WHITE PAPER | IT OUTSOURCING | PUBLIC SECTOR

Transformational Outsourcing

A self-funded approach to transforming an IT organization

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Many government organizations find themselves weighed down by aging IT environments that consume an increasing amount of annual operating budgets and, in turn, may lead to a downward spiral into technological obsolescence. In many cases, these organizations recognize the need for a truly transformative modernization of IT systems and processes, but most lack a funding source or the expertise to implement such a transformation. One innovative approach that government agencies are considering is transformational outsourcing.

In the transformational outsourcing model, an IT services company assumes responsibility for providing key IT services and identifying cost savings, much like the traditional outsourcing model. The difference is on the emphasis. With transformational outsourcing, early cost savings and process improvements are used to free

up operating budget capacity and pay for technology investments to produce future transformation, leading to enhanced service to the public.

This paper is intended to help government IT executives better understand how to structure and implement a dynamic outsourcing program that can fund future technology modernization. In this paper, we will:
- Describe a conceptual framework for transformational IT outsourcing.
- Discuss methods for achieving operational efficiencies and funding a transformation program.
- Demonstrate how an outsourced service delivery model results in reduced costs and enhanced organizational flexibility.

The challenge: Aging technology and scarce resources

Government organizations are growing more reliant on information technology to support mission-critical activities while managing an increasingly complex portfolio of IT systems and infrastructure. As technology ages and a growing proportion of the organization's IT workforce qualifies for retirement, the challenges for senior government leaders and IT managers multiply. How can your organization keep mission-critical legacy systems running, find qualified personnel to operate them and identify funds to gradually modernize these systems?

A typical government IT portfolio consists of an enormous, assorted mix of applications and infrastructure components across a wide range of programming languages, operating systems, databases and devices. Many systems were installed years or even decades ago and have been repeatedly modified to support policy changes or new technology. Even worse, some systems have not been updated in years and are now obsolete or no longer serviceable by the original supplier. Over time, such systems become burdensome to maintain and can only be enhanced to meet changing policy requirements through great effort and expense. As these aging systems reach end of life, they can severely constrain an agency's ability to operate. Sometimes, they represent significant operational risk.

Complicating matters, many government organizations' budgets remain tight and the investments necessary to modernize and transform aging systems are difficult to secure. In fact, organizations are devoting ever larger percentages of operating budgets to simply maintain existing systems, thereby minimizing potential investment in modernization and limiting future opportunities.

Seeking budget support from elected offi cials for modernization and transformation has met with mixed results. Officials are often skeptical of the cost of large transformational projects. Some may support the concept but remain unable to secure sufficient resources given competing budget priorities. Given these roadblocks, many organizations are giving the IT outsourcing model a fresh look.

> **When done properly, transformation outsourcing is self-funding and can lead to a positive upward spiral of investment and modernization that continues indefinitely.**

A transformative model for IT outsourcing

IT outsourcing refers to the practice of transferring responsibility for IT services, such as application maintenance and development, help desk services or other aspects of an IT operation, to a company that specializes in providing such services. In an outsourcing arrangement, the outsourcing organization typically retains overall strategic control of IT but delegates responsibility for the actual provision of IT services to a different organization, often in the private sector.

Large organizations often consider outsourcing IT services when they need to aggressively reduce costs or lack the internal resources to execute a key aspect of IT. However, when structured properly, an IT outsourcing program can also drive self-sustaining technology modernization and continuous business process improvements, freeing up funding to invest in modernization and technology enhancements. This model, known as transformational outsourcing, can ultimately improve service to the public.

The key in any successful transformational outsourcing effort is to eliminate inefficiencies in systems and business processes, and then reinvest the resulting savings in technology and process improvements. When done properly, transformation outsourcing is self-funding and can lead to a positive upward spiral of investment and modernization that continues indefinitely.

Creating a continuous cycle of improvement depends on identifying both efficiencies and new revenue streams. Opportunities to reduce costs in an outsourcing engagement often include:

- Using technology to drive transactions from high cost service channels (for example, walk-in service centers or call centers) to lower cost methods such as interactive voice response (IVR) telephone systems, the web or mobile devices.
- Implementing an outreach campaign that encourages members of the public to improve their experience by using lower-cost service delivery channels.
- Implementing or improving IT service management tools (for example, knowledge bases) that help service delivery personnel improve the efficiency of inperson and phone interactions.
- Shortening or eliminating transaction times by continuously measuring and improving service delivery processes. (This could involve either constituent-facing services or back-office transactions).
- Identifying and leveraging common business processes and systems between multiple agencies to eliminate redundancy, reduce system support costs and streamline business processes.
- Instituting consistent, standard procedures across the organization (for example, in accordance with IT Information Library).
- Refreshing devices to keep them current and serviceable or replacing those that are obsolete.

Another way to fund improvements is through the creation of new revenue. Such revenue can often be gained by enhancing accessibility to key information, adding enriched features or developing alternative services that add value for the public. For example, a government organization can sometimes charge a convenience fee for a new service or for improved service delivery time for existing transactions.

Whether by reducing operational costs or identifying new sources of revenue, a properly structured transformational outsourcing initiative has the potential to create enough budget space to reinvest in transformation projects and to modernize a technology footprint without increasing overall budget size.
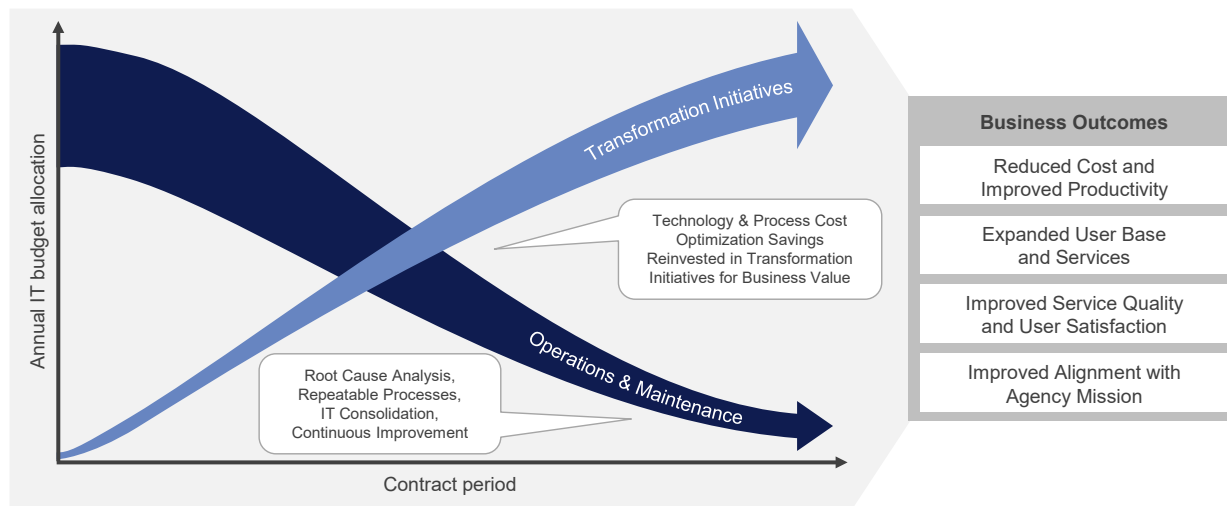
Figure 1: A successful IT outsourcing engagement helps accelerate investment in transformation initiatives while reducing operations and maintenance costs.

As Figure 1 illustrates, the annual budget allocation for operations and maintenance in a successful transformational outsourcing engagement will decline over time, while the budget for transformation grows.

Developing a successful IT outsourcing program focused on transformation

Rarely is transformation the only reason for a large organization to consider an outsourcing initiative. In choosing to outsource IT, an organization may seek to reduce costs, gain access to technical skills and technologies, improve service delivery, modernize technology and reduce risk. Some agencies also conclude that outsourcing IT will enhance their organization's focus on its core mission.

A critical first step in transitioning from an in-house approach to IT to an outsourced approach is to establish clear and compelling objectives. By setting clear objectives, an organization can select the right partner and establish a proper framework for the partner relationship.

Also essential: The organization must commit up front to using its savings from operations and maintenance improvements for transformational initiatives such as technology modernization. Only through the commitment to reinvest its savings can an organization create a continuous cycle of cost reduction and transformation for the long term. Other elements in launching successful programs include:

- **Seeking expert guidance.** Most organizations will likely not have the internal expertise to implement an IT outsourcing relationship with an IT service provider. Given the criticality of an outsourcing endeavor, an organization considering such a transition will want to enlist the help of specialized consulting or legal firms to help prepare and guide them through the process of establishing a contractual relationship with a respected IT service provider.
- **Establishing an internal team.** If rank-and-file employees learn that an organization is considering outsourcing, fear and doubt about job security can lead to an increase in attrition. With this in mind, it is absolutely critical to manage an IT outsourcing initiative in a sensitive manner. A successful approach includes establishing a diverse but tightly knit core internal team that includes agency executive management, outside experts and senior management representatives from IT, legal, procurement and human resources. Such a team can help drive a successful IT outsourcing program.
- **Understanding IT portfolio costs.** IT portfolios grow over time. Often, organizations do not have a proper sense of the real size and ongoing expense of their portfolio. When this is the case, it is important to first perform a complete functional, technical and strategic review of an organization's IT portfolio before trying to structure a transformational outsourcing engagement. A portfolio review helps the organization gain a better understanding of the state of each application, identify underperforming assets, and estimate and prioritize opportunities for gaining significant benefits from an IT portfolio rationalization initiative. A comprehensive portfolio review also includes establishing a baseline for current and past IT spending along with a breakdown of the funding devoted to operations and maintenance activities as opposed to transformation initiatives. All of this information can later serve as important inputs in the outsourcing process. It can also lead to specific recommendations on how to reduce the high cost of low-value applications, infrastructure and services and to maximize the business value of an IT portfolio.
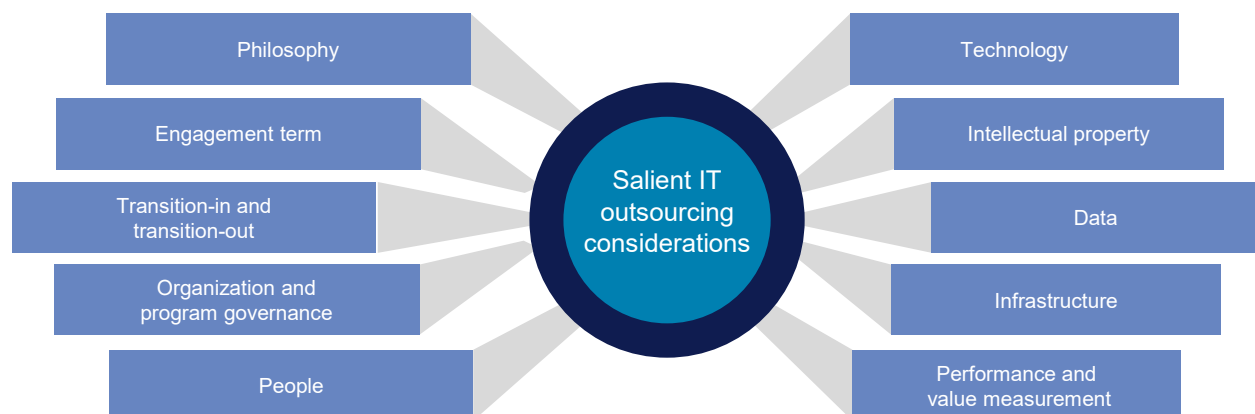

Figure 2: Salient outsourcing considerations -- a successful IT outsourcing relationship must carefully consider several factors.

Additional factors to consider

Government agencies must consider many factors before undertaking an IT outsourcing program. Some of the most significant include the following:

- **General philosophy.** An IT transformation program involving a third-party outsourcer should be developed with the goal of establishing a long-term partnership that is beneficial to both organizations. The outsourcing arrangement must be built on a performance-based model that incentivizes and rewards consistent, positive results and penalizes the IT service provider for sub-par performance.
- **Term of engagement.** Given the size and transformational nature of any large outsourcing engagement, a good initial term to consider is five to seven years with multiple two-year renewal options for the agency. An initial timeframe of this length encourages long-term thinking on the part of both the agency and the service provider when it comes to transforming processes and determining what investments to make in new technology. Such a contractual length also enables the gradual pay-as-you-go transformation approach to have a materially positive impact on the organization.

> **The transition-in process provides the foundation in any outsourced service delivery model, so it must be conducted with great care.**

- **Transition-in.** The transition-in process provides the foundation in any outsourced service delivery model, so it must be conducted with great care. Depending on the size and scope of the IT portfolio, a suitable transition can take up to six months. During the changeover, the IT service provider gradually assumes responsibility for service delivery, operations and IT support. As part of this, the provider's team works with the agency's team and any existing third-party contractors to document standard work processes and procedures.

> **Good governance includes structures for identifying key reports, periodic meetings to monitor performance, and systems to manage and operate the engagement at all levels.**

- **Organization and program governance.** No matter how many services an agency may decide to outsource, it will still need to retain an adequate level of staff to guide overall IT policy, make strategic IT decisions, and manage the relationship with the primary service provider and other IT vendors. In an outsourcing engagement, good governance includes structures for identifying key reports, periodic meetings to monitor performance, and systems to manage and operate the engagement at all levels.

  At a minimum, every engagement requires the establishment of an organizational chart and a list of key roles and responsibilities for all leaders. A proper governance structure also identifies who has authority to approve the projects, products and services delivered by the service provider, as well as how to manage any changes to the agreement that guides the engagement. In addition, agencies must assess and plan for the interdependencies that the outsourcing service provider will have with other key IT suppliers.

> **The service provider's onboarding process needs to inform and prepare employees and clients for change by establishing open and direct communication.**

- **People.** When transitioning a large IT portfolio, the service provider may "rebadge" government employees who fall within the scope of the new service delivery model, at least through the transition period. Doing so protects the interests of existing employees and also mitigates the risk of service disruption. Eventually, some of the transitioned employees may choose to return to the public sector in another capacity. Others may remain with the new service provider, preferring to support the delivery of public services from within the private sector. Whichever path employees choose, the service provider's onboarding process needs to inform and prepare employees and clients for change by establishing open and direct communication. Human resources teams from both organizations must work closely with each transitioned employee to make certain they understand the service provider's compensation, benefits, policies and systems, as well how any existing benefit obligations will be addressed by the agency.
- **Technology.** Once the transition is complete, the IT service provider assumes responsibility for the support of all in-scope systems. The service provider is also expected to review the technology roadmap that applies to all of these systems, as well as to make recommendations on how to evolve them to minimize costs and improve performance.
- **Technology roadmap.** During the transition into an outsourcing engagement, the service provider will assess agency technology to determine if any systems can be migrated to a cloud-based environment and if the systems are accessible across different common user devices and platforms (for examples, browsers).

The IT service provider is also expected to develop a prioritized list of transformative improvements, recommendations and projects, and to present that list to the agency's program management team.

> **The technology roadmap needs to be fine-tuned to the available funding stream and updated at least once per quarter as it evolves.**

The service provider will perform a cost/benefit analysis that will help both the agency and the service provider evaluate the merit of each project. (Transformation projects are usually funded by cost savings due to efficiency improvements and the creation of new revenue streams from value-added services.) Realistic goals should be set for the amount of funding to be made available from cost savings for reinvestment. In addition, the technology roadmap needs to be fine-tuned to the available funding stream and updated at least once per quarter as it evolves.

- **Intellectual property.** Existing intellectual property continues to belong to the originating organization. However, an agency should be willing to discuss how both it and the IT service provider could benefit if that provider were to own any technology and intellectual property created over the course of a transformation program.
- **Data.** An agency typically owns all data related to systems in the scope of an outsourcing engagement. The data also will continue to be protected by relevant privacy and public records laws. With that said, a service provider may seek (or even require) exclusive rights to use that data to provide related services to the public on behalf of the agency. In gaining rights to the data, the service provider may look for ways to use it to create new value and revenue streams for the agency, subject to applicable privacy laws and regulations.

> **Although agencies typically retain ownership of facilities and assets, they should consider transferring it if doing so would benefit both the agency and the service provider.**

- **Infrastructure.** Any successful outsourcing agreement must make clear the ownership, management and maintenance of infrastructure. The service provider's role may include providing standard desktop hardware and software to all of its employees in an outsourcing engagement. Conversely, it may be the responsibility of the agency to provide facilities, network access and telephone access to the service provider's employees. Although agencies typically retain ownership of facilities and assets, they should consider transferring it if doing so would benefit both the agency and the service provider.

One important physical infrastructure consideration is the agency's overall strategy for reducing costs, which could include discouraging traffic at walk-in office locations or encouraging alternate forums for transactions. As walk-in traffic falls in response to such cost-reduction measures, it typically remains the responsibility of the agency to decide whether to maintain or repurpose current office locations.

An effective SLA model includes a system of credits due to the agency when service falls below expectations and bonuses paid to the service provider for sustained superior performance.

- **Performance and value measurement.** The service provider chosen by the agency will be expected to create metrics and a continuous improvement program. During the transition period, the service provider establishes baselines and verifies current customer satisfaction levels. Service level objectives, once finalized, are defined in the service-level agreement (SLA), and will take effect immediately after the transition period.
An effective SLA model includes a system of credits due to the agency when service falls below expectations and bonuses paid to the service provider for sustained superior performance. Such a system enables both the agency and the service provider to focus on the metrics that matter the most to the agency and on continuous performance improvement. The SLA that guides the engagement also includes annual goals for incremental service level improvements.
- **Transition out.** Nothing is forever. A service provider's goal will be to operate an agency's systems in a manner that meets the organization's goals in perpetuity, but the agency may at some point want to pursue a different service model or partner. As a result, the service model should allow for a careful transition-out plan. Typically, this is a highly orchestrated process that can take several months. The agency must make sure the service provider has effectively transferred all relevant knowledge back to the agency, so that it can once again operate the systems or transition to the new service provider. Such transitions may include pre-defined fees associated with the service provider's support of the transition.

Conclusion

Government organizations that previously preferred to perform IT services in-house are once again considering the benefits of a well-structured outsourcing program to modernize and transform IT and to help refocus on the agency's core mission. If done correctly, an outsourcing engagement can reverse the downward spiral of high maintenance costs and falling IT investment, replacing it with a continuous cycle that funds new investments in IT through cost reductions or new revenue streams. Ultimately, by creating budget to improve IT where none existed before, transformational outsourcing has the potential to make an enduring, positive impact on the ability of government organizations to serve the public.

NTT DATA Services: Your transformational IT outsourcing partner

NTT DATA has experience developing transformational IT outsourcing engagements that succeed in transforming IT service delivery, identifying inefficiencies and funding modern technology, as well as offering a pay-as-you-go model. Our experts can work together with your organization to discuss the opportunities and benefits of a transformational outsourcing model that fits your unique circumstances.

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Ashwini Chharia is responsible for capturing large opportunities using solutions that NTT DATA offers to its public sector clients in the United States. He interacts with executive level clients to understand challenges and provide guidance on solutions and develop strategic IT plans. He provides solution leadership in large-scale pursuits and played an active role in helping NTT DATA win its largest transformational IT outsourcing contract with a state transportation agency. With more than 30 years of IT and public sector experience, Ashwini has held many senior IT leadership positions spanning multiple aspects of IT, including project management, sales, marketing, operations, strategy and innovation. Most recently, Ashwini is lending his expertise to NTT DATA's Smart City initiatives within public sector.

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