Evaluating alternative operating models for government-wide shared services

Taking the back office out of mission-focused agencies

EY

Building a better working world

Increasing demand to streamline "back-office" functions across government

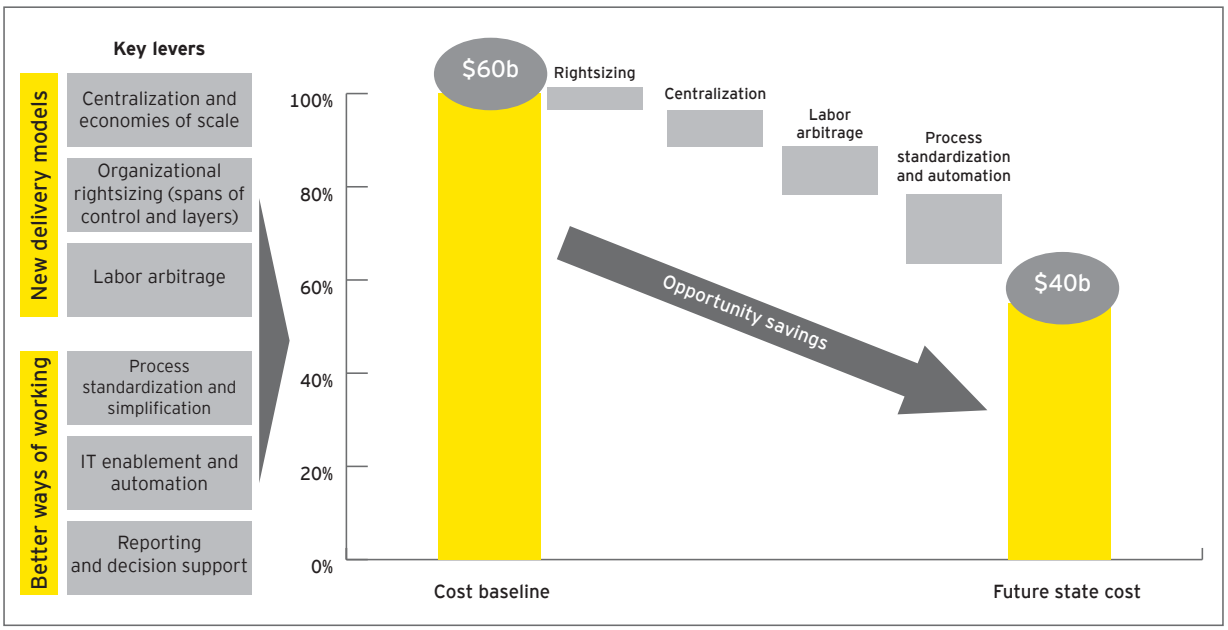
The federal government spends billions of dollars each year on non-mission-focused functions, processes and systems related to agencies' back-office operations – such as finance, HR, IT and acquisition. The absence of a government-wide, "corporate" view and supporting strategy for common back-office services has resulted in widespread duplication of effort, resources and capital investments. In order for government to **work better for the people**, the government needs to improve back-office operations to run more efficiently and effectively.

Many agencies operate in budgetary environments where funds are pulled away from mission programs in order to support the rising costs of back-office operations. Additionally, the new Administration is asking agencies to evaluate opportunities for program and service consolidation and elimination of duplicative functions, with emphasis on back-office functions. Included in this evaluation is an assessment of whether the private sector could do the work better.

All of these factors will increase demand for back-office shared services across the federal landscape. In order to better manage their budgets and achieve cost savings, agencies will look to leverage the back-office systems, business processes and staff of other agencies who can operate them at less cost. In addition, agencies will continue to look internally to consolidate duplicative or overlapping functions to achieve scale economies, and may look to low-cost operating locations in order to reduce expense.

EY's strategic framework for effective government

Considerable savings could be achieved through shared services across the federal government. As an example, cost savings for civilian agencies alone, would drive tremendous savings. According to the FY16 enacted budget, approximately $500b is spent by federal civilian executive agencies in total (including back-office operations). Approximately 10% to 15% of the total spend is for back-office operations, representing $50b to $75b of federal civilian executive agency dollars. A common industry rule of thumb is 75% to 80% of back-office operations are eligible for shared services migration. The range of addressable spend to convert to shared services is likely $40b to $60b. Industry estimates range from 20% to 50% bottom-line savings in moving effectively to shared services. Using a conservative savings range of 20% to 35%, $12b to $20b in annual savings is possible among the federal civilian executive agencies. Key levers of savings are shown in the diagram below



Increasing challenges related to the current shared services operating model

The current supply of back-office shared services in the government is limited and challenged to meet the current demand, let alone the increased demand that is expected as agencies continue to divest back-office operations. In light of the macro trends highlighted above, agencies are looking for opportunities to consolidate back-office operations. But there are currently only a handful of Office of Management and Budget (OMB)- and Office of Personnel Management (OPM)-designated mission-focused agencies that are authorized to provide back-office services and operations to other agencies, in addition to a few agencies that are providing back-office shared services internally for their own bureaus.

Additionally, these current models are constrained by their operating environment and have limited overall potential to expand in order to maximize the benefits of federal wide back-office consolidation. The primary issue with the government's current shared services model lies in positioning mission-focused agencies to provide non-mission-focused services to other agencies. This approach creates competing priorities between the parent agency and the shared services operations. As part of the parent agency, shared services enterprises are continually impacted by the day-to-day issues and notifications agencies must react to, making shared services enterprise planning and incentives for improvement in people, processes, technology, pricing and innovation nearly impossible. Additional constraints in the current model include:

- Limited ability to fund investments across multiple budget years to support operational improvements and drive down costs
- Limited ability to budget for and fund transition costs needed to onboard new agencies and services
- Structural barriers to designing disruptive, innovative delivery models (such as robotic process automation (RPA) software, which has the ability to more efficiently handle simple tasks formerly performed by clerical workers)
- Limited ability to enact incentives for operational performance and customer service and hold responsible executives accountable
- Difficulty in aligning shared services strategy with strategic goals and objectives of the parent agency — which are tied directly to the budget process

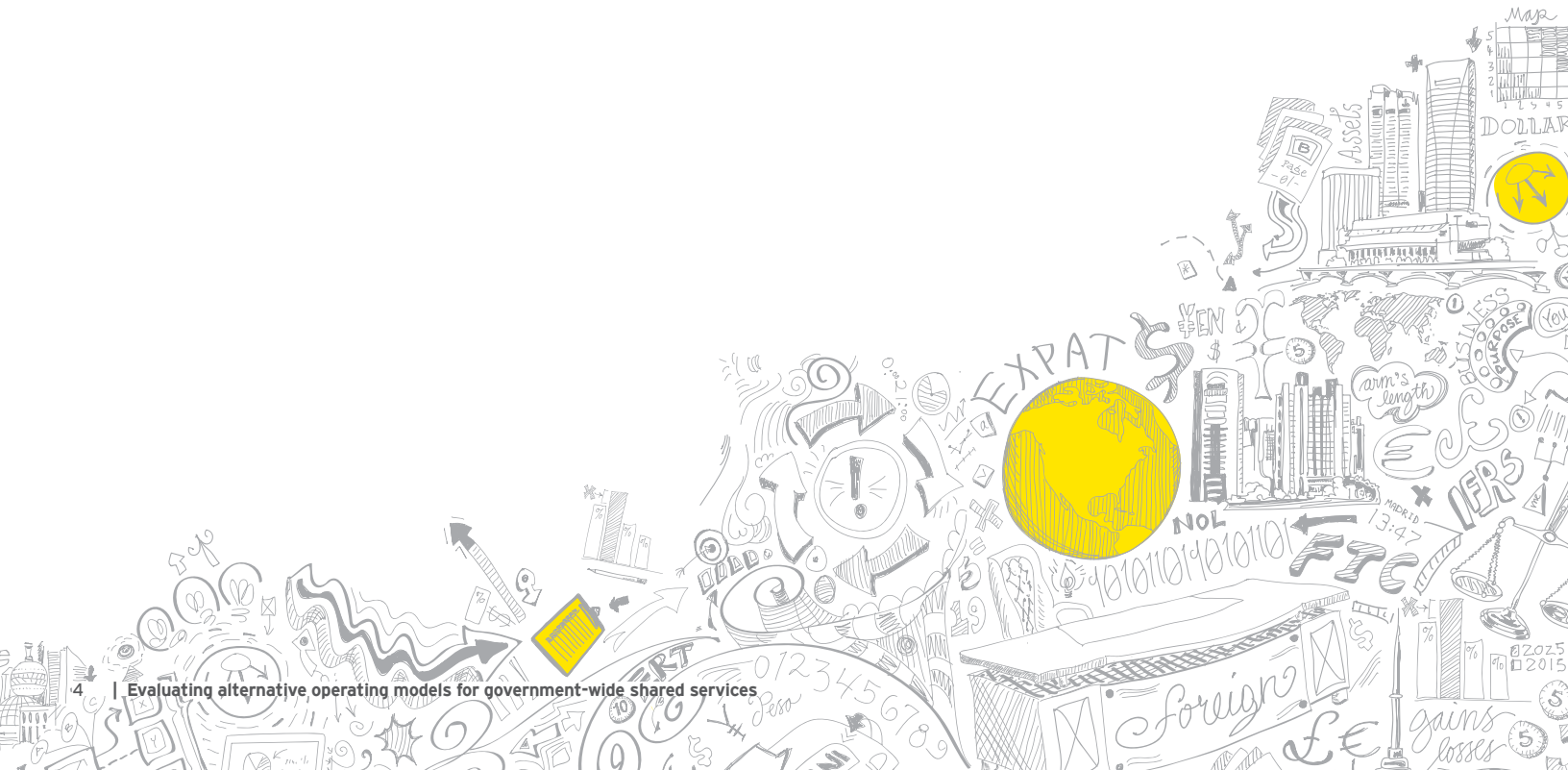
Alternative operating models to serve the federal government's needs

The commercial industry has faced similar challenges and in response has pulled back-office functions and processes outside of their businesses and centralized them into separate shared services operations. The realized benefits have been efficiency (cost reduction), effectiveness (freeing up of management time to focus on more value-added tasks) and control (better ability to manage risk in shared services environment).

The government should follow the example from commercial industry and evaluate options for taking back-office operations out of mission-focused agencies. Government should consider a variety of operating models to increase the capacity in the market to support increasing demand for back-office systems and processes. The potential benefits include:

- Significant cost savings and reduced size of government
- Increased agency focus on the core mission rather than back-office operations
- Improved effectiveness of customer service and operations
- Improved controls and risk management (including critical areas such as cybersecurity)
- Increase jobs outside of Washington, DC, as shared services migrate to lower-cost regions

The following is a summary of alternative shared services business models — several from commercial industry — for consideration. These models could be adopted by the select designated federal shared services providers, as well as agencies that are providing back-office shared services internally for their own bureaus. All these models could be used to support more agencies with their back-office needs.



Shared services models	Performance-based organization (PBO)	Cooperative	Government corporation
Description	‣ A discrete business unit, within an agency, with strong incentives to manage for results	‣ Autonomous operation jointly owned and democratically controlled	‣ Independent federal agency with its own authority, appropriation and mission
Benefits	‣ Has independence and autonomy of operations ‣ Run by experienced performance-based chief operating officer (COO) ‣ Flexibility in personnel, procurement, finance and real property decisions ‣ Requires no legislation (leverages current PBO)	‣ Jointly owned and managed by customer organizations and member-based board ‣ Funded through service fees ‣ Surpluses redistributed to cooperative members ‣ Customers can "buy" into customized services ‣ Board guided by customer and industry-leading practices	‣ Eliminates mission agency vs. shared services conflict ‣ Commercial-based budget and fees ‣ Flexibility of location, structure and governance ‣ Revenue, expenditure and personnel can fluctuate with demand ‣ Leverages existing government corporation structure, specifically designed for self-sustaining organizations with large transactions
Risks	‣ COO reports to agency secretary; lack of independent board could result in bias and mission creep	‣ New territory for legislation to operate as a collective across multiple agencies ‣ Mechanisms to drive continual innovation and improvements need to be agreed-upon and promoted by the cooperative	‣ Requires chartered legislation by Congress ‣ Previous government corporation was used for revenue generation with public, not internal federal agencies ‣ Mechanisms to drive continual innovation and improvements need to be established
Examples	‣ Federal Student Aid ‣ United States Patent and Trademark Office	‣ N/A (in federal)	‣ Federal Deposit Insurance Corporation (FDIC) ‣ Federal Prison Industries (UNICOR) ‣ United States Postal Service

Shared services models	Government-sponsored enterprise (GSE)	Public-private partnership	Full privatization
Description	‣ Privately owned, publicly chartered business	‣ Partnership between government and private industry to finance, build and operate projects	‣ Transfer of ownership of operations from public sector to private; outsourcing of services
Benefits	‣ Eliminates mission agency vs. shared services contract ‣ Commercial-based budget and fees ‣ Operations managed as a business, with significant flexibility ‣ Exempt from federal management and staffing laws ‣ Can be used as transition vehicle from government to privatization	‣ Private industry funds initial investment ‣ Government provides oversight, outreach and ongoing discretion over future investments ‣ Potential hybrid model allows government to retain certain functions ‣ Various financing alternatives for initial build ‣ Potential for government asset contribution	‣ Private industry owns and operates entity separately ‣ Government performs only "inherently governmental" functions ‣ Removal of direct costs from federal books ‣ Fee-based funding and IT needs paid by contractor ‣ Various financing alternatives for initial build
Risks	‣ Requires chartered legislation ‣ Potential for misalignment of goals and objectives with agencies and private industry ‣ Previously used only for capital markets	‣ Potential for misalignment of goals and objectives ‣ Requires senior commitment from each agency and acquisition strategy ‣ Service level agreements (SLAs), change orders and fees require careful management ‣ Requires selection fo contracting entity	‣ The needs of government change ‣ SLAs, change orders and fees require careful management ‣ Competition may be limited to initial contract; future-cost reductions may be hampered by outsourcing contract ‣ Requires selection of contracting entity
Examples	‣ Fannie Mae ‣ Freddie Mac ‣ Sallie Mae (until privatized)	‣ FirstNet ‣ Dulles Greenway	‣ Sallie Mae ‣ Private sector human resources line of business

Translating new operating models into reality

The current shared services supply environment will be unable to meet the increasing demand for back-office consolidation. The government needs to act now to get out ahead of increasing the shared services operations supply and eliminate the constraints that currently hold shared service enterprises back. An evaluation across the federal landscape should be conducted to determine where alternative operating models should be considered. We recommend a variety of operating models be tested quickly and simultaneously in the federal market to drive innovation and meet demand.

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