluation criterion can be undertaken as follows:

- ♦ The evaluation team must assign a score for each of the evaluation criteria in the agreed score range
- ♦ The score is multiplied by the weighting factor to give a weighted value
- ♦ The weighted values are added for each response and the highest scorer may become the preferred tenderer.

Allocation of point scores could be in a range of 0-4 as a possible scoring convention. This needs to be resolved with all members of the evaluation team prior to scoring each response. All members of the team need to have a shared understanding of what is meant by each scoring level. Before responses are scored, the rationale for each scoring number is set and universally adhered to for any particular outsourcing project. The following provides an example of a 5-point scoring scale:

- 0 Does not address requirement
- 1 Marginally fails to meet major requirements
- 2 Appears to be suitable for requirement (minimum hurdle)
- 3 Exceeds requirement overall
- 4 Best practice

A score of 0 for any attribute should normally disqualify the response from further consideration unless there are exceptional circumstances. Where a criterion has been set as a hurdle, a score of 2 or more must be achieved to avoid disqualification of the bid.

## Evaluation team administration

There are a number of administrative matters to consider when setting up and conducting the evaluation. Broadly, these are as follows:

- ♦ The evaluation team needs a secure and comfortable site to use throughout the evaluation process
- ♦ The evaluation team must use administrative arrangements and procedures that are in accordance with best civil service practice and that an appropriate audit trail is established and maintained
- ♦ Responses to the EOI or ITT will only be received at the designated site
- ♦ All tenderers will be noted on a listing schedule. E-mails should include the tenderer's organisation, the date and time the response is removed from the receiving box and the signature of those present at the opening of the receiving box
- ♦ A written record of all agreed decisions and actions during each meeting of the evaluation team must be maintained. The minutes of each meeting shall be available to all members of the evaluation team for endorsement at the subsequent meeting
- ♦ All notes concerning a particular proposal written during the evaluation should be on paper provided for this purpose and retained for audit trail purposes. Notes are to be kept by the evaluation team in respect to each evaluation criterion within their specialist field of interest
- ♦ Evaluation team members need to be careful not to effectively score the same element of the response in several of the evaluation criteria (i.e. avoid double counting)
- ♦ A process should also be designed to deal with any inconsistencies in the evaluation process.

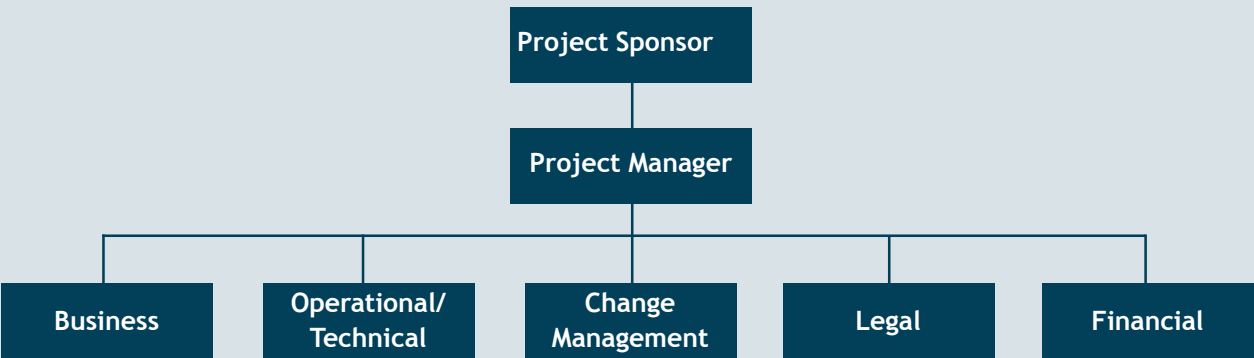
## Appendix 11    Project Team Roles

This appendix provides an overview of a typical outsourcing project team and the functions of each key team member. It may be used as a reference for senior management when allocating resources to an outsourcing project team.

The number of staff used and the time it takes for them to complete their tasks will vary from project to project. It is likely that the outsourcing project will occupy a significant portion of the team members' time throughout the process. It may be desirable for the key team members to be relieved of their day-to-day duties during this period. For example, the project manager and the key technical/operational staff will be necessarily involved in the day-to-day project management and this may require a full-time commitment to ensure that critical time lines are met. One of the most common reasons for delays in outsourcing projects is not allocating sufficient resources to support it.

It is also desirable that arrangements for the outsourcing project team's ongoing roles are agreed prior to the outsourcing exercise. This is particularly the case if their posts are likely to be affected by the outsourcing arrangement. If this is not done, it will be difficult to obtain their commitment to the change. It will also be difficult to develop an objective and unbiased recommendation.

### Roles and responsibilities of project team



*Figure A11.1: Example of project team for business case and tendering and selection phases*

#### Project Sponsor

The project sponsor acts as the project spokesperson to senior management. This person will typically be a senior manager (at Directorate level) with sufficient authority to sign off on commencing the project, and also sign off acceptance of the project being satisfactorily completed. The project sponsor is ultimately responsible for the successful completion of the project, and consequently must obtain all necessary resources to ensure its satisfactory completion.

#### Project Manager

The Project Manager reports directly to the Project Sponsor. The Project Manager is responsible for the overall management of the project on a day-to-day basis. The Project Manager often acts as the primary contact for the service provider during the outsourcing phase of the project.

### Project team members

The project team members will be drawn from a number of disciplines. This will vary due to the nature of the service to be outsourced. Broadly the team members can be classified under the headings of business, technical/operational, financial, legal and change management. These are the basic skills that will be required for any outsourcing project. One person can fill any number of the roles if the size of the project and the skill set allow.

These skills will be necessary to guide the project from the business case phase to the end of the tendering and selection phase.

The team members report directly to the Project Manager. The roles of the team members are to:

- ♦ Collect and collate data
- ♦ Prepare the various sections of the business case, EOI and ITT, dependent on their experience and expertise
- ♦ Assist in evaluation
- ♦ Assist in due diligence checking.

Specialist team members may also be part of the negotiating team. For example, legal advice is necessary to develop the outsourcing contract, particularly if variations to standard government contracts are envisaged. Lawyers should also be used to assist with reviewing the tender documents prior to issue. The contract will form the formal part of the outsourcing relationship and it is vital that it be correctly drafted. Legal advice may also be necessary on the negotiating team. This is particularly important when points of law are being discussed as part of the negotiations. Involvement of the Department of Justice and/or external legal counsel should be considered as early as possible in the outsourcing process.

Another specialist who is part of the tendering and selection process but not part of the department team can be the probity auditor. A probity auditor oversees the tendering and selection process providing an independent guarantee of the probity of the processes undertaken. Probity auditors are most likely to be established by a department when contracts are very large, or it can be expected that the tendering and selection process may be subject to considerable scrutiny and the department wishes to assure all stakeholders of the transparency, fairness and reliability of the process.

### Departmental contract management team and service provider management team

Specialist team members should be engaged by both the service provider and the department to manage the contract on an ongoing basis. It is possible that many of the staff involved in the business case and the tendering and selection phases, from both the department and the service provider, will stay involved in the contract management process.

The contract management structure will be a dynamic one. It will evolve as the contract progresses through transition, implementation and ongoing contract management. The cost and structure in the final year of an outsourcing contract may be different to that of year one.

The number of departmental staff required will be less than an in-house operation as the organisation is no longer involved in the day-to-day operation of the services. The department should only be involved in managing service delivery and troubleshooting issues as they arise. The service provider is in charge of both the “doing” and the reporting on the “doing”. Value for money is unlikely to be achieved if the department employs significant numbers of staff in an area that has been outsourced.

Changes in contract scope may also influence the type of contract management expertise required and the number of staff employed in this area. Another influence on change could be the evolution of the reporting process and the end of the change management process. Both of these may be expected to become less time intensive over the life of the contract as the changed arrangements are bedded down.

Regardless of the scope, there is often a need to maintain access to certain project skills independent of the service provider. The reasons for this include:

- ♦ Ensuring that those managing the contract and managing incidents on a daily basis are regarded throughout the department as having sufficient expertise to do so
- ♦ Using the retention of these skills as a form of insurance in case the outsourcing is not successful. The department can then build itself up to the point where it is again able to manage the service internally
- ♦ Retaining sufficient corporate memory to:
  - ensure that systems and processes are implemented in accordance with policies
  - know the reasons behind the policies
- ♦ Retaining sufficient corporate memory to ensure that policies are set for the contract management function. This would be done by the contract management staff in conjunction with the service provider and key customers within their organisation.

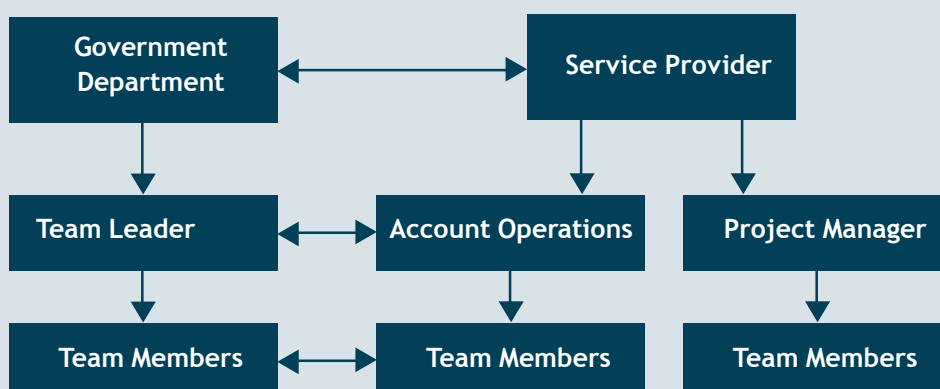
The departmental contract management team should be appointed as early as possible. They should begin work prior to the commencement date of the contract. This is because they will be required to assist with:

- ♦ Transition planning
- ♦ Recruitment and/or training of staff members (if sufficient contract management skills are not available in-house)
- ♦ Contract negotiations (particularly the contract managers)
- ♦ Developing knowledge of the outsourcing contract terms and conditions
- ♦ Developing and documenting contract management policies
- ♦ Communicating and promoting the use of the outsourcing arrangement throughout the department
- ♦ Establishing good working relationships with their service provider counterparts.

The project sponsor will also need to be involved during this phase of the outsourcing.

### Roles and responsibilities of contract teams

**Figure A11.2: Service provider and departmental contract management teams' roles and responsibilities**



The roles and responsibilities of the respective service provider and departmental teams should correspond with each other in equivalent level for the key positions as far as is possible. These key positions are the department contract manager, department team leader, service provider account manager, account operations manager and project manager.

**Department: Contract Manager**

**Primary Function:** To manage the relationship between the department and the service provider. Responsible for assisting the service provider in communicating, promoting and encouraging the use of the services within the department. Also sets the strategy for the service performance in conjunction with the Team Leader. The person chosen to fill this role will depend upon the department's arrangements for managing contracts. Some departments will establish specific contract management units. If the head of this unit has sufficient authority then he is likely to take on the role of Department Contract Manager. In other instances this role will be filled by the Directorate level officer responsible for the service area being outsourced.

**Responsibility:** The management of the outsourcing contract. Ultimately responsible for monitoring and enforcing service levels. Facilitates benchmarking and auditing exercises. Reports to senior management on contract performance. Responsible for building an effective contract management team.

**Department: Team Leader**

**Primary Function:** To interface with equivalents on the service provider side. Manages the relationship at that level. Facilitates reporting processes and analyses reporting data provided against the service levels set in the contract.

**Responsibility:** Responsible for compiling service level measurement data and submitting reports to the Department Contract Manager. Responsible for enforcing service levels where required.

**Department: Team Members**

**Primary Function:** To liaise with the service provider team members and to manage the relationship at the operational level of service delivery.

**Responsibility:** Responsible for assisting in resolving day-to-day performance issues in conjunction with the service provider. Responsible for assisting the Team Leader and the Department Contract Manager as required.

**Service Provider: Account Manager**

**Primary Function:** To build and manage the service provider relationship and business in an outsourced account, by ensuring profitability, growth and customer satisfaction on all service provider services. Sets the strategy for the service performance in conjunction with the Account Operations Manager.

**Responsibility:** Strategic planning, growth, direction marketing, delivery and profit and loss for the account.

**Service Provider: Account Operations Manager**

**Primary Function:** Manage the delivery teams, including recruitment and skills development. Performs either directly or through a matrix organisation. Ensures customer satisfaction through the efficient and effective delivery of contracted services to the customer.

**Responsibility:** Delivery of all operational services to the customers according to the SLA and ensuring that delivery costs are within or better than the delivery costs contracted. Acts as a single point of contact with the customers for tactical operational issues.

**Service Provider: Project Manager**

Primary Function: Liaison with peers in the department to achieve specified project outcomes. Operates in conjunction with the Account Manager.

Responsibility: Overall direction and delivery of all projects related to transition, implementation and ongoing service delivery. Reports and escalates all issues requiring senior management intervention. Reports progress against plan, including contingency strategies and options to improve mutually agreed business objectives.

**Service Provider: Team Members**

Responsibility: Team members are involved in the delivery of services provided to the department.



## Appendix 12 Outsourcing Benefit Analysis Template

### Summary

Tangible Benefits	Estimated Savings (\$M)	Actual Savings (\$M)	Reasons for Deviation
Recurrent Savings (from year      to year      )			
(I) Realisable Savings			
(II) Notional Savings			
Non-recurrent Savings (during year(s)      )			
(I) Realisable Savings			
(II) Notional Savings			

These figures should be net savings, taking into account all cost elements arising from the outsourcing (e.g. payment to contractor, contract management and staff redundancy). Details should be shown on the schedule on the next page.

Intangible Benefits	Planned	Realised
(I) Service Standards		
(II) Additional Services		
(III) Accessibility Improvements		
(IV) Others (specify if any)		

## Tangible Benefits: Details

Tangible Benefits	Estimated Savings (\$M)	Actual Savings (\$M)	Reasons for Deviation
Recurrent Savings (from year      to year      )			
<b>(I) Realisable Savings</b>			
(a) Reduction in staff costs (deletion of existing/approved posts)			
(b) Reduction in other operational costs (e.g. consumables, hire of services)			
(c) Increase in revenue to the government			
(d) Reduction in costs incurred by other departments (e.g. rental payment)			
(e) Others (specify if any)			
<b>(II) Notional Savings</b>			
(a) Fragmented staff savings for internal redeployment			
(b) Increase in productivity			
(c) Cost avoidance to meet growing demand or future needs (e.g. avoidance of additional staff and replacement of equipment)			
(d) Reduction in costs currently not charged to the department (e.g. government accommodation)			
(e) Others (specify if any)			
Non-recurrent Savings (during year(s)      )			
<b>(I) Realisable Savings</b>			
(a) Revenue from transfer/sale of assets			
(b) Others (specify if any)			
(c) Offsetting costs of implementation (e.g. write-off of assets, redundancy costs)			
<b>(II) Notional Savings</b>			
(a) Avoidance of capital investment (e.g. system development for new service)			
(b) Others (specify if any)			

This guide has been prepared by the Efficiency Unit.

It has been posted on <http://host1.ccgo.hksarg/cso/eu/psric/> and may also be accessed via [www.info.gov.hk/eu/](http://www.info.gov.hk/eu/)

For copies of this guide and advice on outsourcing please contact the EU Help Desk (Tel : 2165 7255)

Other documents in this series are:

- Serving the Community By Using the Private Sector (June 2001); and
- An Introductory Guide to Public Private Partnerships (PPPs) (August 2003).