The Conference Board

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HR Outsourcing in Government Organizations

Emerging Trends, Early Lessons

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About this report
As Human Resources outsourcing is still a nascent practice in the public sector, this report is designed to present a picture of the drivers, considerations, and experiences of those pioneering organizations.

This report is based on extensive interviews with HR executives at state, provincial, and national government organizations, as well as industry practitioners from the vendor and consultant community. Among the HR executives interviewed are many non-practitioners who had worthwhile insights on the unique considerations of HR outsourcing for government organizations.

About the author
Janice Koch has more than 14 years experience as a writer, researcher, and editor specializing in organizational management, strategy, investment management, and pension-related issues.

A former columnist for *Institutional Investor*, she has contributed to a wide range of business publications, including *Worth* magazine and *Advertising Age*. She creates marketing and corporate communications and research papers for leading organizations and has been editor of the *Balanced Scorecard Report* (jointly published by Harvard Business School Publishing and Balanced Scorecard Collaborative) since 2001.

To contact Janice Koch, e-mail jkwest@att.biz

Additional Interviews
David Dell is the former Research Director of Capabilities Management and HR Strategies at The Conference Board. Dr. Dell has more than 10 years' experience as a research director serving senior executives in multinational companies. He currently heads Sustainable Profitability Group, a research and consulting practice focused on corporate capabilities.

To contact David Dell, e-mail david@daviddell.net

Contributing Writer
Lauren Keller Johnson is a business writer based in Harvard, Massachusetts. Her work appears regularly in *Harvard Management Update*, the *Balanced Scorecard Report*, and *MIT Sloan Management Review.* She is co-author of the *Harvard Business Literacy for HR Professionals* series, jointly published by Harvard Business School Publishing and the Society for Human Resource Management.

To contact Lauren Keller Johnson, e-mail scott-laurie@att.net

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HR Outsourcing in Government Organizations

Emerging Trends, Early Lessons

by Janice Koch, with David Dell and Lauren Keller Johnson

contents

Foreword

Outsourcing is gaining momentum in corporations worldwide. The pros and cons are publicly debated, but I believe that outsourcing—if executed the right way—can produce a win-win situation.

The public sector can benefit from outsourcing in much the same way as has the private sector. Indeed, the public sector is showing a greater impetus in its examination of outsourcing and has pioneered some important contracts. Countries like the United Kingdom and Australia already have gained considerable experience and reaped many benefits.

Outsourcing parts of the HR function can offer many advantages, not in the least to the government employees themselves. Improved communications, faster feedback, rapid problem-solving, computerized training, do-it-yourself HR programs are just a few of the benefits outsourcing can provide. These elements can help improve employee morale and service levels.

But outsourcing is not without its problems. Government has different objectives than the private sector, thus, it cannot blindly follow the private sector's lead. Many elements must be taken into consideration, including political climate, unions, local economies, employment situation, and the investments required and available. Government officials must carefully weigh the potential negative consequences—job loss, skills transfer, unemployment costs, and disruption of local economies—against the promised benefits.

Faced with the necessity of making large-scale investments in new HR systems and upgrading HR processes, as well as chronic understaffing, the public sector must take a hard look at outsourcing before determining the appropriate course of action. I strongly believe that outsourcing carefully chosen HR functions and processes will greatly benefit the government sector and improve its service to society.

In this report, The Conference Board offers a complementary study to its spring 2004 HR outsourcing report, presenting the current thinking and practices of HR outsourcing in the public sector. Surely, the public and private sectors can benefit from each other's experiences, and research bridging both sectors can only further performance.

Ton Heijmen
Senior Adviser on Outsourcing/Offshoring
The Conference Board

Introduction

Few subjects today have garnered the level of public attention and debate as outsourcing and its subset offshoring. Pros and cons have been extensively—and emotionally—debated on the American presidential campaign trail and in the media. Government officials, labor unions, candidates for elected office, reporters, company spokesmen, and academic leaders all have offered viewpoints. Despite its controversial nature, outsourcing has become the latest new way that business is doing business.

Outsourcing involves handing over non-core business functions—generally, IT-intensive transactional processes, though services increasingly are being outsourced as well—to an outside provider. Outsourcing promises to reduce costs, achieve efficiencies, and provide new capabilities that economies of technological scale offer. Advocates tout enhanced productivity, access to latest technologies, and the ability for organizations to free themselves of administrative burdens and focus more on strategic activities.

There are those, however, who voice caution (if not opposition) to what appears to be an irreversible progression toward heightened levels of outsourcing. Opponents worry about job losses—increasingly, those of white-collar, technical, and analytic jobs. They also express concerns about the implications of shifting formerly internal skill sets and institutional knowledge out the door.

Like it or not, outsourcing is not merely gaining momentum; it is already a fixture of modern global business practice in the private and public sectors alike.

Companies have been outsourcing discrete business operations (IT functions such as data and network management) for about 20 years. But today's budgetary pressures and a new business-efficiency mindset that has swept through government have spurred the interest in outsourcing. In particular, more organizations are considering the wholesale outsourcing of integrated functions, including human resources.

Investigating the Trend

In spring 2004, The Conference Board released its findings from a comprehensive survey regarding human resources outsourcing practices among major U.S. corporations.[1] This in-depth study revealed a surprising level—and acceleration—of HR outsourcing among large companies. For example, at least 76 percent of respondents outsource one or more major HR function. Today, only 9 percent have ruled out the practice, versus 23 percent just one year before. Across all industries, large firms are outsourcing multiple HR functions, and none plan to take outsourced functions in-house.

The Conference Board's exploration among large corporations prompted us to investigate HR outsourcing activities in the public sector in the United States. Were the same drivers—avoiding capital investment in technology and improving services—at work? Is there a similar push in government organizations to liberate HR departments from their onerous, transactional processes so they can play a more strategic, value-added role? Does this reflect a broader move to downsize government?

As a nascent practice, HR outsourcing at the national, provincial/state, and municipal levels has generated scant formal documentation and few statistics. We interviewed the handful of trailblazers at the national and provincial/state levels to learn about their efforts and experiences; we spoke with public-sector HR managers and executives who are *not* engaged in outsourcing but who are watching developments closely; and we gained the insights of a few leading vendors. From these conversations, along with available information from the media, we present a picture of current thinking and practice.

Though by no means definitive or all encompassing, this report offers a cross-section of HR outsourcing efforts at various stages and of differing scopes. It discusses the benefits and drawbacks to HR outsourcing in the public sector and the particular constraints and obstacles public-sector organizations face in deciding whether to outsource human resources operations. This study also considers the practical, political, and philosophical issues confronting government administrators who are contemplating this move.

1 Dell, David. *HR Outsourcing: Benefits, Challenges, and Trends*, R-1347-04-RR, The Conference Board, 2004. The survey is based on 122 major U.S. corporations with revenues of $1 billion or more.

Why Outsource HR?

> "We see a tremendous savings opportunity in HR [outsourcing]. If it's not there, we'll walk away."

GREGG PHILLIPS Deputy Executive Commissioner for Social Services, Texas Health and Human Services Commission

While HR outsourcing among government organizations is significantly less common than in the private sector, the rationale for outsourcing is not very different. There are three basic financial drivers behind HR outsourcing:

- Save money (ongoing expenditures)
- Avoid capital outlay (often a more important consideration than direct cost savings)
- Turn a fixed cost into a variable one (Thus, if the workforce shrinks, HR costs can be reduced accordingly.)

Avoiding capital outlay is perhaps the greater concern for public-sector organizations, many of which are operating with decades-old legacy mainframe systems and can scarcely afford routine software upgrades.

From a services standpoint, outsourcing invariably means upgrading to new, often state-of-the art services that provide a better work environment for employees while giving HR executives the tools they need to manage more effectively. These services run the gamut: Employees can learn the status of a paycheck online, sign up for online training via the organization's intranet, file an insurance claim, or download their organization's medical benefits policy from home.

HR administrators get such capabilities as automated payroll—a big plus for government organizations with their primarily unionized workforces and complicated payrolls. Administrators also get a call center that fields benefits inquiries and deals directly with the company's insurance carriers, as well as the ability to conduct online performance reviews and manage employee relocations.

But convenience and cost reduction or avoidance are not the only attractions offered by HR outsourcing. For one thing, outsourcing enables companies to centralize highly decentralized processes that are repeated at multiple locations, through the shared-services model. The resulting efficiencies enhance organizations' ability to hire—and keep—talented workers.

Through technology tools and processes that most public-sector organizations could not afford to build internally, outsourcing can provide improved and more convenient services for employees. This is a particular concern for public-sector organizations, which generally cannot compete with the private sector's pay packages to attract and retain talent.

Outsourcing additionally enables organizations to turn their attention from administration to more strategic efforts. By outsourcing the more rote, repeatable transactions and providing 24/7 self-service mechanisms, HR professionals can devote their time and energy to activities, such as developing leadership skills throughout the ranks, designing rewards programs that support the organization's mission, and helping the executive team define and implement strategy. Moreover, outsourcing puts previously unavailable data in HR professionals' hands, enabling them to analyze and prepare for the organization's current and future needs five, even 10 years down the line.

Government's Unique Triggers

Outmoded IT systems and Byzantine business processes common to government organizations are as much a function of leadership change as they are of insufficient capital. While changes in leadership can be disruptive to any organization, the public sector is particularly handicapped by it, whether from elections or high turnover. The Detroit Public School system (profiled on p. 24), for instance, has had seven superintendents in the last 11 years. And in any public-sector organization, as Stephen A. Hill, executive director for the Detroit Public Schools system points out, each new leadership team means new administrators, new philosophies, and new initiatives. Leadership change can also mean multiple IT platforms, and many of them are legacy systems, which can't connect. The result? Process inefficiencies throughout the organization.

To be sure, many public-sector administrators see the need for reform. But it's difficult for any government organization to reinvent itself single-handedly—no matter how committed it is to the process. Political pressures can prevent decisions that for private companies would be simple, uncontroversial, and cost-effective. As Bill Simon, secretary of the Florida Department of Management Services, notes, "Often it's much easier for us to hire somebody who can reinvent us."

Consider the example of the Ontario, Canada, Ministry of Transportation (MOT), which outsourced its drivers' license exam operation in September 2003—and in the process, reduced the waiting period for an exam from six months to a mere two weeks. Adding more resources is not the only way outsourcers improve efficiencies. Serco Group, the MOT's provider, has greater flexibility to improve service than does its civil-service client. For instance, notes MOT's Ernie Bartucci, working conditions had prevented examiners from traveling to other locations to fill in for absentee employees, which used to add to the backlog. Private companies have no such limitation.

Also, notes Bartucci, procurement rules are more burdensome for government organizations. But a private company can hire any general contractor it chooses—unlike the government, which must issue a competitive tender. These two limitations would have hampered the MOT's ability to make big improvements easily.

Why Outsource Now?

Three forces are converging to fuel the HR outsourcing movement among governments. First, IT systems are reaching the end of their life span. Legacy computer systems, some 25 years old, need replacing. With ballooning deficits and a reluctance to increase taxes, many provinces/states are looking at capital outlays of $80 million to $100 million to replace these systems—expenditures beyond their reach. Unlike with private companies, even financing technology upgrades is impossible for many government organizations, given the rapid rate of technological change and persistent cost-reduction pressures.

Second, the economic downturn that rippled through the global economy in 2002 only added to the problem. The recession created severe budget shortfalls throughout the government sector, particularly in provincial/state governments. Rising deficits threaten government's ability to perform key services, but politicians remain reluctant to raise taxes.

At the same time, a cadre of business-minded government bureaucrats has emerged. These individuals have embraced the private sector's management precepts: efficiencies, technological solutions, customer service, and performance. More and more legislatures and provincial and state government executives are advocating privatization and outsourcing as ways to finance bulging government budgets. And despite the perennial talk of downsizing government, in reality, citizens of all political persuasions recognize that the increasing demands of a growing population mean that government services likely won't diminish. However, these citizens also realize that the pressures to deliver services more efficiently will grow.

Who in the Public Sector Is Outsourcing?

A number of government entities in the United Kingdom, the European continent, and Australia (including the state of Victoria) already outsource their HR functions. For many reasons, the trend has been slower to take root in the United States. One reason is that HR—whether in the private or the public sector—doesn't have the same high-level organizational stature it does in other geographies. Additionally, the public sector in the United States is often perceived as a follower of private-sector business practices than an innovator. This has only recently begun to change as organizations slowly recognize the strategic value of human capital and other intangible assets in today's largely service-based economy.

Beyond a handful of trailblazers (the U.S. Transportation Security Administration, the State of Florida, Detroit Public Schools, and the Texas Health and Human Services Commission) industry experts estimate that another 10 to 15 states are currently actively exploring HR outsourcing—that is, these entities are developing a business case and preparing for any necessary legislative approval needed to make the move.

The Office of Personnel Management, the U.S. government's HR agency, is also weighing the merits of outsourcing HR. In the United States, the trend is likely to center on the federal and state level, since scale is necessary for organizations to realize outsourcing's full benefits and justify its costs. And despite political sensitivities and union resistance, industry players see no abatement of interest from public-sector organizations.

Words of Advice from Overseas

Victoria, Australia, was one of the first in the public sector to outsource its HR functions. From this experience, Department of Treasury and Finance Deputy Secretary Laurinda Gardner has the following suggestions for those in the public sector that are considering the move to outsourcing:

- Be sure senior executives are committed to the outsourcing relationship.
- Recognize that managing an outsourcing contract requires constant work–in managing the provider relationship as well as in devising a well thought-out governance regime that retains flexibility.
- Develop a "contract management manual." Use it to build a knowledge base for what needs to be done so institutional knowledge is not lost when people move on. Allow the manual to evolve over time; it isn't possible to include everything in the first year.
- Expect to invest time continually to keep communicating company needs and issues to the provider.
- Don't jump into outsourcing without being clear about the company's objectives and maturity. The more clearly articulated the priorities, the better off the organization will be.

Based on his experience with HR outsourcing so far, Copenhagen Deputy Chief Executive Jimmy Kevin Pedersen offers several words of advice for other municipalities:

- Clearly define the scope of the outsourcing arrangement, and ensure that the services needed are listed explicitly in the contract. Stipulate the boundaries of the arrangement; make sure it is clear which activities the HR team will continue to be responsible for, and what tasks the vendor will charge extra for doing.
- Prepare a comprehensive plan for communicating with employees about the outsourcing initiative–especially those who will be transferred to a new employer.
- Ensure that top management supports the initiative. Keep executives informed about vendor candidates, costs, and scope of the work.

What Does Public Sector HR Outsourcing Look Like?

"After the [vendor] contract, we started putting more attention into answering the question, 'What do we want out of HR?' We began looking for different services, for improvements over what we'd had."

LAURINDA GARDNER Deputy Secretary of Strategic Management Division at the Department of Treasury and Finance, State of Victoria, Australia

HR departments at the national and provincial/state levels have long hired outside consultants to perform non-routine activities for which their internal staff either lacked the time or expertise. These subcontracted tasks have included analyzing employee data, performing workforce projections (such as a downsizing's impact on payouts), conducting leadership classes, and developing curricula for training programs.

Simplifying Complexities

Now, HR departments are taking the next step toward the bona fide outsourcing of HR processes. These can range from automating payroll or health and welfare benefits administration—the two most heavily transactional processes—to self-administered processes, staffing and recruitment, and even online training and development programs. Among the HR functions and services that outsourcers provide:

- Transaction processing (payroll, benefits)
- Web sites and call centers (employee self-service)
- Vendor management (e.g., dealing with medical insurance carriers)
- HR process redesign
- Service delivery strategy
- Analytics: consolidation of HR information, data warehouse design, performance benchmarking
- Staffing and recruitment
- Designing and building IT infrastructure

Payroll and benefits administration are particularly complex in the public sector—a result of multiple union agreements and the hodgepodge of funding sources. (Some state jobs are federally funded, while some are co-funded by the state and federal government.) This complexity may well explain why government organizations that chose to outsource opted for total outsourcing of any given function versus partial outsourcing, which is more the rule in the private sector.

But such complexities make these functions especially well suited to outsourcing. With some government workforces more than 90 percent unionized, an organization can easily have 10 different benefits packages, the terms of which must all be accurately reflected in employee databases. Many government organizations also have multiple workweek start dates and dozens of categories of leave. Legacy IT systems that don't interact make updating data more onerous and invariably result in costly errors.

Outsourcing services typically include employee help lines (call centers) staffed by people who answer questions and provide problem resolution on demand. This is a big improvement over the old way—in which employees tried to reach, in person or by phone, one of a few overworked benefits administrators. Outsourcing arrangements also include an array of online employee services, such as access to the individual's personal information, plan policy information, and transactional information (like claims status). At the far end, such online services can include training programs.

Example in Practice

Suppose an employee has filed a medical claim and has not yet received the reimbursement check. Instead of seeking out the overworked HR staffer, she can call a toll-free number (anytime, even from home) and get a customer service representative to help track the claim's status. The rep will also follow up with the insurer to make sure the claim processing stays on track.

The employee can also go online to check her coverage. During open enrollment season, the employee and her spouse—at any time from their home computer—can review the many plan options her employer is offering.[2] She can also update her dependents' information online from home. By making employees responsible for updating their data, organizations reduce errors and alleviate delays substantially.

And consider the benefits in staffing and recruitment that outsourcing offers the HR executive. Outsourcing can cut in half the amount of time it takes to fill a position. The vendor registers qualified applicants in advance of the job opening, notifying them electronically when appropriate job positions open. The vendor then prescreens candidates based on qualifications criteria provided by the organization. Next, it manages the ensuing processes, such as background checks, employment verification, and drug screening. By capitalizing on technology and leveraging employee information, outsourcing helps the organization manage and develop its workforce much more proactively than before.

It is not merely the intensive data processing itself that outsourcing makes efficient, but the interaction of *all* HR information. Outsourcing unifies data from disparate sources automatically, either through single enterprise software, middleware technology that links existing systems, or shared services environments. By minimizing manual input, it prevents error and fosters speed. Instead of single, discrete services, the trend, vendors say, will be toward the full-scale outsourcing of all HR services, from payroll to e-learning. Such integration across HR disciplines would provide the ability to anticipate future workforce needs, to identify places where turnover is greatest, to track retirement trends—in other words, to enhance strategic planning.

What Lies Ahead

Learning is probably the big "emerging" discipline among outsourced HR services. Outsourced learning services encompass technology infrastructure (the learning management system) as well as the administration of the system itself, which would be supported through a shared service center. System administration also enables management to assess learning activities, ensure effective training, define job competencies, and so forth.

In addition, the technology enables organizations to store learning content online. While many large government organizations already have such individual systems in place, these systems are rarely integrated. Total outsourcing provides one system and one integrated process for training, learning, and development that can then be integrated with the rest of an organization's HR systems—performance management, job reclassification, and the like.

2 Open enrollment is a period when employees covered under a health plan have the chance to switch to an alternate health plan being offered, or when uninsured employees and their dependents may obtain coverage without providing evidence of insurability.

Structuring the Outsourcing Program

Any organization thinking about outsourcing some or all of its HR function must weigh what can seem like a bewildering array of considerations, including which processes or functions to outsource (should we do a portion of HR—payroll, but not health and welfare benefits?), how to select a vendor, what kind of service delivery model is most suitable, what kind of contract to set up, and how to manage the vendor relationship. Indeed, the decisions can prove so complex—and the stakes so high—that some organizations get help from consulting firms that specialize in this very area.

An important goal of outsourcing is to obtain value-added services, not merely to automate and ameliorate the performance of existing functions. Thus, the decision to outsource requires that organizations consider the future capabilities they'd like to acquire to serve their employees better. And since government organizations generally cannot compete with private-sector compensation, many such public-sector entities see outsourcing as a way to provide competitive amenities and benefits specifically for the purpose of attracting and retaining talent.

Selecting a Vendor: Outsourcing Models

Leading vendors—the providers of bundled, end-to-end enterprise services—come out of the business process outsourcers' world, the IT outsourcers business, and the management consulting business. Other providers include process specialists (known for their expertise in a specific function, like payroll) and emerging mid-market HR outsourcing specialists. Even the largest "one-stop shops" may subcontract specific portions of an outsourcing project to specialists. Independent consultants provide strategic guidance in such areas as whether to outsource, how to navigate the marketplace, and how to structure the deal and oversee the project.

Generally, there are two major categories of service that HR outsourcing vendors provide. The first category is traditional human resources outsourcing (HRO). Vendors that fall into this category have established a common technology platform on which discrete HR processes (e.g., payroll, benefits administration) for all their client companies are run. Known for their ability to provide expanded services and lower costs for client organizations, such vendors seek to regularly enhance their established technology platform to benefit all their clients.

The second category is business process outsourcing, or HR BPO. In many, but not all cases, vendors that provide this category of service take client organizations' existing staff, processes, and technology approaches into their environment but customize their services to work with each client's established technology platform.

Some HR BPO vendors intend to eventually standardize their clients' technology platforms. Moreover, the two outsourcing models are rapidly converging in the marketplace. With the available models in such flux, how can public-sector organizations decide which model is right for them? The choice depends on several criteria:

The timing of outsourcing investments Clients who select a vendor that works from the transaction processing model can expect an up-front "platform migration fee," with relatively small future investments. By contrast, going with an HR BPO vendor can mean a small to no initial investment but possible increases later as the vendor further customizes its services to the client's technology platform. Thus, organizations that have recently made major investments may find HR BPO more attractive. And of course, clients who lack an established platform would do better selecting the HRO model.

Definition of value When the HR outsourcing market first emerged, vendors competed primarily on price and capability. As the market has grown and rivals have proliferated, vendors have begun competing more on functionality—that is, they seek to provide "value-added features" such as workforce analysis, compensation planning tools, and performance management methodologies. To select the right vendor, client organizations must carefully consider which features have value for them and how much they are willing to invest in this value.

Offshoring With offshoring such a political hot button in the private and public sector alike, government organizations must carefully weigh this consideration while evaluating potential HR outsourcing vendors. Public-sector organizations can avoid inadvertently pushing this hot button by:

- familiarizing themselves thoroughly with the laws governing offshoring;
- asking potential vendors explicitly whether they use offshoring; and
- limiting vendors' ability to offshore without their client's consent.

Managing the Vendor Relationship

In addition to selecting vendors, working out the details of an HR outsourcing contract can present daunting challenges. The Conference Board's spring 2004 study of the private sector revealed that most problems organizations encounter can be traced to flaws in the negotiating stage.[3] One common mistake: leaving the negotiating table without instituting an ongoing vendor management process. In general, it is advisable to tap outside expertise, such as legal and consulting, before, during, and after the initial discussion to help define the strategy, manage or renegotiate the contract, and establish service level agreements (SLAs).

Just because the ink has dried on an HR outsourcing contract doesn't necessarily mean that its implementation will unfold precisely as the two parties expect. The seeds of future trouble can be planted in the form of several mistakes that all too many client organizations make while establishing agreements with vendors or in managing the relationship once the contract is put into action. Among the most common errors:

Failure to clearly define the scope of services
Most organizations find it much easier to describe a final product that they want to get from an outsourcing arrangement than to describe a desired service. To avoid misunderstandings, confusion, and tensions down the line, client organizations should create a detailed statement of the work they want a vendor to provide, including which responsibilities will remain with the client and which will fall under the vendor's purview.

Because defining services is challenging, organizations may benefit from obtaining industry standard definitions of services and customizing them to their own needs. Consulting firms that specialize in this area can provide these standards, help customize them, and express service agreements in terms that vendors understand—saving client organizations significant amounts of time.

Failure to manage the vendor relationship proactively
Many client organizations make the mistake of getting overly involved in trying to resolve day-to-day problems as they arise once the outsourcing contract is implemented. This reactivity, or impulse to "put out fires," can suck an organization back into handling the very tasks it is trying to outsource. To avoid this scenario, client organizations need to remember that it's the vendor's job to solve the day-to-day problems. The client's job is to monitor the vendor's performance and manage the relationship to objective standards of service quality.

3 Dell, *HR Outsourcing: Benefits, Challenges, and Trends*.

HR professionals must transition from managing a function to managing a vendor—two entirely different activities. Rather than putting out fires, client organizations should determine how to improve the quality of service they are getting from the vendor. Again, external consulting firms can help by providing vendor-management training, templates for monitoring service quality, coaching, and dispute-resolution services.

Failure to let market competition improve service quality Owing to outright weariness or a commitment to "sunk costs," too many client organizations try to engineer modest improvements in their relationship with an HR outsourcing vendor when trouble crops up. Instead, client organizations should let competition in this expanding marketplace work in their favor. With more and more vendors to choose from, it is easier than ever to replace poor-performing vendors with better ones. Yes, the replacement process takes time, but service quality is more likely to increase throughout this market if clients demand more from their vendors and back up those demands with decisive action, if necessary.

Protecting against risk is obviously important. While practitioners recommend that requirements and expectations (as well as penalties) be spelled out in the contract, some advise against waiting for every last detail to be hammered out before proceeding with implementation. Database preparation, for example, can take months, and if preliminary steps were not undertaken early, an organization would find it impossible to roll out services in a reasonable time frame.

Two other guidelines are worth noting:

Grant sufficient time for the contract period While many organizations may be tempted to seek shorter-term commitments, vendors and government HR administrators alike advise a minimum five-year contract for a complex outsourcing implementation. Seven or even 10-year contracts are not unusual. Developing a multi-service program may take many months, from the handshake to the time the first service is rolled out. Depending on the complexity of the data input, the conditions of the IT systems, and the integration needs, "going live" may take a year or longer. Given all the up-front work invested by both parties, it takes time to see the payoff.

Bring all the weight you possibly can to the negotiating table It's easy for public-sector executives to be outgunned by vendors; often, a vendor's employees are making two to three times what their state counterparts take home. "You put four state workers at the negotiating table with seven [software company] attorneys, and you can guess how that's going to turn out," says Florida Department of Management Services Secretary Bill Simon. He urges government executives to "bring the same gravitas to the table as those [you are] negotiating with" and to maintain it throughout the implementation period and the ongoing management of the vendor relationship.

Constraints and Obstacles to Public-Sector Outsourcing

"We are very controlled by policy and need to live within strict boundaries. It's very different from what happens in corporations."

DICK WHITFORD Associate Administrator for HR, United States Transportation Security Administration

Public-sector organizations considering outsourcing HR processes often face numerous constraints in the form of public sentiment, legislative barriers, and union resistance.

Public Pressures

Slow job growth, particularly in the service sector and among white-collar professions, has raised anxiety levels about outsourcing, in particular, offshoring. Indeed, outsourcing has made front-page news with increasing frequency. To be sure, corporations are just as subject to public criticism for outsourcing as are public-sector organizations.

Yet sensitivities run higher when it comes to government outsourcing efforts. "IBM could outsource, and it'll be a blip on page nine of the newspaper. We [the state of Florida] do outsourcing, and it's headlines," says Bill Simon. "And managing the headlines is certainly difficult because the press will always find an opposing point of view from an opposing party member."

According to Simon, government's position as a big employer—in some jurisdictions, the primary one—is another reason for the intense media scrutiny of Florida's HR outsourcing effort. State government is Tallahassee's main employer, and if a sizeable number of employees were to lose their jobs as a result of outsourcing (this hasn't been the case), they would find few employment opportunities locally. This creates a conundrum: If laid-off employees can't find new jobs locally, the state often ends up paying for them in the form of unemployment insurance, food stamps, or public support. "You end up not actually saving the money, but just spending it out of a different pocket," Simon observes.

In HR outsourcing, organizations realize efficiencies and cut costs through the deployment of processes and technology, not necessarily by "lopping heads." In fact, at the government level, a bigger problem than job loss is chronic understaffing, which prevents HR from performing its functions fully and effectively.

During an election year, political pressures intensify dramatically. So highly charged is the outsourcing/offshoring issue in the 2004 U.S. presidential race that some observers believe that despite the interest in pursuing outsourcing, public-sector organizations fear acting until after the November election. Certainly, federal administrators, as political appointees, may be putting their decisions on hold until they know the results of the election.

The absence of reliable data only fuels passions about outsourcing. The debate about what outsourcing may mean, not only in economic terms, but also to society generally, is complex and nuanced. Simply put, it doesn't lend itself easily to sound bites.

Legislative and Regulatory Barriers

Besides political pressures, legislative barriers (existing or proposed) and practical impediments, such as antiquated constitutions or a rigid budget process, can prevent or stall even the most carefully thought out HR outsourcing effort.

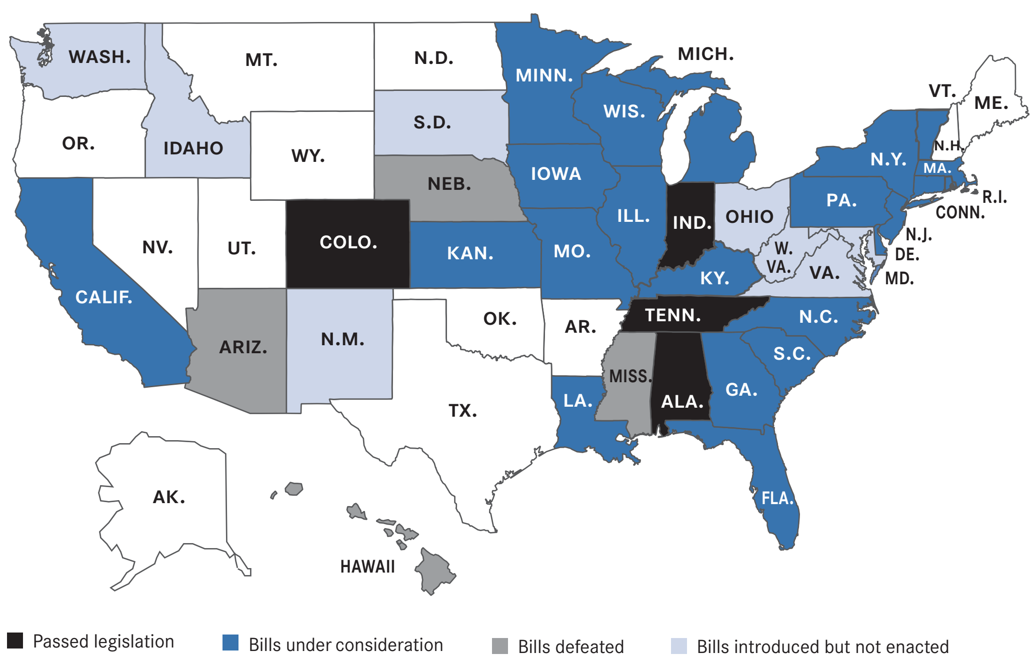
For example, one 1988 California statute forbids counties from contracting out any functions or services already performed by civil employees for cost-saving purposes unless counties obtain statutory authority. The result: Despite deepening deficits, at least some county administrators won't even contemplate the value of outsourcing services or functions because the statutory hurdles are so high.

At publication time, legislatures of 38 U.S. states had introduced anti-outsourcing bills, most of them prohibiting offshoring activities. Every bill, however, has been either killed or so diluted as to be inconsequential in practical terms. Though bills haven't become laws, the efforts have exerted an important impact: Many of these states now include provisions in outsourcing contracts that require work to be outsourced either within jurisdiction or somewhere in the United States. These provisions are designed not only to help prevent the net loss of jobs from the area, but also to keep tax revenues from vendors in local coffers.

The legal barriers aren't always new. Colorado's state constitution, for example, is rife with restrictions in everything from employment practices to procurement rules, according to Kim Burgess, director of HR at the Colorado Natural Resources Department. Burgess adds that state agencies are sitting tight, waiting to see whether the state's Civil Service Reform Act, which would introduce flexibility in hiring and contracting into Colorado's civil service system, will pass this November. The Act would, for example, allow for "competitive sourcing," something the U.S. government and U.S. states like Texas now practice (see profile, p. 35). In competitive sourcing, the internal department is invited to compete against outside vendor bids to retain the service.

Raising Legislative Barriers

Thirty-eight states have introduced anti-outsourcing bills, but none that would significantly curtail the practice has passed.



Colorado: Allows state contract work to be done overseas if a department meets certain conditions.

Arizona: Governor imposed ban on giving contracts to firms that outsource abroad.

Indiana and Tennessee: Each passed a nonbinding "preference" for hiring in-state companies for state contracts.

Alabama: Resolution encourages state and local entities to use Alabama-based professional services.

Source: Coalition for Economic Growth and American Jobs and National Foundation for American Policy

Government administrators who have received the go-ahead to outsource emphasize the importance of getting buy-in from the governor and legislature from the beginning. (See, for example, the State of Florida and the Texas Health and Human Services Commission, pp. 29, 35.) Such support can come in the form of enabling legislation (as in Texas's case) or simply through an endorsement of the move. Lawmakers and officials can help communicate the value of outsourcing to taxpayers, activate support mechanisms for laid-off government workers (such as job placement programs), and promise remedial action if problems arise. In the least, their visible support serves as a check and balance for vendors, who recognize that future contracts depend on their current performance.

The New York City Fire Department's experience shows the downside of weak support. "When we tried to outsource [general functions, not HR]," says Steve Rush, assistant commissioner for budget and finance, "it felt like the whole city was ganging up on us. We were getting it from all sides. [Though] we were charged from the top with trying to [outsource], we weren't getting a lot of support. It was a really frustrating process for us—and for the contractor waiting in the wings. Unless the impetus comes from the top, there is no way to withstand the pressure."

On a practical level, government entities considering outsourcing might want to heed the hard lesson learned by the early adopters. When the state of Florida began organizing employee records in preparation for creating the unified enterprise database, notes Bill Simon, it wasn't always clear why certain tasks or procedures had become so complicated. Simon's team struggled to determine whether a procedure was readily changeable—that is, its complexity derived simply from bad process design—or whether there was some statutory reason for the complexity.

In Florida's case, even if the Legislature was willing to amend a law to simplify the procedure, an amendment would have required additional time—just when Simon was already concerned about the cost of implementation delays. But given the often disorderly state of employee databases, Simon urges administrators to consider researching the underlying procedures before the implementation process even begins. That way, if changes are needed, the organization has time to get the required legislation passed.

Union Resistance

State, county, and municipal workforces throughout the United States are highly unionized. Unions seek to protect the ultimate interest of their members—namely, jobs—and thus vehemently oppose outsourcing. The Web site of the American Federation of County, State and Municipal Employees, for example, provides a template for states looking to propose legislation that opposes outsourcing overseas. According to Steve Rush, when New York City pursued privatization during the late 1990s, labor unions imposed so much political pressure that the City's fire department is now reluctant to consider any major outsourcing projects without compelling evidence of an exceptional return in quality and cost savings.

Such blanket opposition ignores the proven benefits to HR employees who suffer the effects of understaffed offices. The significant efficiencies and improvements that medical benefits administration outsourcing yielded to the Detroit Public School System (see p. 24) demonstrates these benefits clearly: Impossible workloads became manageable and HR employees performed more effectively and experienced greater job satisfaction. All employees gained an efficient, accessible, and responsive benefits administration. Even the unions won: They were relieved of the constant flood of employee grievances as well as the contentious relationship they had endured with education administrators.

Weighing the Concerns

Since HR outsourcing is relatively new territory for the public sector— indeed, the few major efforts are not even completed—the lack of data and performance metrics makes broad assessments of outsourcing's value difficult at this point. A host of questions remain to be answered.

How Do We Ultimately Account for Savings?

How much do implementation delays, which require maintaining the existing system and staff levels, add to the total cost of an outsourcing effort? How often is additional outside expertise required, for example, in the form of an IT consultant to help make changes in the existing enterprise software? And how do these costs fit into the bigger picture? While contracts generally include risk protections such as penalty clauses, exactly how much would an entity need to spend to maintain existing systems while the vendor works out "bugs"?

Without first calculating the cost and value of adding those capabilities and services to existing HR services, how can governments fairly evaluate the cost of a total HR outsourcing bid? Many people assume that privatizing will always yield savings. This notion presupposes "that government agencies are inefficient, whereas in many cases they are actually understaffed," points out New York City Fire Department's Steve Rush. "Outsourcing would definitely improve service levels, but the baseline doesn't reflect appropriate staffing needs." For all these reasons, it may be tough to justify outsourcing on a cost/benefit basis. The cost/benefit analysis indicates you'd improve quality but reduce the opportunity for savings. Such a scenario also allows political opponents to accuse bureaucrats of awarding outsourcing contracts based on favoritism.

What About the Loss of Internal Capabilities?

Some people worry that, by outsourcing entire functions, organizations may be paving the way for future headaches. Over the long term, losing the institutional knowledge—skill sets as well as infrastructure capability—may make it difficult to ever bring the work in-house again.

Total outsourcing may end up putting government organizations in a vulnerable position. Specifically, they might have to pay up without choice—by being forced to either outsource forever or rebuild internal capacity if they decide to stop outsourcing.

How Do We Place the Displaced?

While taxpayers expect fiscal prudence and efficiency in government, the lack of a profit motive in government makes the public more critical of job layoffs from government entities. Government administrators understand well the need and moral obligation to do their utmost to help place laid-off workers elsewhere—in other government agencies, in the private sector, or even with the outsourcing provider.

For some displaced public-sector employees, the private sector may offer a more interesting, challenging, and lucrative career path. Outsourcing companies claim that these workers, with their knowledge of the client organization, can be very valuable. Such vendors often speak of efforts to absorb workers effected by the outsourcing. But when the outsourcing initiative is over, how permanent are those jobs?

Are We Forfeiting Government's Role?

It's one thing to contract out transactional processes to specialists who can afford to maintain the latest technologies; that's economy of scale in action. Some public policy observers, however, worry about the wisdom—and the ethics—of exporting functions such as program design and decision making to the for-profit sector. This is a particular concern in social services.

The question, perhaps not only for government executives, but also for society, is, does it matter for HR?

The Outlook for HR Outsourcing in the Public Sector

"We will always be willing to outsource a support function if the market can do it better and cheaper."

JIMMY KEVIN PETERSON Copenhagen Deputy Chief Executive

In the private sector, which is often the trendsetter, HR outsourcing got a slower start than the outsourcing of other functions. That is partly because HR is often last on the list for transformational initiatives—even though its responsibility for intensive transactional processes makes it a perfect candidate for outsourcing.

Although The Conference Board's earlier study indicated that cost savings is still the greatest driver for outsourcing HR in the private sector, companies recognize that HR's ability to devote itself to strategically important activities is one of outsourcing's big benefits. And while freeing HR personnel to engage in strategic work (workforce planning, training, and benefits structuring) is of equal concern to private- and public-sector employers, it is especially important in the lower-paying public sector for competing for talent.

But beyond the HR department's role in advancing HR outsourcing, certain forces had to come into play—namely, IT system obsolescence and chronic, widespread budget crunches—before executives began taking a serious look at outsourcing HR. And as steeply rising employee benefit costs continue to strain organizational budgets, executives will likely increasingly look to outsourcing for cost efficiencies in administrative areas.

These same forces, of course, affect the public sector and have thus prompted more and more government organizations—increasingly efficiency-oriented and sensitive to taxpayer wallets—to consider HR outsourcing. And they are not likely to disappear anytime soon. Public and political pressures might easily slow the expansion of the practice. As one vendor pointed out, "The political environment is so polarized that you may find in any given state there are as many people hoping the organization will fail as there are working to see the effort succeed. All it takes is for one high-profile initiative to fail or not do well, and everyone can point to it as an example of why not to [outsource]."

Case Studies

Examples of HR outsourcing in the public sector are few, but the lessons learned by any organization about such an ambitious endeavor can be valuable to readers.

The following trailblazers, all of whom are outsourcing multiple HR functions, are listed in chronological order of implementation; Victoria, Australia, among the first in the world, began its outsourcing effort in 1996, while Texas Health and Human Services is (as of summer 2004) just beginning to implement what will be the first of a long list of outsourced functions. It's worth noting that beyond their jurisdictions, these organizations' outsourcing experiences are little known.

State of Victoria, Australia

Detroit Public Schools

U.S. Transportation Security Administration

State of Florida, Department of Management Services

City of Copenhagen, Denmark

Texas Health and Human Services Commission

State of Victoria, Australia

Number of state employees 1,100 initially (two agencies); 1,800–2,000 today (three agencies)

Outsourcing began 1996

HR functions outsourced Payroll, HR information systems and reporting, HR policy

Cost savings realized 30 percent

Though as business-savvy and sophisticated as a government organization in any industrialized nation, Australia's government might nonetheless seem an unlikely global innovator of organizational processes. Yet in HR outsourcing, Victoria State's government is one of the world's public-sector trailblazers.

In 1996, Victoria's government defined an assertive new goal: Stabilize and revitalize the state's then-flagging economy. As part of its strategy for achieving that aim, the government committed to a program of privatization and outsourcing aimed at reducing cost and increasing efficiency and effectiveness.

That same year, Victoria forged a five-year, A$ 8 million (U.S.$ 5.5 million) contract with a vendor to deliver a broad range of HR and payroll services to the state government's two central agencies: the Department of Premier and Cabinet (DPC), and the Department of Treasury and Finance (DTF). Together, these departments totaled about 1,100 staff. Yet they each had separate human resource and business priorities and contrasting work practices. Outsourcing would fulfill the goal of establishing a shared-services arrangement between the two departments in IT as well as in HR.

Expanding the Scope

In 2001–2002, the departments expanded the scope of the HR outsourcing initiative to include additional HR processes and services, specifically:

- HR policy;
- enhanced HR information and reporting; and
- an HR portal that includes a self-serve kiosk and more advice and "value add" for managers.

Previously, some services, such as performance management and learning and development, concentrated on administration, not professional advice and assistance. But they have since become more important, according to Laurinda Gardner, deputy secretary of the Strategic Management Division at DTF and the designated head of the outsourcing contract. "After the contract, we started putting more attention into answering the question, 'What do we want out of HR?' We began looking for different services, for improvements over what we'd had."

The contract also was extended in 2003 to include a newly established state agency: the Department for Victorian Communities (DVC). Set up in December 2002 to deliver better services and infrastructure for Victorian communities, the new department supports the state's mission of "growing Victoria together." In July 2003, the vendor began coordinating DVC staff from six separate payrolls, with six different terms of employment, into a single payroll system.

While the three departments share the HR contract, each one has its own HR department with its own needs. And each is involved in managing the service provider. Initially, Victoria managed the contract from a separate area, but this centralization made “people lose a sense of ownership,” Gardner notes. Today, each department has its own HR liaison.

Achieving Advantages

Through its HR outsourcing initiative, Victoria’s government reduced costs for the three departments by 30 percent—the result, Gardner notes, of the combined efficiencies of a shared-service structure and outsourcing. The government also reduced errors and enabled managers and employees to access information more quickly and conveniently. Several services made these achievements possible, including:

The Contact Management Centre This “one-stop” shop provides a single contact for all HR-related communications, questions, and requests from employees, and consolidates the departments’ HR-management skills and knowledge.

myHR@DPC and myHR@DTF These Lotus Notes-based portals enable each staff member to gain access to all HR-related information and services from their desktops.

Employees can view policies, access departmental information, complete HR forms, and learn about professional development opportunities. Meanwhile, access to policies, tools, reports, and up-to-date details about staffing enables managers to oversee workforce performance and plan staff development online.

Besides achieving its explicit goal of offloading transactional processes to concentrate more on strategic tasks, Victoria has gained the “freedom to do more new things,” says Gardner. The HR departments now can experiment with new initiatives, such as expanding their recruitment of college graduates or developing an intern program. “Once we are sure what we want, we can turn it over to our provider.” In addition, Victoria gets independent HR advice and benefits from the global experience of its provider.

Equally important is the discipline of documentation and data gathering that outsourcing has brought. By documenting the services it receives from its provider, the government now has a clear idea of what tasks it performs and those tasks the provider performs, thus making total costs more visible. As part of its contract, Victoria benchmarks its vendor’s performance externally to ensure it is competitive in quality and price.

But beyond its performance data, the vendor produces valuable data on the HR departments’ performance. For example, when Victoria wanted to identify the causes of high turnover in DTF, HR asked the vendor to analyze the qualitative data it gathers from its exit interview and outplacement support services to provide analysis and insight.

Detroit Public Schools

Detroit population 950,000

Detroit Public Schools ranking Among the nation's top ten largest public school systems

Students enrolled (K-12) 150,000

Number of employees 26,000 (largest employer in Detroit)

Percent union members 96%

Outsourcing began February 2001

Implementation completed January 2002

HR functions outsourced Medical benefits administration

Direct savings realized $5 million initially; $1 million per year

As with many aging urban or industrial cities, Detroit's decades of decline have saddled its public education system, the nation's eighth largest, with a disappointing legacy: a crumbling infrastructure; a 25 percent drop in student enrollment over the past decade; a 50 percent functional illiteracy rate among the city's adult population; and a $70 million deficit exacerbated by the loss of state funding whenever a student drops out, switches to private school, or moves.[4]

The economic downturn that struck the nation in the 1990s only intensified the city's budget crunch. After a string of unsuccessful public education reforms over the years, educators realized that policy reform without fiscal reform was not enough. It was time to borrow from the corporate playbook: Seek efficiencies and accountability, and give school administrators the flexibility to make executive decisions that could exert a big impact—a mission embodied in the public education initiative called "Redefining Reform."

So when Stephen Hill joined the Detroit Public Schools (DPS) system as its executive director of risk management in 2001, he wasted no time in pursuing one of the district's vital goals: being a data-driven, efficient, and effective organization. Hill's first step? Overhauling DPS's employee benefits administration.

The High Cost of Errors

In particular, DPS's medical plan administration was very complex. With four different, non-integrated databases for HR, payroll, finance, and benefits, there was no reliable headcount of insured employees. Indeed, the tally varied every month by as many as 300. Four staffers were responsible for maintaining employee benefit information, manually processing information on 26,000 employees and their 25,000 dependents.

Sixteen unions, with 22 separate bargaining agreements, represented this 96 percent unionized workforce. The variability in benefits was huge, as was the margin of error. Carriers, for their part, were suffocating under mounds of paperwork, aggravated by DPS's inefficiencies and inaccurate information. One irate carrier slapped the district with late fees totaling $350,000 a year.

4 Enrollment dropped from 200,000 to 150,000. Over the past 20 years, enrollment has fallen 50 percent, from 300,000 to 150,000.

And because insurers had no confidence in DPS's head-counts, they inflated the numbers to cover themselves. "It was costing us an additional $5 to $6 million a year in premiums for employees who shouldn't have even been in the plan or who were placed in the wrong coverage categories," Hill points out. For employees, the medical plan's hit-or-miss nature was "like the lottery. We didn't know whose Blue Cross card would actually work when they went to the emergency room at 2:30 in the morning," says Hill.

Employees routinely were bounced back and forth between the benefits office and insurance carriers, each of whom would contend that the other would have an answer for them. This breakdown had been "going on for decades," notes Hill, eroding unions' trust in the system's administrative abilities.

To set things right, Hill decided the best option was to outsource benefits administration.

Making the Business Case

Initially, Hill built the business case to present to the system's financial team: the CFO, the Senior Deputy CEO, and CEO. Hill knew that the cost of outsourcing medical benefits administration processes would have to pay for itself—and, in the process, provide significant benefits. He demonstrated that the expense would immediately reduce existing expenses by between $3.5 million and
$5 million by eliminating the exorbitant late fees and administrative costs; eventually, it would enable DPS to negotiate competitive plan rates. CEO Kenneth Stephen Burnley and the financial team gave Hill the green light to sign a five-year, $12.5 million vendor contract.

Implementation: Scrubbing, Building, Testing, Training

Next, Hill examined all the information in the system to get an accurate accounting of employees and their benefits, based on their union affiliation and eligibility. Working with his Risk Management team, as well as representatives from benefits, labor, finance, payroll, HR, and the vendor's project management team, Hill organized, scrubbed, and checked data. In the process, the district added online open enrollment, COBRA, and flexible spending options—new administrative options for employees that gave them the ability to make choices and changes on their own.

As expected, assembling and scrubbing all the employee records took about five months. With comprehensive, accurate data, the vendor was now ready to load the information into one enterprise database. But the systems of all the players (the vendor and the insurance carriers) needed to interact seamlessly. The vendor team therefore made multiple IT system tests to ensure that information could be downloaded to all key parties and that the Web-based interaction between it and insurers worked properly. Some programs had to be written to ensure that the interfaces functioned correctly.

It was then time to educate the vendor's customer service team—the call center representatives who would field employee problems and questions—about every aspect of insurance coverage relating to DPS's 16 unions and multiple carriers. Extensive training included learning the various policy provisions and procedures of each insurer. Representatives learned how to get answers to employee questions and learned strategies for resolving employee problems as promptly as possible.

With the DPS team's guidance, the vendor also developed other communications media, including a Web site, a voice response system, and booklets that provide plan information, allow employees to make changes in their information and coverage, and enable them to get answers and resolve problems.

The unions, Hill says, were “apprehensive” about outsourcing at first, mostly because of DPS’s poor track record in handling employee claims and problems. Job losses weren’t a concern; the DPS benefit team was woefully understaffed. “In fact,” adds Hill, “we were able to demonstrate that these employees . . . would enjoy a better core service responsibility.” Specifically, they would be relieved of the impossible administrative burden they were once forced to shoulder. As soon as union leaders understood the new system and, in particular, the new benefits employees would receive, they became converts.

DPS’s implementation may rank among the most complex—thanks to the many unions, multiple constituents, and the politics of Detroit and its school system. Yet the district managed to meet its aggressive timetable and “go live” just eight months after starting this project. For an implementation of equal complexity, the process normally would take 12 to 15 months. By January 1, 2002, the new IT system became accessible 24/7: Web access now enables employees to retrieve all their eligibility information, check the status of their claims, compare plans, switch carriers, and change dependents. E-mail inquiries are answered the next day.

To track employee perceptions of the new system, the system records all calls between employees and the vendor. Each month, a third-party firm randomly selects 10 percent of the telephone calls for follow-up, including contacting the employees for feedback. As a “data-driven” school district, DPS can later show these satisfaction rankings to union leaders and other stakeholders.

Big Savings, Newfound Credibility

The cost savings that Hill initially projected for his finance team proved right on the money: So far, DPS has saved $5 million from the initial data cleanup and $1 million each year in carrier overpayments. Together with eliminating onerous late fees, DPS has cut 4 percent off its annual health insurance costs. Premium payments, wired directly from the vendor, are remitted in 48 hours versus the 90- to 180-day cycle of old. Now a prized customer of insurers, DPS has negotiated premium increases 7 percent below the average (now 13 percent versus 20 percent)—an impressive feat at a time when medical insurance costs have skyrocketed. As Hill says, “By becoming a better client, we are a lot less costly to do business with.”

DPS’s benefit-plan costs compare impressively with those of other Michigan school districts: Total annual benefit costs (health, life, dental, and vision) average $7,500 per employee versus $14,000 elsewhere. Health insurance coverage alone averages less than $5,500 per employee each year.

Moreover, union-management relations have vastly improved. With its credibility restored, DPS now has greater bargaining power in labor negotiations. And by improving customer (employee) service, DPS has alleviated the number of benefit-related grievance calls unions would normally receive. The district’s relationships with insurance carriers also have improved dramatically.

The four staffers who used to handle every phone inquiry from the district’s 26,000 employees have been relieved of that burden and can now handle planning and strategy-related activities, such as staffing, recruitment, and training.

DPS’s experience with medical benefits outsourcing has proved so positive that the district is considering outsourcing other HR applications, such as payroll-related information processing (e.g., changes in employee location or job classification and workshop attendance). Already, DPS outsources property claims, and it is considering doing the same with risk-related business processes, such as claims administration and training for emergency-preparedness and Homeland Security Department initiatives.

U.S. Transportation Security Administration

Origin Created on November 19, 2001, when President George W. Bush signed into law the Aviation and Transportation Security Act (ATSA), which established the Transportation Security Administration (TSA) within the Department of Transportation; TSA is now part of the Department of Homeland Security.

Mission "To protect the nation's transportation systems to ensure freedom of movement for people and commerce."

Employees 55,600 passenger and baggage screeners hired by December 2002.
Since December 2003, TSA has had 45,000 full-time equivalent screeners, as directed by Congress.

Budget $5.3 billion requested by President Bush for FY 2005.

Outsourcing began At TSA's inception

HR functions outsourced Total

Estimated cost savings through outsourcing 20–25 percent

Established through the Aviation and Transportation Security Act just two months after the September 11, 2001, terrorist attacks in New York, Washington, and rural Pennsylvania, the U.S Transportation Security Administration (TSA) has faced enormous time pressure to fulfill its mission of protecting the United States' transportation systems. Thus, it's perhaps not surprising that the TSA has outsourced the majority of its HR functions.

In addition to outsourcing recruitment, assessment, and selection of new hires, such as passenger and baggage screeners and executive staff members, the TSA has established contracts with vendors to provide training and development as well as to handle employee relations, health insurance, and employee assistance programs. It does all its outsourcing through four major contracts.

During its initial buildup in the summer of 2002, the TSA hired about 5,000 people every week. It was, in fact, "one of the largest ramp-ups in government since World War II." Today, the TSA can get new screener hires to their first day on the job just 60 days after placing a recruitment ad. Though this two-month time frame may leave some private-sector organizations unimpressed, it's dramatically superior to the federal norm, which can be as long as 120 to 180 days.

What explains the speedy implementation of such a comprehensive outsourcing program? As TSA Assistant Administrator for HR Dick Whitford explains, "We did not have cultural barriers or an existing HR office that might be very resistant to outsourcing—especially in an organization of this size. We bypassed [the experience] of, for example, going to shared services. We had the flexibility and the legal authority that other [government] organizations do not have." In these respects, the TSA's experience differs markedly from that of other large federal agencies.

To make this vast outsourcing program work, TSA managers and employees had to develop a specific set of competencies—particularly in the areas of program management, contract management, and quantitative analysis. And according to Whitford, vendor-relationship management has become another vital skill set. "Our providers knew how to map out work and maximize repeatable processes," he says. "But they lacked expertise in the world of HR in the context of federal civil service—which is all very codified and regulated." For government employees, everything about their term of service with the federal government must be documented in specific ways in personnel records. "We are very controlled by policy and need to live within strict boundaries," Whitford explains. "It's very different from what happens in corporations."

During the first two months after the TSA began operating, employees faced many challenges. Some new employees of this new agency had difficulty navigating the uncharted waters of pay and benefits problems, and, in many cases, the TSA had to lean on its contractors for support. “The provider has had to come up to speed on these processes,” Whitford says. The TSA’s unavoidably massive and rapid ramp-up, which included evaluating an estimated 1.7 million job applications during 2002 alone, spawned other, more disturbing problems as well.

In February 2004, an internal investigation at the Department of Homeland Security (of which the TSA is now a part) revealed that the TSA erroneously hired screeners with questionable backgrounds and individuals who were less than forthcoming on their job applications. The TSA took swift action to ensure that a workforce that meets the highest standards are on the job and subsequently fired about five percent of its workforce for these problems. Moreover, some screeners were allowed to remain on duty at security checkpoints for weeks or months after discovery of their criminal past. In 2003, the TSA fired more than 1,900 screeners after background checks found criminal records, deceptions on job applications, and other problems. According to David Stone, the TSA’s assistant secretary, the agency has since taken steps to strengthen hiring procedures to ensure that “airport screeners are second to none.”

To ensure better service from the TSA’s HR outsourcing vendors, Whitford and other TSA officials meet three times each week with all the organization’s providers. The agency introduced performance metrics into the vendor-management process and goes through “a real budget exercise with vendors each year [to] keep us focused on getting improvements,” Whitford says. “Because we are a government agency, we have an extended contract that has to be renewed and re-approved every year. . . . A multiyear contract gives us the stability we need,” while the yearly budget exercises enable enhancements in service quality. More “meaningful” service-level agreements further reinforce the importance of service quality—for example, guaranteeing that employees receive a callback and satisfactory response within 24 hours, as opposed to a guarantee that all calls are picked up by the third ring.

The TSA isn’t the only federal agency that must grasp the importance of vendor management. “Anyone who believes that the contract signing is the end of the process is fooling himself,” Whitford maintains. “Federal people need to understand that there is real work to do in cooperating with vendors. You [must] not only solve the problem of the moment, but also build a repeatable process.”

Though Whitford says the TSA does not have detailed data on what its costs might have looked like without outsourcing, he believes that outsourcing has gained the agency cost savings of about 20 percent. He uses additional criteria to assess the benefits of HR outsourcing. For instance, the agency’s vendors have helped provide the information the TSA needs to respond to oversight questions from the Office of Management and Budget, the Department of Homeland Security, congressional committees, and other government agencies. Also, he cites vendors’ speedy installation and ramp-up of software applications that provide needed value in the form of faster records processing and automation of staffing and payroll. Vendors get these applications up and running in “a couple of months instead of a couple of years,” Whitford notes.

So what might HR outsourcing at the TSA look like in the future? The earliest stage of the effort focused on staffing up. Next came “putting the house in order”—for example, streamlining HR processes, such as mailing employees health-benefit cards and handling hundreds of thousands of documents that didn’t exist in the past. According to Whitford, these achievements established a “brain trust that [has helped] us to move forward. Now we are trying to work out how [our vendors] can help us [improve our] internal governance and strategic planning while we rely on them for basic staff.”

State of Florida, Department of Management Services

Population (2000) 16 million (fourth-largest state in United States)

Population growth (1900–2000) 24%

Number of state employees 118,000 (with university system employees, 189,000)

Department budget $400 million (administration), $1.1 billion (benefits)

Outsourcing began August 2002

Expected completion date September–October 2004

HR functions outsourced Total

Targeted cost savings $173 million over seven-year contract

Three years ago, the IT system supporting Florida's human resources functions was on its last legs. Like most government IT systems, it consisted of a patchwork of legacy systems that not only were aging, but also couldn't talk to each other. Replacing the system, however, would cost the state a staggering $80 to $100 million up front. Though Florida had escaped the worst of the nation's economic downturn (the state has led the United States in job growth for the past two years), an expenditure of that magnitude was clearly out of the question.[5]

The very factor that one might attribute to Florida's robust economy—its pro-business environment—is also what made state executives consider outsourcing. State officials quickly took note of the growing outsourcing movement in the private sector. And with the support of the Governor, they presented a proposal to the Florida Legislature. After some debate, the state's House and Senate approved the move.

A lot was at stake. This would be the largest state outsourcing initiative anywhere in the United States, affecting 118,000 state workers throughout 28 agencies. Florida adopted a comprehensive HR outsourcing effort—dubbed "People First"—that encompassed everything from staffing, hiring, and open enrollment to employee assistance, payroll, and benefits administration.

State administrators launched an invitation-to-bid process, which, unlike the standard request-for-proposal process, seeks the best solutions, not necessarily the lowest bidder. Although heartened by the relatively big response (six vendors), they soon discovered that no vendor had experience with a major public-sector outsourcing effort on a scale anywhere near what they were seeking. In fact, so new is total HR outsourcing that many respondents' proposals stipulated that the vendors would need two to three years to launch certain functions.

Florida chose a vendor with private-sector experience, and by August 2002 (some six to eight months after initiating the idea of outsourcing), the state signed a $293 million, seven-year vendor contract.

5 Press release, Florida's Agency for Workforce Innovation, April 2004.

Uncharted Waters, Hard Lessons

As executives at the Department of Management Services (DMS) structured the sweeping initiative, they decided to stagger the implementation, rolling out more straightforward functions, such as staffing and hiring, first. This initial "module" includes a vendor-managed Web site containing employment and job postings. The vendor screens job applications in accordance with state or agency criteria and then passes them to the relevant agency for review. Once the applicant is hired, the vendor provides the newcomer with many details from the "on-boarding" package.

Open enrollment, as well as employee assistance programs (in the form of a referral hotline), was also launched early on. According to DMS Secretary Bill Simon, all of these functions were relatively simple to roll out, partly because they represented entirely new services with no employee data yet accumulated.

The final, most complex outsourced functions (payroll and employee database management) were rolled out in May 2004. For several reasons, these implementations proved difficult and suffered delays. Challenges included the disparate operating processes and procedures from agency to agency. The thicket of statutory and union requirements made for a dizzying number of data inputs. The vendor, new to the public sector, had not anticipated such intricate rules and processes.

To illustrate, about half of all state employees is on a biweekly payroll, and the other half is on a monthly pay schedule. Federally funded jobs have a Monday workweek start, state-funded jobs have a Friday start, and jointly funded jobs (such as military affairs) have a Monday noon start time. And there are 51 varieties of leave, including one variety of paid leave for employees who are selected for athletic duty, such as the Olympics.

This proliferation of classifications is the result of decades of statute written upon statute. The state really needed just three categories of leave—"paid," "unpaid," and "other"—notes Simon, but his team was unable to make that change without legislation. The 11 collective bargaining agreements with unions (and the multiple requirements contained within them) also complicated data gathering. While multiple union agreements are a fact of life, the statutory complexities are not irrevocable. "If we had [requested legislative changes] in the first place, we would have been able to make the implementation go a lot quicker," says Simon.

Employee database management takes a paper-based process involving data entry by an HR staffer into a mainframe system and transfers that responsibility to employees for online entry (e.g., current address, deductions, and other personal information). Employees also input their timesheets electronically and transmit them to their manager, who forwards the electronic file to the payroll department for processing. But as with payroll, this portion of the implementation had its problems, too: "A simple thing like employees managing their own addresses presumes that we have their correct addresses to start with," observes Simon. In a manual-entry world, it's easy to imagine the difficulty of maintaining updated information on 118,000 people.

These headaches led Simon to draw several important lessons. First, both the state and the vendor initially understaffed the outsourcing effort. IT managers should have been involved in the planning process, not just the HR team.

Second, Florida's initial nine-month timetable for a "big bang" rollout of payroll services proved unrealistic; nine months would be considered aggressive for a one-unit private-sector company, let alone a 28-agency public-sector entity, Simon notes. Data entry and fact checking turned out to be monumental endeavors.

Third, the rationale for certain agency procedures wasn't always clear, and Simon's team struggled to determine whether a problematic procedure stemmed from a statutory requirement or was readily changeable. "The transformation of the processes needs to happen before the implementation," Simon contends. "Before you launch into writing code and all the things you need to do to automate a payroll, you need to have a thorough, top-to-bottom review of all the processes so you can root out what's required, what's desired—and then write your code to the new processes, not the old."

Finally, like most public-sector organizations, the state lacked the level of IT expertise needed to resolve complex data issues in-house. (Typically, outside IT consultants built the mainframe systems and install software, and the administration's IT department maintains it.) As a result, the state had to hire outside IT consultants to help it manage the vendor through the complexities of IT implementation.

Coping with the Job Loss Issue

Florida executives were not unmindful of the political sensitivities surrounding outsourcing, particularly potential job losses. These concerns surfaced in the beginning and remain at the forefront of the public's attention, especially as the presidential election campaign heats up.

For one thing, the press and public often confuse outsourcing and offshoring, the cross-border variety of outsourcing. It is nearly impossible to outsource government services offshore—"You can't do toll collections from India," Simon quips. Most of the services the state government provides are to its citizens, he notes. They, by definition, reside in state and thus necessarily receive those services within the state boundaries.

Working in Florida's favor is its sound economy; it has led all states in job growth for two years. It also has been a net "insourcer" of jobs; the healthier job environment has helped mitigate the degree of public opposition other states are facing as they consider outsourcing.

Nonetheless, by the time Florida's HR outsourcing effort is complete, approximately 900 employees will have been displaced. Both Simon and the vendor emphasize their early, proactive effort to address job cuts:

- Many laid-off employees are eligible to retire.
- The state helps place others in jobs elsewhere in state agencies.
- Still others are offered positions with the vendor.

Thus far, no DMS employees have become jobless; they have either retired or were reassigned, notes Simon. Florida's contract with the vendor, in fact, stipulates that outsourced jobs must stay within the state. Thus, for many displaced employees, their employer will have shifted from the government to the vendor. In fact, as of June 2004, DMS's vendor had hired 24 state employees, and it expects to hire more.

In Florida's case, sensitivity to job losses perhaps runs deeper than it might in other places. Why? The biggest employer in Tallahassee (one of two outsourcing locations) is the state government. Unlike larger, more economically diverse capital cities, such as Atlanta, Georgia, there aren't many places outside of the government for laid-off workers to find new employment.

Nonetheless, Simon views these changes as a welcome redefinition of civil service. "Good people who work hard and deliver good value will always have a job and shouldn't worry," he says. "The concept of a state job as a tenured role is over. People need to understand that their job, like every other job in the United States, is a competitive position. They need to perform well every day to maintain it."

Countering any job losses, Simon points out, is a beneficial multiplier effect that many opponents of outsourcing overlook: When the state performs a service, the money trail ends at the employee's paycheck. But when that same money is spent on an outsourcing contract, the outsourcer pays taxes on its profits, thereby fueling the local economy.

"Ready, Aim, Fire. . . . Aim Again . . ."

Florida expects to realize approximately $173 million in savings over the life of its vendor contract. The first $85 to $90 million represents cost avoidance (from not having to buy a new IT system) and has already been realized. As for the rest, time will tell.

And though HR represents its pioneering effort, Florida's outsourcing program doesn't stop there. The state is outsourcing an ambitious array of services, including management of its welfare and Medicaid payment programs, food service and healthcare in state prisons, toll collections, and professional licensing programs (such as real estate licensing). It also has moved the state procurement function to an e-commerce system, replacing the old paper-driven bid system.

Florida's vendor contract stipulates detailed performance standards and measures, which Simon considers necessary but sometimes limiting. Contractual protections (e.g., specifying service delivery dates and penalties for delays) are critical, but at the same time, it's important to build flexibility into the implementation process. The outsourcing process, he says, doesn't happen strictly as it is defined on paper, and you don't want to constrain yourself. These projects aren't a matter of "Ready, aim fire," Simon notes. "It's more like 'Ready, aim, fire. . . . Aim again, fire again, aim again. . . .'" Often, adjustments need to be made throughout the process. For example, once essential capabilities may no longer be necessary. In such cases, the contract will need to be amended instead of Florida continuing to pay for those capabilities.

The delays Florida experienced not only added costs (maintaining the old system for longer than expected), but also added to employee workloads (operating with reduced personnel while awaiting the new services). But the administration also has come under fire for its contracting process. Simon points out that such failings are basically the result of an overly aggressive timetable. Legislatures and the public, he adds, are very forgiving of government employee inefficiencies, but they hold private vendors to a much higher standard.

To address these problems, Governor Bush recently established the Center for Efficient Government within DMS and appointed Simon to oversee all of Florida's outsourcing programs. Simon and his team will track progress on each outsourcing initiative, ensuring that the business cases are developed with consistency, that the procurements are handled properly, and that contracting and monitoring receive adequate oversight. Simon will issue an annual report to the governor and Legislature on progress against goals. In addition, consolidating the outsourcing lessons acquired by various agencies will help all future efforts proceed more smoothly.

Simon, one of the new cadre of government bureaucrats who brings a performance mindset from his mostly private-sector experience, believes that state government ultimately is obligated to deliver efficient, effective services for its citizens—however that happens. "We should forget outsourcing as a concept," says Simon. "We should look at what is the best, most efficient way to run any particular state task or function. And in many cases, the answer will be 'keep it internal.'"

City of Copenhagen, Denmark

Number of city employees 60,000

Outsourcing began 2003

HR functions outsourced Payroll, HR information systems (HRIS), online employee data, and benefit plan information

Targeted cost savings $8.5 million over first five years

Just as HR outsourcing raises unique questions and challenges for private-sector versus public-sector organizations within the United States, it can have different ramifications across continents as well. As one of the first municipal entities in Europe to outsource HR, the city of Copenhagen can offer valuable lessons for other government organizations—in Europe and the United States alike—that are considering outsourcing HR.

The Promise of Synergy

City officials first began considering outsourcing HR in Copenhagen in 2002, when the municipality's existing payroll system was about to be phased out and replaced with a new HR information system (HRIS). At that time, Copenhagen Deputy Chief Executive Jimmy Kevin Pedersen says, "We decided that the new system should include some HR management as well."

But the system was expensive, and the city had no budget for it. To avoid burdening taxpayers—as well as maintain existing service levels at a lower cost—the city "issued a tender for a combination of payroll and new HR IT, as well as implementation of the new system." Resulting synergies, officials hypothesized, would enable Copenhagen to afford the new system. The resulting arrangement transferred 100 of the city's 108 HR staff members to a new company that handles 635,000 transactions involving 60,000 active employees with 180 types of pay agreements—and pension administration for 25,000 retirees. An integrated subsystem processes time and attendance records.

From Baseline to Benefits

One way to assess outsourcing's payoff is to establish a baseline against which to compare costs before and after outsourcing. Two years prior to the HR outsourcing initiative, Copenhagen created a shared-service center for payroll that eventually provided an opportunity to define a baseline.

Specifically, the payroll center sought to operate as a profit center by sending invoices to clients in other city departments. This process enabled the city to calculate the costs of various services, such as producing a salary statement. Overall costs formed the baseline for evaluating savings gained from outsourcing. In Copenhagen's case, these savings amounted to $8.5 million over five years—enough to pay for a new Oracle-based HRIS.

Outsourcing yielded other benefits as well. For example, the new system enables employees throughout the municipality to access data online, such as personal information and benefit plan information. This change freed the HR function from having to input and update data, as well as answer employees' questions. Now the HR staff can focus on enhancing HR practices—a much more strategy-oriented effort than it had time for prior to the outsourcing initiative. And, according to Pedersen, HR is delivering the same level of service quality (as assessed by metrics like the number of payroll errors) that it delivered before the initiative—at lower costs. Once the city acquires more experience in using the new system, officials plan to consider outsourcing other types of services, such as recruitment.

Political and Cultural Hot Buttons

In any major change initiative that Copenhagen considers, the potential benefit for taxpayers serves as the city's major decision-making criterion. "We will always be willing to outsource a support function," Pedersen says, "if the market can do it better and cheaper." But as in any organization, employees' concern about their future constitutes another major consideration during an outsourcing effort.

To address such concern, Copenhagen guaranteed HR staff members' jobs for the first year of the initiative, provided a lump-sum compensation for the move to the new company, and employees' secured their pension benefits. City leaders also conveyed the message to outsourced HR employees that they would now be working for a vibrant company that would grow and take on new customers in the future. The city expects that 80 to 90 percent of the outsourced HR employees will still be with their new employer in September 2004—one year after the initiative began.

City officials also took steps to engage the unionized workforce, which, according to Pedersen, actually supported outsourcing. By involving union members in the outsourcing preparation process and enabling transferred unionized employees to remain with the union, Copenhagen earned the support of this workforce component.

Vendor Selection in the European Union

Though European and U.S. organizations face similar considerations in outsourcing HR, there are also important differences. For instance, as Pedersen points out, "In the European Union, there is a detailed tender system that we all have to follow. The EU principle is that every vendor should be treated equally. That means we can't negotiate before choosing a vendor; we can't talk to them before choosing."

In this system, if one vendor asks a potential client organization a question, the organization must provide the answer to all potential vendors through a disciplined process. These requirements have led to the development of a detailed request-for-proposals (RFP) process. In Copenhagen's case, the effort involved receiving and evaluating bids from seven vendors, whittling the candidates down to three, and finally selecting one.

Vendor Management

To ensure high-quality service from its HR outsourcing vendor, Copenhagen relies heavily on the contract's service-level agreements (SLAs), which were determined from the baseline the city established. Pedersen is part of a steering committee whose members meet regularly to discuss day-to-day concerns related to the vendor relationship. He says problems have been resolved amicably so far, and decision-making is pushed to as low a level as possible, with only major conflicts handled by top management. If legal issues crop up, the city gets a second opinion on how best to resolve them.

Texas Health and Human Services Commission

Role Oversight of the state's health and human services agencies;
administers certain programs, such as Texas Medicaid and Children's Health Insurance Program

Number of employees Approximately 46,000

Budget $20 billion annually

Outsourcing began 2004

HR functions outsourced Total (excluding policy and planning)

Targeted cost savings $1 billion for reorganization within first two years of implementation,
$63 million in HR savings over five years

Texas does almost nothing on a small scale, and the state's 2003 reorganization bill is no exception.[6] Consolidating 12 state agencies into five, the newly streamlined Health and Human Services Commission (HHSC) today has 46,000 employees who run 200 programs at more than 1,000 locations. With a budget of $20 billion annually, Texas HHSC counts among the largest government organizations in the nation; if it were a private corporation, it would rank about 33rd in the *Fortune* 500.

HHSC has a hefty responsibility: not just to facilitate Texans' access to social services, but also to find better ways to serve the state's citizens. Besides seeking efficiencies, its mandate is to shave costs. Consolidation allows HHSC to outsource to the private sector as many operations as it deems appropriate. As Gregg Phillips, deputy executive commissioner for social services, notes, "Our goal, by law, is to seek the best value."

But HHSC has another impetus to outsource as well: the ballooning budgetary challenges that Texas, like most states, is facing. The rate of growth of employee services, besides being so costly, is straining government bureaucracy, Phillips notes. The agency has a $1 billion savings target it must hit in the first two years of implementation and a total of $3.6 billion over a five-year period, as stipulated in the legislation. These savings should help reduce the state's $10 billion budget deficit considerably.

6 House Bill 2292.

HHSC plans to outsource a wide array of functions, starting with HR. Why begin there? The commission needs to get a handle on its personnel and future needs in the newly constituted enterprise. In addition, executives recognized early on that "we were a little fat," Phillips says. For these reasons, and with its antiquated paper-based systems, HR was considered "low-hanging fruit." Outsourcing everything from payroll to benefits administration, and from recruitment and screening to "you name it," says Phillips, the commission will, in effect, become a holding company; it will retain management and oversight responsibility, supervising the vendor, ensuring performance, and creating workforce strategy.

In May 2004, HHSC completed its search for a vendor to handle the processes targeted for outsourcing. But to ensure a fair evaluation of its existing HR organization, the commission had followed the same "competitive sourcing" model used by the federal government, in which the internal department is invited to compete against outside vendor bids to retain the service. In the fall of 2003, before issuing requests for proposals (RFPs), HHSC challenged its HR department to price its services, both existing and "optimized" (the ideal array of services, including new value-added ones). The HR department's bid competed with those of the commission's two outside finalists.

With an outside vendor, few people will remain employed in the agency's HR department. A good percentage of the 420 employees now in HR, payroll, or the enterprise (software) service center will necessarily become redundant. Notes Phillips, "Job reductions are a key concern of ours, but not a decision driver."

Phillips points out that the Texas Workforce Commission (TWC), a job placement agency, is poised to help HHSC employees who may face layoffs as a result of the commission's outsourcing efforts. TWC's programs—in particular its Rapid Response team—are highly effective, and Phillips is optimistic that HHSC employees will either be placed elsewhere in Texas government or find work in the private sector. With an implementation of this scale, the primary vendor often subcontracts pieces of the work to anywhere from 10 to 20 smaller companies. Vendors and their subcontractors frequently absorb many employees who were laid off as a result of the outsourcing.

Legislative Support, Public Reaction

With Texas' unequivocally pro-business environment, the governor and Legislature support privatization and have stood behind the effort from day one.

But with such sweeping latitude and so aggressive a plan, where does the public stand on HHSC's outsourcing effort? "Texans expect us to run things efficiently and effectively in their service," Phillips says. "I don't think they care whether it's done in-house or is outsourced."

And though the strategies are aggressive, HHSC has taken what Phillips considers a "measured and conservative" approach to implementation. "We haven't been aggressive in our timeline. We'll bide our time, and collect and develop all the supporting documentation." However, the notion of offloading such functions as eligibility (deciding who should receive government benefits) to a privately run call center makes many in public policy circles uncomfortable. HHSC will evaluate the potential benefits of outsourcing some eligibility functions, but state employees will continue to certify cases for benefits.

Keeping It In-State

While the reorganization bill contains no jurisdictional restrictions on where the outsourcing activity must take place, Phillips maintains that HHSC wants Texans to handle the work. For call centers, it makes sense to have a backup center located out of state, for disaster-recovery purposes. But "we'll try to get vendors located as much as we can in Texas." Given the limited number of providers, going out of state would expand the pool of vendor candidates, thus increasing the chance of getting the best-priced deal. Still, according to Phillips, vendors aren't pushing the jurisdictional issue; no one, for example, has proposed sending any outsourced services offshore.

For Texas HHSC, HR is but one of many outsourcing initiatives designed to enhance services delivered to Texans. This summer is shaping up to be a busy request-for-proposals season, as the commission plans to evaluate the potential to outsource some components of its benefits eligibility services: Medicaid enrollment and claims management, food stamps, and temporary assistance to needy families, along with such functions as pharmacy benefit management and purchasing.

Policymakers, politicians, bureaucrats, and outsourcing vendors, of course, are all eagerly watching Texas' radical experiment because it could easily open the floodgates to the private sector assuming the traditional work of government on a grand scale. Meanwhile, HHSC is forging ahead. Like other government trailblazers, the commission has leaders who are confident that the efficiencies and value-added services realized will far outweigh any pain that may come with job displacements.

Of course, the reorganization is far from complete, Phillips acknowledges. Between managing the transformations and challenges associated with the reorganization and outsourcing initiative, HHSC won't know for some years whether outsourcing HR pays large or small dividends. For now, Phillips says, "we see a tremendous savings opportunity in HR. If it's not there, we'll walk away."

Lessons Learned

Although public-sector HR outsourcing is still evolving, the pioneers already have many lessons to share.

Get support from the top for the effort: executives, legislators, and the governor.

Develop a communications program for employees, the public, and the press about the benefits outsourcing can bring—not just internally but for taxpayers. Publicize the efforts under way to take care of effected workers.

Work within the government budget process. Because budgeting is different (generally, annual) in government organizations, it helps to have proposals completed and ready for review in time for regular budget appropriations. Also, contracts must often be renewed and re-approved every year, so a multiyear contract provides stability. The renewal process affords the vendor the chance to boost service quality if it has slipped.

Establish clear-cut, rigorous procedures for the vendor selection process to ensure fair consideration and avoid even the appearance of impropriety.

Seek a vendor with experience in the public sector. Policy guidelines and union agreement requirements make for strict processes and procedures.

Negotiate and agree on service-level agreements that contain useful performance expectations and metrics. For example, using a metric on providing a satisfactory response to a caller within 24 hours, instead of answering calls to the call center on the third ring.

Ensure adequate staffing throughout the effort on both sides. Involve IT personnel, not just HR personnel, from the outset.

Allow for flexibility. Certain services initially contracted may prove unnecessary over time; others overlooked at first may later seem attractive or vital. However, delivery dates and penalties should be built into the contract.

Consider requesting legislation to streamline procedures before implementation. Doing so can make data entry and IT work vastly easier—and save considerably.

If workforce reductions will be significant, **create early job placement assistance** with the vendor that taps the resources of job placement agencies and programs. Explore with vendors what job opportunities they may be able to offer displaced employees.

Engage the appropriate unions early by communicating the benefits of outsourcing, offering to help transfer union employees, and helping them retain their union status.

Avoid an overly aggressive implementation timetable. Delays cost dearly, not only in dollars and public support, but also in the goodwill of the employees who must operate with reduced head counts before the new services come online.

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The Conference Board, Inc.
845 Third Avenue
New York, NY 10022-6679
United States
Tel 212 759 0900
Fax 212 980 7014
www.conference-board.org

The Conference Board Europe
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B-1000 Brussels
Belgium
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