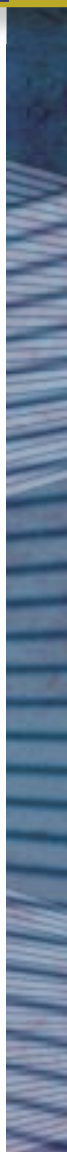
Australian Government

Information Management Office

A Guide to ICT Sourcing

for Australian Government Agencies

Developing and Executing an ICT Sourcing Strategy



The Australian Government Information Management Office (AGIMO) fosters the efficient and effective use of ICT by Australian Government departments and agencies. It provides strategic advice, activities and representation relating to the application of ICT to government administration, information and services. AGIMO acts as a catalyst for change in government to improve the delivery of public services and achieve long-term efficiencies by using the enabling capabilities of information and communication technology (ICT). It works across Australian jurisdictions to maintain and develop Australia's position as a world leader in the use of ICT for the operation of government.
AGIMO provides leadership in defining and driving government-wide ICT strategy, standards, and technical architecture, and embraces security and resilience issues.

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The Boston Consulting Group (BCG) is a general management consulting firm and a global leader in business strategy. Founded in 1963, the firm now operates over 50 offices in 34 countries. BCG has assisted many large organisations across all elements of ICT sourcing, including developing sourcing strategies and assessing, negotiating and managing ICT sourcing arrangements. For further information about BCG's ICT sourcing experience, please contact:

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Consulting Insights (CI) is a Canberra-based consultancy specialising in strategic performance improvement and information management. CI has extensive experience across large and small Australian Government agencies, and a good practical understanding of how ICT sourcing by the Australian Government has evolved in recent times. CI expects to tailor services to maximise value to individual agencies, in particular to transfer skills and to build an ongoing capability for agencies to easily make well-informed, defensible decisions about ICT sourcing.

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Contents

Foreword

This is a guide to effective practices for Australian Government agencies that are dealing with information and communication technology (ICT) sourcing issues. It was developed in response to a demand from agencies, recognised by the Information Management Strategy Committee (IMSC) and the Chief Information Officer Committee (CIOC), for clear and objective information about ICT sourcing.

This is not a policy document or rule book. It is a guide that provides options and strategies for decision-making about ICT sourcing. It describes how agencies might manage ICT sourcing based on a four-phase lifecycle, which starts with a decision about whether to change the current sourcing strategy and concludes with an approach for transitioning to, and managing, a new sourcing solution.

Instead of detailing step-by-step instructions for every sourcing scenario an agency might encounter, the guide provides practical frameworks to consider and resolve the key challenges and questions that agencies are likely to confront. The guide gives emphasis to Phases I and II of the lifecycle – establishing the case for change and developing a sourcing strategy – because these have been identified as elements of greatest need by agencies, and because there are several Australian Government publications that address the other phases.

The appendices provide supporting tools and information to help agencies work through this lifecycle. In particular, Appendix A describes a tool that was developed to help agencies determine the economic value of an existing or proposed sourcing arrangement; this will be essential during the first two phases.

Before agencies begin any ICT sourcing process, including the one presented in this guide, it is important that they are aware of the principles and policies that underpin Australian Government procurement, including those that relate specifically to the procurement of ICT goods and services. The Commonwealth Procurement Guidelines articulate these requirements and are available, along with other supporting material, at the Department of Finance and Administration website: http://www.finance.gov.au .

Agencies can also refer to an ICT Sourcing website, established by AGIMO at http://www.sourceit.gov.au . It contains up-to-date information about ICT sourcing, as well as tools, checklists, Head Agreements, and details of upcoming ICT sourcing events. Access to this website can be gained through each agency's CIO or ICT Manager.

Much of the material in this guide was derived from The Boston Consulting Group's experience with ICT sourcing assignments throughout the world, and from Consulting Insight's experience across the Australian IT sector, particularly with Australian Government agencies. AGIMO, BCG and CI have worked together to consolidate and customise these materials into a single document relevant to the needs of agencies.

The contents of this Guide will be reviewed regularly, to ensure that it continues to reflect the needs and expectations of agencies and developments in the marketplace.

John Grant

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Introduction

What is ICT?

ICT is a management information tool to support an agency's business requirements. It typically includes components such as applications development, infrastructure (mainframes, midranges, desktops and servers), communications, strategy and administration.

What is ICT sourcing?

ICT sourcing determines where an agency's ICT components are obtained, managed and run. The basic objective of ICT sourcing is to deliver the best level of support for the agency's business requirements in the most cost-effective way. This is encapsulated in the Government's policy objective of achieving the best overall Value for Money ICT outcome.

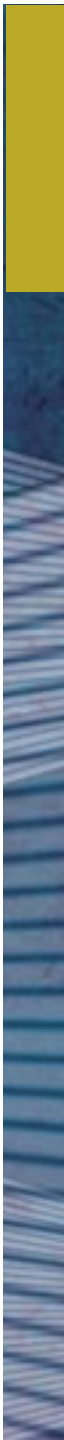
For some agencies, the 'best level of support' may mean access to skills and expertise not available internally, or greater flexibility to allow ICT to meet changing business requirements. Others may use ICT sourcing as a way to release resources and allow for a greater focus on strategic objectives.

We have defined three broad types of ICT sourcing, based on the degree to which ICT is managed externally and the number of vendors involved:

Self-managed:	ICT is predominantly managed and run by internal resources, possibly including contractors or consultants, with little or no service level agreements (SLAs) with external vendors.
Single sourcing:	ICT is predominantly run by a single external party under an SLA.
Selective sourcing:	ICT is predominantly run by multiple external parties under one or several SLAs.

Single sourcing and selective sourcing are often grouped together and called 'outsourcing', while self-managed is also be referred to as 'in-house'. In a self-managed arrangement, agencies would purchase goods from suppliers, and procurement would largely be transactional. In an external arrangement – either single or selective – agencies would generally need to manage a more complex relationship with a vendor. Most agencies would typically use a mix of all three sourcing methods for different aspects of their ICT.

There are other sourcing models such as Business Process Outsourcing (BPO), shared services, co-sourcing, offshore, and contracting out. These can be considered variations within the three basic models described above.

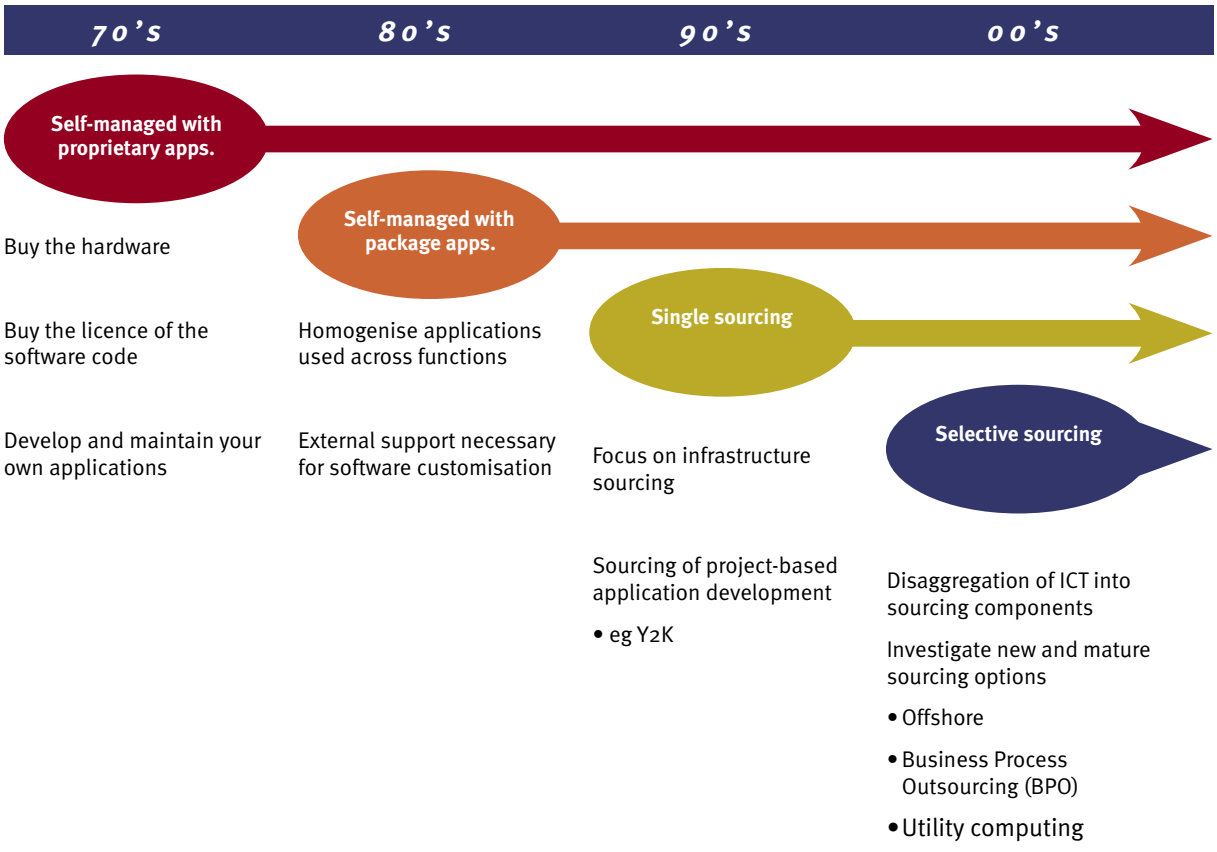


Overview of ICT Sourcing

Evolution of sourcing strategies

In recent years, many organisations have become more sophisticated in the way they run their ICT, disaggregating it into components instead of managing it as one large block of requirements. This allows them to better understand their specific strengths and shortcomings, and to move from the familiar single sourcing approach to one based on selective sourcing (Exhibit 1).

EXHIBIT 1



One of the main benefits of selective sourcing is that it allows agencies to engage different specialists for particular ICT components. However, compared to single sourcing, it involves greater effort and complexity in selecting and managing vendors.

Consistent with recent Gartner research, Australian Government agencies are including selective sourcing as an ICT outsourcing option, recognising that there is no one method that suits all requirements.

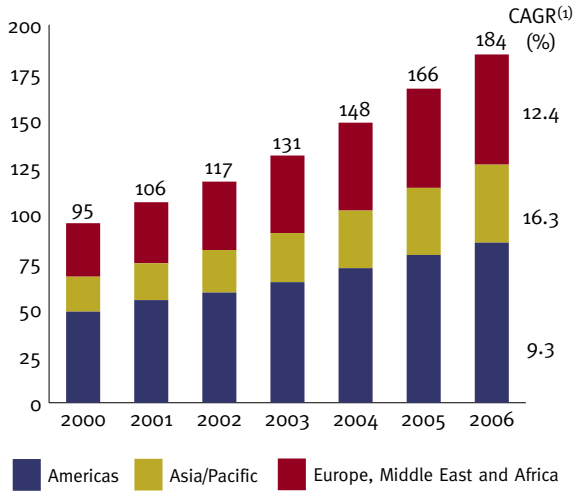
Growth of ICT outsourcing

ICT outsourcing (both single and selective sourcing) has emerged as a massive industry over the last decade, with worldwide spending growing from $9 billion in 1990 to over $100 billion in 2002. This is predicted to exceed $150 billion worldwide in about two years.

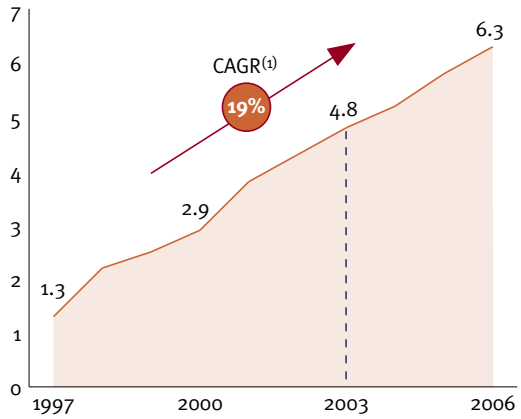
While Australia's total spend on ICT outsourcing is only a fraction of this total – it is expected to reach almost $5 billion in 2003 – it is growing at a faster rate than the worldwide average (Exhibit 2).

EXHIBIT 2

Worldwide IT Outsourcing Spend by Region: 2000-06 (A$b)



Forecasted Australian IT Outsourcing Spend: 1997-06 (A$b)



(1) Compounded Annual Growth Rate
Source: IDC World Outsourcing Services: Midyear forecast update 2002; IDC Australia; Press Search; US$ converted to 2002A$;

This growth is an outcome of the large number of Australian organisations that have outsourced at least part of their ICT budget. A recent University of Melbourne survey[1] of 235 large Australian public and private organisations indicates that while only 20% have outsourced more that half of their ICT budget, 67% of respondents have outsourced at least 10%.

1 Rouse, A. C. (2002). *IT outsourcing revisited: Success factors and risks*. Unpublished PhD Thesis, The University of Melbourne. and Seddon, P.B., Cullen, S., Willcocks, L.P., Rouse, A. C., and Reilly, C.T. (2001) *Report on Information Technology Outsourcing Practices in Australia, 2000*, Working Paper, Department of Information Systems, The University of Melbourne.

TABLE 1: UNIVERSITY OF MELBOURNE SURVEY

Proportion of IT budget spent in external service agreements	Proportion of 235 survey respondents
‹10%	33%
11% to 50%	47%
51% to 80%	12%
› 80%	8%

ICT Outsourcing Policy

The Australian Government's ICT outsourcing policy devolves responsibility for implementing ICT outsourcing to agency Chief Executives and Boards. In this environment, agencies can determine the most appropriate model(s) to meet their ICT requirements and business needs, within the bounds of the policy objectives of:

- Achieving Value for Money ICT; and
- Maximising Australian industry development.

The outcomes of the chosen ICT model are included in the overall performance assessments of agency Chief Executives and Boards, while agency progress is monitored and reported publicly in the State of the Service Report. For more information relating to the policy, and in particular, the Commonwealth Procurement Guidelines (CPGs) see http://www.finance.gov.au.

Why do organisations outsource?

Organisations typically pursue external sourcing arrangements for two reasons. From an economic perspective, they use outsourcing to control or lower their ICT costs (in the University of Melbourne survey, 58% of respondents cited cost savings as the main reason for outsourcing). From a strategic perspective, they use it to allow them to focus their energy and attention on core business processes or objectives, access better or more skills or expertise, and provide services not available internally.

At the same time, many organisations have clear reasons for not outsourcing ICT services:

- The market price for outsourcing may be higher than internal costs – some organisations find that they can fulfil their ICT requirements more affordably on their own.
- The risk associated with relinquishing control is too great – for some organisations, ICT is essential for business continuity, or is an integral part of what they do, and they want to keep it close to ensure that it is always capable of supporting their needs.
- The risk of losing organisational knowledge is too high – this is of particular concern for organisations that have complex, customised technology.

Learning from experience

Organisations have generally been satisfied with some specific strategic benefits of outsourcing. In the University of Melbourne survey, 47% of respondents said they achieved 'moderate' outsourcing benefits by gaining access to services that could not be fulfilled internally, while a further 43% reported 'substantial' benefits for the same reason. Also in the survey, 45% and 41% of respondents reported 'moderate' and 'substantial' benefits, respectively, from gaining access to better skills and expertise. In addition, 29% and 26% reported 'moderate' and 'substantial' benefits, respectively, through better utilisation of their in-house personnel.

The University of Melbourne survey found that only around one-third of organisations (36%) were unequivocally satisfied with their IT outsourcing arrangements, and less than half (41%) were satisfied with the Value for Money of their outsourcing arrangements, even though the majority of respondents cited cost savings as the main reason for outsourcing. In particular, many organisations have been underwhelmed by outsourcing's economic benefits. They found that their ICT costs dropped initially, only to return to pre-sourcing levels during the contract. In the survey, 7% of the participants said they achieved 'substantial' savings, while 35% reported 'moderate' savings. However, 22% said their cost of IT services was now 'worse' as a result of outsourcing, while 36% reported 'no change'.

An overview of the Australian Government's ICT outsourcing activities can be found in Chapter 10: Outsourced Services of the *State of the Service Report*, issued by the Australian Public Service Commission.

Understanding costs and complexities is the key to success

Many organisations agree that selecting and managing a sourcing arrangement was far more complex than they expected, and that they would proceed with much greater care the next time around. In particular, they would put forward a stronger legal and contract management team, and would take more time to arrive at the right ICT sourcing choice.

In addition, BCG global experience suggests that many organisations have misjudged the true value of sourcing arrangements, in part because they did not analyse a sufficient range of options or were not careful enough when it came to structuring exit provisions, which can trigger termination costs that make switching prohibitively expensive.

The message from this collective experience is clear: ICT sourcing can provide both strategic and economic benefits for certain organisations, but the process needs to be handled with timely and careful deliberation due to high levels of risk and complexity.

Managing ICT sourcing as a lifecycle

Given the complexities and risks of ICT sourcing, agencies need to be methodical and analytical about the way they assess, select and manage their sourcing requirements – this requires much more than a series of one-off purchasing decisions.

A four-phase ICT sourcing lifecycle

Sourcing is a continuous process – a lifecycle that starts by understanding the case for change, then choosing the best sourcing option, assessing vendor offers, and transitioning to and managing the chosen sourcing solution. The lifecycle begins again when a renewal decision must be made, or when changes have occurred that could affect an agency's self-managed strategy.

We have developed a four-phase approach to guide agencies through this lifecycle (Exhibit 3).

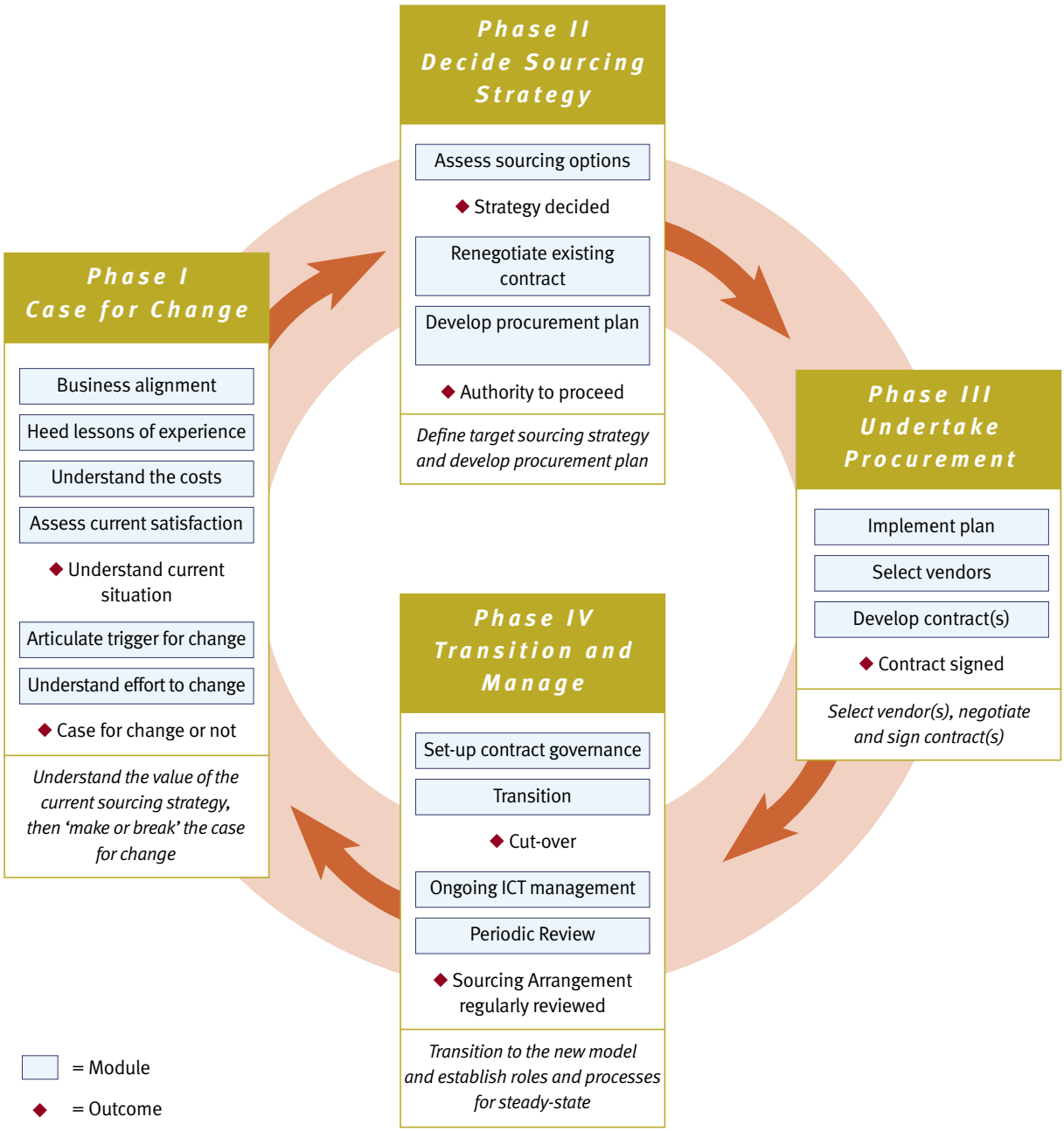
By following the lifecycle, agencies will be able to develop ICT strategies that are defensible and accurate, and are grounded in an unbiased assessment of their ICT sourcing options. This, in turn, will ensure that top management can easily understand and make well-informed decisions about their ICT strategy. It should also help build executive commitment to the outcomes, and ensure alignment with overall business objectives.

At any given time, different agencies will be at different phases of the lifecycle, and some agencies may well be across multiple phases for different components of their ICT. Large and complex agencies may have ICT activities with both shorter terms (such as telecommunications contracts) and longer terms (for example, a five-year hardware contract). This may result in ICT activities that are "out of phase". In these cases, it may be more difficult to understand the costs or the effort required to change as there is likely to be a more complex interaction between these various elements.

Officials should refer to their Chief Executive's Instructions, or other operational guidance, for specific directions that may apply to their agency in relation to their activities at all stages of the procurement cycle. In addition, at all stages of the process agencies should maintain appropriate documentation of all decisions and actions, to provide a record of their procurement activities and facilitate scrutiny of these activities in the future.

The objectives of each phase are described as follows:

EXHIBIT 3



- Phase I: Case for change

The objective of this phase is to consider changing sourcing arrangements to meet the agency's strategic ICT objectives. Agencies that self-manage their ICT could consider switching to external sourcing, while agencies that already have external sourcing arrangements need to determine whether they should renew or consider other options.

Phase I includes four modules for understanding the current sourcing strategy, one of which involves understanding the costs and the real value of the existing sourcing strategy. To perform this cost and real value analysis, agencies could use the economic diagnosis tool, which is described in greater detail in Appendix A and on the Source IT website. This phase concludes with modules for building the case for change and determining whether change is feasible.

- Phase II: Decide sourcing strategy

Agencies that establish a case for change should use strategic, qualitative and quantitative analysis to arrive at the most appropriate sourcing strategy for their needs. Agencies may also wish to investigate the market for ICT goods and services in order to obtain a real picture of potential costs and the benefits of alternative solutions.

Phase II includes three modules, beginning with the determination of the best sourcing strategy. This is a complex module that again involves detailed cost and real value analysis – this time, of potential sourcing arrangements. If the most appropriate strategy is external sourcing, agencies should develop a 'target' contract along with a detailed procurement plan. These activities make up the other two modules in this phase – renegotiating the contract and developing a procurement plan. Agencies considering self-managing their ICT should begin working out a transition plan (if applicable), and should proceed to Phase IV after this phase.

- Phase III: Undertake procurement

If agencies have decided on an external sourcing arrangement, they should proceed with the procurement plan defined in the previous phase, launching a tender process, screening and selecting vendors, performing due diligence, and negotiating a contract with their chosen vendor. Some agencies may choose to undertake several procurement processes in parallel to select multiple vendors. An agency that has opted to self-manage ICT will still need to have a procurement plan – for example, for software, hardware and other components of ICT. This type of procurement, which generally does not involve vendor relationships that are as complex as those undertaken in single or selective sourcing, may not require the strategies detailed in this guide.

Phase III includes three modules: implement the procurement plan, select vendors, and develop contracts.

- Phase IV: Transition and manage

This phase describes the steps needed for transitioning to and managing ongoing ICT sourcing arrangements. Here, agencies should focus on ensuring that the expected value from their chosen sourcing strategy is delivered.

Phase IV includes three modules. The guide provides less detail on this phase, primarily because there are already Australian Government publications that address these issues, particularly the management of contracts. It is also assumed that agencies are already familiar with many of these issues, such as change management, internal communications, and risk management, as these would apply to a host of activities, not just ICT sourcing.

Where does an agency sit in the lifecycle?

The lifecycle, on its own, cannot ensure the success of an agency's approach to ICT sourcing. It needs to be supported by several prerequisites.

For example, it is assumed that agencies that are entering Phase I of the lifecycle already have a project team for ICT sourcing. The size of the team will, of course, vary according to each agency's needs – some agencies will have more complex ICT needs than others, and will therefore require larger teams and greater expertise.

At a minimum, a project team should have a good understanding of an agency's ICT requirements. It should also be familiar with the basics of successfully managing a relationship with an external vendor, such as contract negotiation and management, and risk management (the Australian Standard for risk management is referenced in Appendix B). Agencies that have little or no experience in managing external vendors should consult with other agencies about the best way to build these skills, and should also refer to other

government publications that address these issues. A knowledge of Australian Government procurement policies and good practice is also essential within the project team.

Timing for agencies that have external sourcing agreements

Phase I should begin long enough before the end of existing sourcing arrangements to allow sufficient time to analyse these arrangements, develop a new sourcing strategy, assess a range of vendor offers, select the most appropriate vendor, and transition to this new vendor while maintaining services from the incumbent.

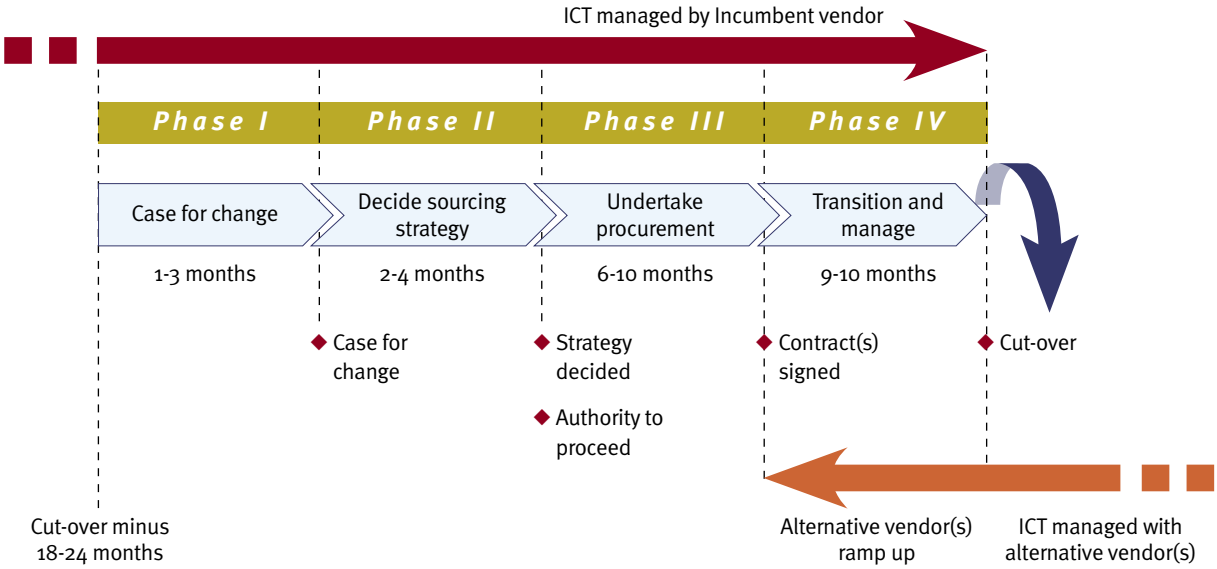
Exhibit 4 provides an indicative timeline that would typically apply to large agencies that have one major arrangement in place and are switching to one or several other vendors. Please note that Phase I and Phase II can sometimes overlap.

Obviously, when agencies establish their own timeline, which could look quite different from this one, they will need to consider numerous factors including:

- External factors and contextual circumstances: next foreseeable change in the Machinery of Government, contract end date, etc.
- Scope of the exercise and whether it applies to vital business functions
- Level of internal expertise; first-generation agencies – ones that are outsourcing for the first time – might take longer than second-generation agencies on some aspects (e.g. thinking and preparing termination), and less time on others (e.g. transferring knowledge)
- Availability of resources and information (especially for costing analysis)
- Potential to run tasks in parallel
- Internal decision-making processes
- Level of risk (including security) the agency is willing to take
- The market approach (one phase, going straight to an RFT, or two phases, beginning with an REOI), and whether it includes a prime contractor, one contract or multiple, etc.
- Whether it involves alliances with other agencies.

EXHIBIT 4

Illustration of a transition between different vendors in the case of a large agency



Phase I: Case for change

The purpose of Phase I is to develop a clear understanding of the agency's current ICT sourcing situation. This perspective, which can be used to build a case for either changing or keeping the existing sourcing arrangements, is based on four modules:

- *Understand business priorities:* What are the most critical ICT activities?
- *Heed the lessons of experience:* What can be leveraged from our own and other organisations' experiences?
- *Understand the costs:* How do the agency's costs compare to alternatives?
- *Assess current satisfaction:* How satisfied is the agency with its current ICT sourcing?

At the end of these modules, agencies should perform a trigger point analysis to determine whether alternatives need to be considered. If this confirms the case for change, agencies then need to understand the effort to change – are they in a position to transition from their existing sourcing solution?

Understand business priorities and corresponding ICT requirements

Business priorities will drive ICT requirements. Throughout the lifecycle, agencies should never lose sight of this link; a sourcing strategy will only be successful if it provides ICT that can fulfil these requirements.

To understand this link, agencies should identify and categorise their business activities as:

- *Vital:* These activities are the reason why the agency exists in the first place. They are generally unique to the agency. If the agency cannot perform a vital activity, the impact will be immediate and profound. For example, the management of the Budget is a vital activity for The Department of Finance and Administration (Finance).
- *Duty-bound:* These activities are part of the agency's mission. They are important, but other agencies could potentially perform them. For example, managing Ministerial and Parliamentary support services is part of Finance's mission, but it could potentially be another agency's responsibility.
- *Discretionary and support:* These activities are neither strategic nor core. Nevertheless, faults or disruptions to these activities can still affect an agency's ability to fulfil its

mission. They represent all activities that do not fall in the previous two categories. These are usually common across several agencies; for example, accounting or personnel.

Once this is done, agencies should determine the corresponding ICT requirements for each category. The relative priorities can differ by agency. For instance, the storage and easy retrieval of documentation may be vital to the National Library, whereas it may be considered a support function for other agencies.

At the end of this assessment, agencies should have a clear understanding of the key success factors for the agency (defined as business priorities) and the corresponding key success factors for ICT. This understanding will provide the context – a sense of purpose for ICT sourcing, in general – for the rest of the lifecycle.

This assessment also has a risk management application. To begin with, agencies should recognise that relying on external vendors to manage components of ICT involves certain risks, primarily from relinquishing control over these components. Although vendors may be contracted to share some of the operational risks, the agency will ultimately be accountable for the functions it is meant to provide. For this reason, the link between business priorities and ICT requirements will be an important factor in developing a sourcing strategy, in Phase II, and informing potential vendors about the agency's expectations.

This assessment should be performed after any government-driven events that reallocate business activities among agencies or that create, merge, or split agencies, as these actions could modify an agency's business priorities.

Heed the lessons of experience

When building a case for change, agencies should share sourcing lessons, particularly with agencies that have similar business or ICT characteristics. This will reveal whether other agencies have been able to achieve stronger economic or strategic benefits through their sourcing arrangements, and can provide an initial indication about the 'competitiveness' of an existing sourcing strategy.

Sharing these lessons among agencies has been difficult in the absence of standard frameworks and terminology. This guide, together with the Source IT website, should help to establish a common language to facilitate information sharing.

Agencies should also look for lessons outside government and outside Australia. Much can be learned from the way businesses, both here and abroad, have dealt with the challenges of executing a successful ICT sourcing strategy. Likewise, other governments have had to work through similar issues, and have published studies about the lessons learned from external ICT sourcing.

Understand the costs

BCG experience has shown that many organisations base their sourcing strategies on the perceived, rather than the real, value of an arrangement. For this reason, the guide places a strong focus on helping agencies understand the costs associated with sourcing. In particular, we have developed an economic diagnosis tool, which is described in greater detail in Appendix A and on the website. Agencies could use the tool at various points in the first two phases of the lifecycle, including this module.

ICT sourcing decisions are traditionally based on perceived value

To start with, agencies should develop a view of the perceived value of their existing sourcing strategy. To do this, they need to understand the economic drivers that explain the cost difference between self-managing an ICT component and sourcing it externally. This difference is called the perceived value and is shown in Exhibit 5.

EXHIBIT 5

As the exhibit shows, there are several factors that explain the difference in cost-to-serve (ie the total cost necessary to run and maintain the IT operations that serve business activities). These are offset by a vendor's margin, which then makes both cost bases comparable from the point of view of the agency. Broadly, the types of economic benefit are:

- *Scale and cost position,* which involves the benefits associated with higher volumes and advantages such as lower cost of technology or labour.
- *Quality and efficiency,* which involves advantages such as more efficient, simplified processes, and access to better or more skills and expertise.
- *Risk exposure,* which involves advantages such as lower costs to cover the same risks, or lower costs to repair damages if and when they occur.

The economic diagnosis tool describes three steps for calculating perceived value. First, agencies should understand their current ICT costs. Second, they should understand, in broad terms, how these costs compare with hypothetical alternatives. Third, they should disaggregate perceived value into its major components – in other words, How does perceived value break down along the four major drivers shown in Exhibit 5?

The tool describes three approaches that agencies can use to perform the second step. In each of these approaches, the actual process of analysis will vary according to an agency's current strategy. An agency that self-manages ICT will begin on the left-hand side of Exhibit 5, with the initial annual cost base for ICT, and will use one of these approaches to derive the value on the far right-hand side. An agency that has a single or selective sourcing strategy will begin on the right-hand side of Exhibit 5, with the annual face price of each existing arrangement, and will use one of these approaches to derive the value on the far left-hand side. In both cases, an agency should be able to compare the costs of its current sourcing strategy with the estimated cost of an alterative.

To perform the third step, agencies then need to disaggregate perceived value, regardless of how it was calculated, into its four drivers: scale and cost position; quality and efficiency; risk exposure; and vendor margin. The specific elements that typically make up these drivers are described in the economic diagnosis tool.

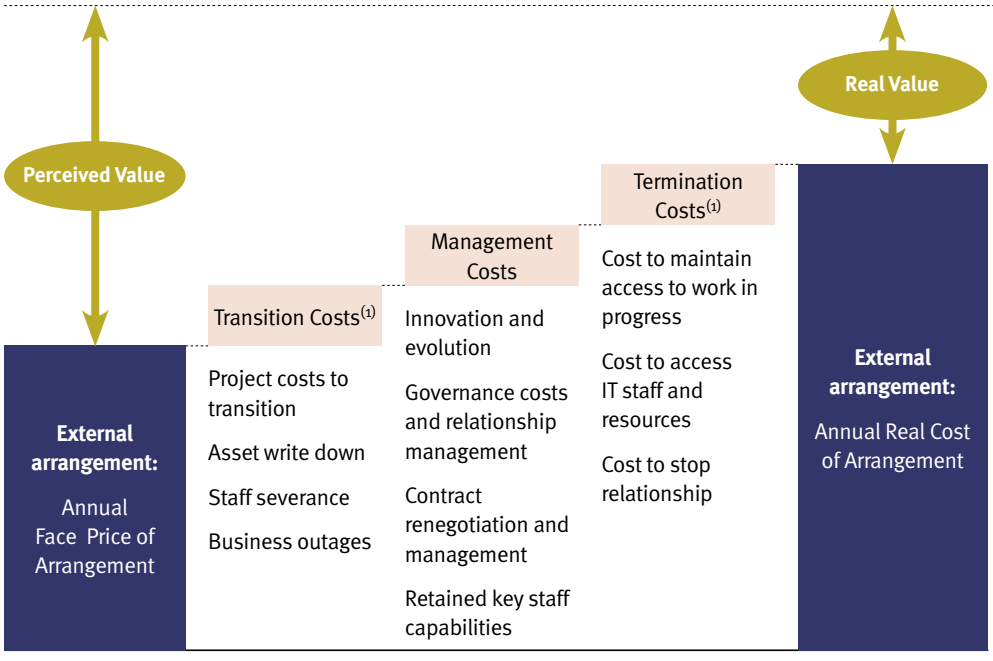
The purpose of this step is to explain the difference between the self-managed option and an external arrangement; to highlight the most significant factors that account for this difference. It is therefore more important for agencies to understand these drivers, broadly, than it is to get an exact value for each one.

With this breakdown complete, agencies should have a clear view of the overall magnitude of perceived value, along with its key sources. However, this is only the first step towards understanding the costs and value of a sourcing strategy.

ICT sourcing decisions must consider the real value of an arrangement

Agencies need to recognise that perceived value excludes other costs that are incurred solely because of the sourcing arrangement – these costs need to be assessed in order to understand the real value of a sourcing arrangement. For instance, there are transition costs for moving the ICT activity from one model to another; management costs for governance and contract management; and termination costs, which entail the cost to maintain access to work in progress, or to ICT staff and resources, once the contract expires.

EXHIBIT 6



(1) Distributed over the contract duration

Factoring these costs into the perceived value produces a picture of the real value of either an existing or hypothesised sourcing arrangement (Exhibit 6).

Agencies that self-manage ICT will work their way towards a real value calculation by using benchmarks to estimate the three components that sit between perceived value and real value: transition, management and termination costs. The tool provides checklists for the various costs agencies should plan for. These costs will be compiled on top of the annual face price of an optimal single or selective sourcing strategy (as derived during the perceived value calculation).

Agencies that have single or selective sourcing strategies, on the other hand, will estimate these costs based on historical information for transition costs; current data for management costs; and estimates based on clauses in the contract for the termination costs. The tool provides checklists for where to look for this information. When detailed historical information for transition costs is not available, which often happens, an estimate has to be made. Agencies could, for instance, assume that these costs are no more than the increase of ICT budget that was experienced during the last transition.

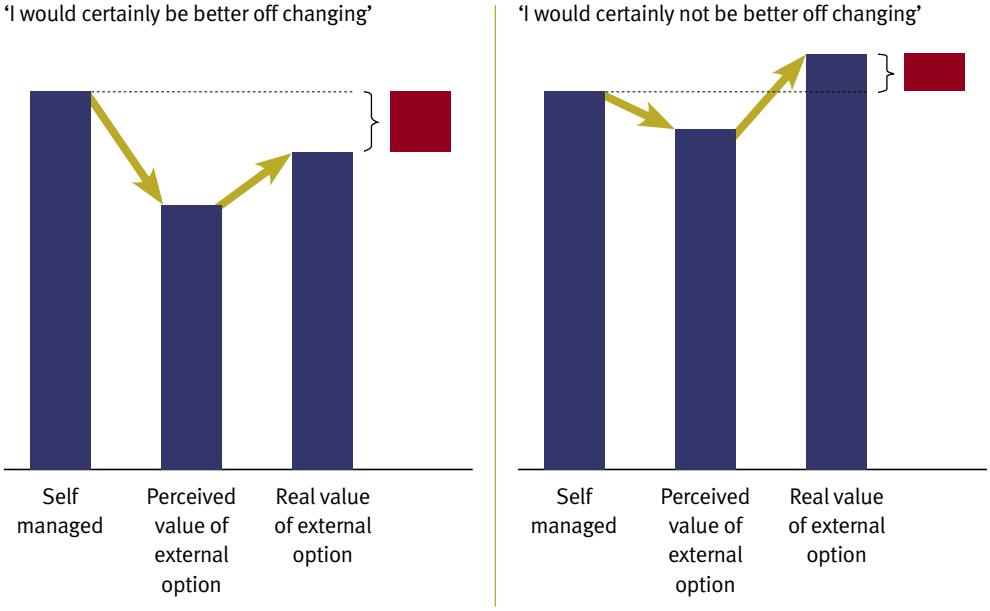
At this point in the analysis, it is not necessary for agencies to run a complex exercise. The intent is not to perform an analysis and come up with a fully certified number. Instead, agencies should focus on performing analysis that will give them enough confidence in the numbers to allow them to take one of three positions, from an economic perspective:

- I would certainly be better off changing,
- I would certainly not be better off changing, or
- Both scenarios show similar costs, and it would be difficult to justify a case for change.

Exhibit 7 illustrates how real value analysis could steer an agency toward these conclusions.

EXHIBIT 7

Comparing the value/cost of an external option with an existing self-manage approach



The analysis should also be rigorous enough to allow an agency to understand the cost drivers of the current solution and to compare these drivers with other scenarios.

Assess current satisfaction

The fourth and final step in building the case for change is to assess the satisfaction with the current sourcing arrangements. Exhibit 8 provides a checklist for assessing sourcing satisfaction for externally managed arrangements.

EXHIBIT 8

Checklist for Assessing the Qualitative Value of your ICT Sourcing Contract(s)

Relationship	• Is your overall relationship with your vendor open and constructive? • Is the relationship flexible and cost-effective in meeting changing volumes? • Is the relationship flexible and cost-effective in rapidly responding to agency needs for new technology? • Is the relationship flexible and cost-effective in rapidly responding to new Ministerial and legislative requirements?
Staffing	• Has the productivity of agency staff been negatively impacted during the life of the contract? • Are you happy with the vendor team's understanding of the agency's business? • Has the vendor's team been of a consistently high quality? • Has the vendor maintained a consistent team throughout the life of the contract? • Has the vendor transferred knowledge to your team effectively? • Is the agency happy with the influence it has over vendor staffing?
Contract	• Has there been transparency in pricing, volumes, SLAs and invoicing throughout the life of the contract? • Has the contract stayed intact throughout the relationship? • Have there been any issues that have not been resolved by the direct relationship management team? • Are there any looming issues if you decide to switch to a new vendor?
Innovation	• Are you comfortable that you have benefited from natural technology evolution over the period of the contract? (lower technology unit prices, technological innovation) • Do you feel that the vendor has sufficiently innovated your ICT functions?

At this point, an agency should have a clear picture of its overall ICT sourcing situation – in particular, its business priorities and corresponding ICT requirements, the key opportunities that can be leveraged from other agencies, the real value of existing and alternative sourcing arrangements, and the current satisfaction with sourcing. It should therefore be prepared to 'make or break' the case for change.

Previous assessments could also lead the agency to identify re-engineering needs. For instance, one agency's pricing model for outsourcing did not encourage the vendor to reduce the number of servers, as the contract specified a price per server, independent of whether it was actually used. After several years of Machinery of Government and business needs variations, the agency was paying too much for what it was getting from ICT. But the numbers and functions of servers were not questioned, because the contract did not stipulate any re-engineering of ICT operations.

Articulate the trigger point for change

To test their case for change, agencies should perform a trigger point analysis. As with previous analyses, this will vary according to whether an agency currently self-manages ICT or has a single/selective solution in place.

The trigger point frameworks described below, in Exhibits 9 and 10, are meant to provide agencies with a sense of the kinds of questions they should ask when exploring the feasibility of changing the current sourcing strategy. Specific issues will vary from agency to agency, but the broad questions posed in these exhibits should be relevant to most.

Assessing these trigger points for change will involve the business priorities, satisfaction with the current sourcing arrangement, and the real value analysis described earlier.

EXHIBIT 9

Trigger point for change for self-managed agencies

Is my ICT aligned with my business priorities and is it agile enough?

Is my ICT competitive when compared with experiences of similar agencies?

Do I show competitive value for money service levels?

Are agency management, customers and users satisfied with the ICT service?

Do I have access to the required capabilities?

Can I access the required people?

Do I have enough time?

Do I have sufficient funds?

Can the outsourcer provide a better service for my business?

Can the outsourcer provide more skilled people?

Are my unit costs higher than the outsourcer's?

Does the outsourcer have more efficient processes?

If I give my volume to the outsourcer, does it reduce their costs?

Can the vendor incorporate my volatility at a lower cost than myself?

Would the outsourcer pass on benefits and savings to me for the life of the contract?

- Skilled people
- Cost savings

Can I mitigate the risks of sourcing?

- Strategic
- Financial
- Operational

Can the outsourcer provide the flexibility that I need at a reasonable cost?

- Changing volumes
- Rapid response to Ministerial direction
- Innovation
- Changes to Machinery of Government

Will I be able to migrate away from an engaged relationship at a reasonable cost?

Building the case for change for agencies that self-manage ICT

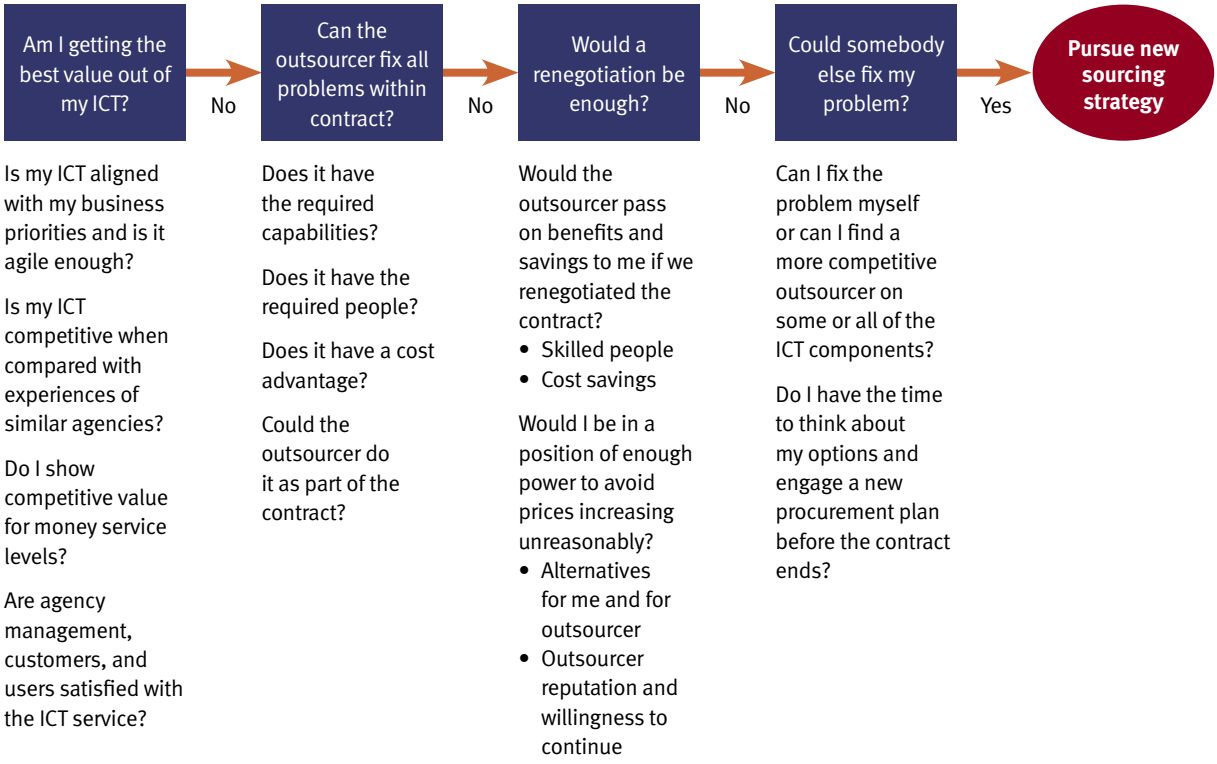
Exhibit 9 describes the conditions that an agency should meet before deciding to move to an external sourcing strategy. These are described below:

- *Is the agency getting the best value from its ICT?* The impetus for change is when an agency realises it is not getting the best value from its ICT. Agencies should then investigate sourcing strategies that will fulfil business needs and achieve better Value for Money. The satisfaction and real value analysis, described above, should help agencies make this determination.

- *Are there more efficient alternatives?* Based on the potential to improve the ICT operations, an outsourcer might be in a much better position than the agency to deliver the best value from ICT. For instance, an outsourcer might be able to run a data centre operation with a unit cost much below that of the agency, or run an application development team that yields far greater innovations.
- *Is the agency able to delegate this task to an external party without too much risk?* The relationship needs to be set up so that at least some of the value provided by the outsourcer is transferred to the agency without any unreasonable risks. In addition, the agency must be comfortable with managing a complex business relationship.

EXHIBIT 10

Trigger point for change for externally managed agencies



Building the case for change for agencies that have a single or selective sourcing arrangement

Agencies that already have a single or selective strategy in place also need to 'make or break' the case for change. To do this, they should go through a series of decisions and analyses such as the one presented in Exhibit 10.

Understand the effort to change

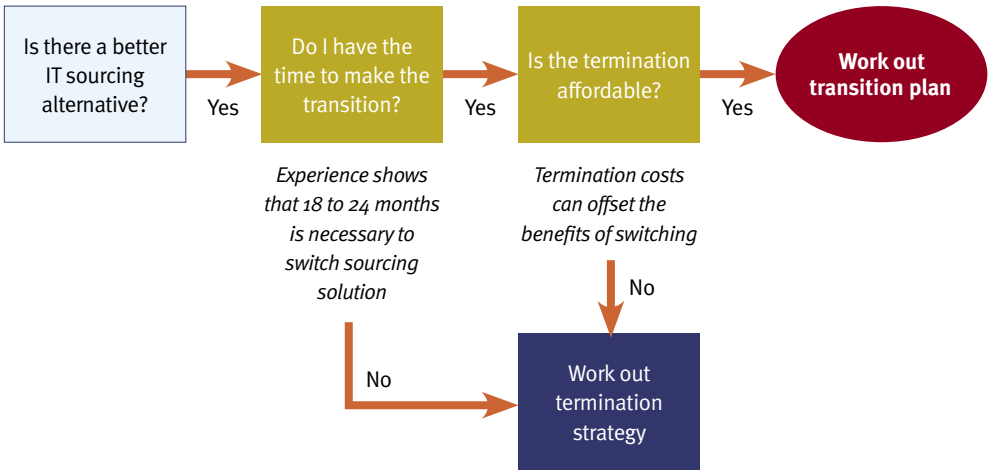
If it is clear that the current situation should be changed, the agency must ask one more question before proceeding to the next phase: Is it in a position to change?

For agencies that self-manage ICT, this will involve a change management program to help address potential cultural, legal and social issues. The cost, timing and strategic impact of such issues need to be part of the case for change, as they may offset the benefit of an option.

This question is even more critical for agencies that already have major external arrangements in place. From BCG's global experience, some organisations do not allow sufficient time or do not plan their termination strategy well enough to allow them to change when they want to (Exhibit 11). These organisations often have no choice but to exercise the extension option contained in most contracts.

If an agency is indeed restricted to its current arrangement, it should define a termination, or disengagement, strategy that will put it in a more workable position in the near term. The impetus for changing will most likely still be there.

EXHIBIT 11



A strategy for avoiding this trap mostly relies on a negotiation with the incumbent vendor, and might include the following contract-related actions:

- Negotiate a contract extension (in itself a Value for Money decision)
- Get help from outsourcer for transition to third party
- Progressively remove key projects and applications maintenance
- Standardise IT within the outsourcer
- Get the outsourcer to place staff closer to your teams
- Hire key outsourcer staff members.

Agencies could also take contract-independent actions:

- Accelerate internal decision lead-time
- Redesign governance to best practice
- Get external support or build additional resources
- Mix internal staff within outsourcer's teams
- Extend/develop relationships with other vendors.

Phase II: Decide sourcing strategy

Agencies begin Phase II knowing that they need to consider a change to their current sourcing strategy, be it self-managed, single or selective. The aim of this phase is to decide precisely the type of sourcing solution they should aim to establish. To do this, agencies need to do three things:

- All agencies, regardless of their current sourcing arrangement, need to assess their sourcing options, both strategically and economically, then select the best one.
- Agencies that have outsourcing arrangements in place may need to renegotiate their existing contracts to provide the benefits associated with the ideal sourcing option.
- Based on the new sourcing option and the outcome of the renegotiation, further procurement may need to be undertaken. If so, agencies must develop a procurement plan. At this point, agencies should have authority to implement the new sourcing strategy and have due regard to all relevant procurement policies. Agency budget constraints should also be considered during this phase; for example, are ICT purchasing ambitions consistent with available resources, and has approval been given for the proposed spending of public money?

Assess sourcing options

In this module, agencies will disaggregate their ICT and identify components that would be suitable for self-managed or external sourcing. For components suitable for external sourcing, they will also look for opportunities to bundle, factoring in the comparative risks and benefits associated with doing so. They will also decide which type of vendor relationship they require, and will consider opportunities to form sourcing alliances with other agencies.

Agencies will conclude this module by performing strategic and economic assessments of their various sourcing options, and selecting the best one.

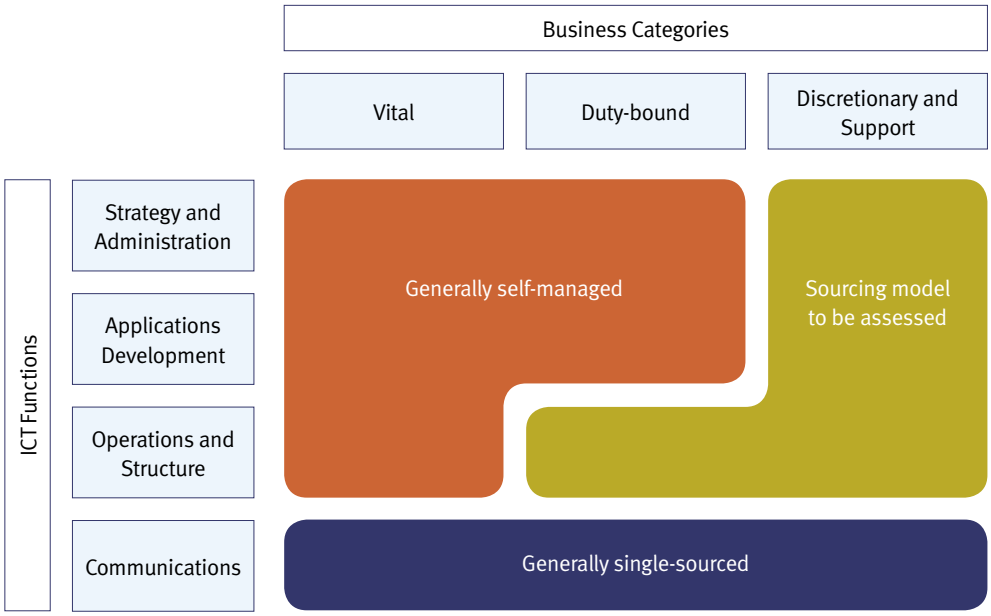
Disaggregate ICT and build broad options

In order to map out all possible sourcing options, ICT should be disaggregated along two dimensions – business categories, as described earlier (vital, duty-bound, and discretionary and support), and ICT functions. These functions are often broken down along the following lines:

- *ICT Strategy and administration:* ICT strategy; planning and control; ICT architecture; ICT security; vendor management and procurement; contract management; and training
- *Applications development:* Project management; operational applications development (CRM, ERP, SCM, etc); and functional applications development (finance and accounting, HR, etc)
- *Operations and infrastructure:* Mainframe applications, infrastructure and storage; mid-range applications and infrastructure (including web infrastructure); distributed infrastructure and LAN servers (desktop, laptops, printers, software licences, local servers); operations management (operations administration, database management, firewall, disaster recovery, etc.); and helpdesk support
- *Communications:* Communications infrastructure (PABX, videoconferencing, etc); voice (fixed and mobile); and data/ISP.

The resulting matrix should help agencies narrow down their broad sourcing options (Exhibit 12). Exhibit 12 is only indicative. Each agency should have its own understanding of what a 'vital' business activity is, and whether it could tolerate having an external vendor provide a service associated with it.

EXHIBIT 12



This exhibit provides a framework for thinking about the link between business categories and ICT requirements, and how that will affect the development of agencies' sourcing strategies. It is meant to be a starting point for determining which activities could be outsourced, not the final answer.

Agencies are more likely to consider external solutions when the business risk for a particular ICT activity is less than vital, and when:

- Activities are standard and common to a large class of agencies, allowing the outsourcer to reach economies of scale and absorb risks, or are too small to justify an internal capability.
- Activities have predictable business requirements and likely volumes (within parameters) over the life of the contract; involve stable technologies where knowledge about how to specify, measure and manage them is well-codified; or are stand-alone, with few impacts on other systems and processes in the agency.
- Alternative vendors are available for the service, forcing more quality deliveries, and the service involves little customisation (which would empower the outsourcer).
- There is a potential to generate better Value for Money.

Identify opportunities to bundle ICT components

Agencies that have determined that some of their ICT functions should be managed externally need to assess whether there are opportunities to bundle some functions together. This will determine whether the agency should pursue single or selective sourcing – if all the elements suitable for external sourcing can be bundled into one group, then single sourcing is the appropriate strategy; multiple bundles lead to a selective sourcing strategy.

In general, single sourcing is better suited to agencies in which ICT is not highly strategic or customised, or to small agencies, because it is easier to manage. These arrangements only require a single vendor negotiation. The vendor assumes risks, even for ICT functions where it is not a specialist, and it may subcontract some functions to other vendors (for which the agency potentially pays a management margin). This is likely to be more cost-effective for small agencies than managing multiple vendors.

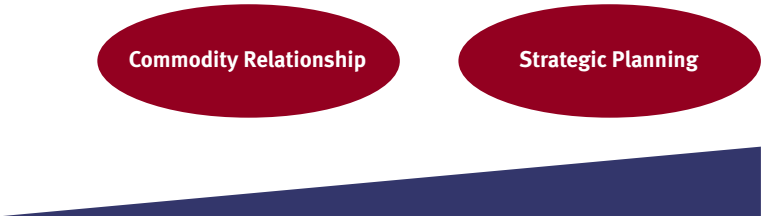
In general, selective sourcing is better suited to larger agencies or agencies where some ICT functions are highly specific or strategic. It provides greater control and delivers higher performance. However, it also requires multiple vendor negotiations and, although risks can be shared across multiple vendors, the coordination risk is borne by the agency. An agency may choose to designate one of them as the 'prime' contractor, to mitigate integration and management costs. The prime contractor would assume responsibility for coordinating and managing other vendors.

The major benefit of selective sourcing over single sourcing is clear: it allows agencies to access best-of-breed services across their ICT components. But this model also poses challenges. In particular, it results in significantly increased complexity – as agencies must cope with managing several vendors at once – and demands greater expertise in governing stakeholders with different motivations. The cost of coordination/governance should be a major criterion for deciding whether to separate functions or bundle them (this factor, along with other criteria, will be measured later in this module, when agencies assess the economic and strategic benefits of potential sourcing strategies).

Determine the type of vendor relationship required

The type of sourcing relationship varies according to the degree of access and influence given to a vendor to improve business performance (Exhibit 13).

EXHIBIT 13



Expectations	• ICT process efficiency – low costs – no innovation – no shared risks – full control	• Business value – high quality/efficiency – innovation – equity risk shared
Suitable Activity	• Process intensive • High volumes • High fluctuations • Low strategic value	• Highly ICT dependent • High strategic value • Customised ICT • Large customers

On one end of the spectrum are 'commodity' relationships, which are generally used when the priority is to control or reduce costs, rather than develop innovative ways for technology to improve performance. On the other end are 'partner' relationships that are based on in-depth collaboration. This suits ICT components that are strategic, particularly where the technology needs to be customised and can play a key role in improving business performance. For these components, receiving the highest quality ICT service takes precedence over cost savings. In between these models are varying degrees of engagement, all of which involve different trade-offs between the elements that determine the real value of the arrangement.

Consider undertaking alliances with other agencies

Small and medium-sized agencies wishing to adopt a single or selective sourcing model may want to partner with similar agencies for some or all aspects of the lifecycle (such as negotiation, contract development, etc). The two main benefits of these alliances are shared costs and heightened negotiation power during the development of the sourcing strategy, the implementation of the vendor selection process, or even during the management of the contract. This does not necessarily mean agencies share the same contract; they can have their own.

We have defined two types of alliance that agencies may want to consider:

- *Big Brother:* Align with a larger agency that has similar needs, or has sourcing arrangements that appear to be suitable.
- *Swarm:* Two or more agencies group together to reach critical mass. They need to have similar needs in terms of business and ICT functions, Machinery of Government and business cycles. They could have a joint contract with the vendor, or individual contracts. The following table outlines the pros and cons of each option.

TABLE 1: COMPARISON OF ALLIANCE OPTIONS

	Pros	Cons
Big Brother	• Ability to share costs of procurement, contract negotiation, and potentially disengagement • Ability to leverage strong expertise in ICT management • Ability to potentially obtain better service levels (disaster recovery sites, etc)	• Most compromises will benefit the large agency • Priority usually given to large agency • Less responsiveness from vendor • Risk of incurring costs generated by large agency • Risk of lack of transparency in the invoice • High risk of Machinery of Government impact
Swarm	• Ability to share costs of procurement, contract negotiation, and potentially disengagement • Increased power and ability to procure large and skilled vendors • Ability to be more innovative and efficient through sharing transferable best practices	• Risk of slow decision making process • Difficulty of aligning requirements increases with number of agencies • Higher negotiation or change request costs in business as usual • High risk of Machinery of Government impact

Assess options strategically and economically

At this stage, agencies should have an understanding of the sourcing options. To choose the most suitable one, they need to conduct a strategic and economic assessment of each one. Assessing risk is an important part of this process. Effective risk management can help agencies determine which risks to reduce, transfer or avoid, as well as which risks to accept, potentially opening up significant opportunities.

The following three tables provide some areas for agencies to consider when assessing strategic fit and economic benefits. There is one table for each set of options faced by agencies that currently have a self-managed, single, or selective ICT sourcing strategy.

TABLE 2: OPTIONS FOR AGENCIES THAT CURRENTLY SELF-MANAGE ICT

Scenario	Potential benefits	Potential constraints, drawbacks, and risks
No change	• Maintain level of control and responsiveness to business requirements • No business disruption and potentially better fit and innovation for business • No procurement process required • Maintains current capabilities	• Purchasing power limited to agency's size • Innovation limited to current capability and learning processes • Lack of incentive to control consumption of common IT resources • Difficulty to recruit or retain staff
Change to single vendor	• Economies of scale • Greater availability and range of skills, better expertise • Better focus on core business • Better match of resources to demand • Access to skilled personnel	• Requires careful assessment of termination costs (i.e. existing staff, assets) • Need to identify risks and establish a risk mitigation strategy • Procurement costs • New vendor does not know agency business • Need to build new relationships • Need for contract management skills • Loss of control • Transition costs and duration might be significant • Flexibility in change requests subject to contract arrangements
Change to selective sourcing	• Best-of-breed benefits: better service levels, specialist skills, low costs to operate • Provide services not available internally • Better focus on core business • Maintains a certain level of cost transparency • Ability to select from more vendors	• Requires careful transition sequencing to avoid service disruption • High procurement costs • New vendors do not know agency business • Need to build new relationships • Need for contract management skills • Agency keeps most delivery risks • Complex contract governance • Need to address cross-vendor disputes

TABLE 3: OPTIONS FOR AGENCIES THAT CURRENTLY OUTSOURCE THEIR ICT TO A SINGLE VENDOR

Scenario	Potential benefits	Potential constraints, drawbacks, and risks
No change	• Contract variation or renegotiation may lead to better outcome given the difference between today's requirements and when original contracts were signed • No procurement costs • No business disruption • Established relationship • Known performance history	• May indicate a restrictive situation (however, renewal may only be deferring high termination costs) • Increased costs may result from renewed contract
Change to another single vendor	• Better business outcomes as a result of a better arrangement with new vendor	• Careful assessment of transition and termination costs • Procurement costs • Complex hand-over • May discourage other bidders because of incumbent vendor • New vendor does not know agency business • Need to build new relationships • Need to identify risks and establish a risk mitigation strategy
Change to selective sourcing	• Best-of-breed benefits: better service levels, specialist skills, low costs to operate • Low risk approach • Provides a better level of cost transparency • Ability to select from more vendors	• Requires careful transition sequencing to avoid service disruption • Careful assessment of transition and termination costs • High procurement costs • May discourage other bidders because of incumbent vendor • New vendors do not know agency business • Need to build new relationships
Change to self-managed	• Increase level of control and responsiveness to business requirements • Increase transparency in ICT costs • No RFT procurement costs	• Requires strong business case to justify move (contestability) • Reduced focus on core business • High transition costs to rebuild internal resources and recover asset base • May have high termination costs • Investment in innovation limited to available budget for resources/ training

TABLE 4: OPTIONS FOR AGENCIES THAT CURRENTLY OUTSOURCE THEIR ICT TO MULTIPLE VENDORS

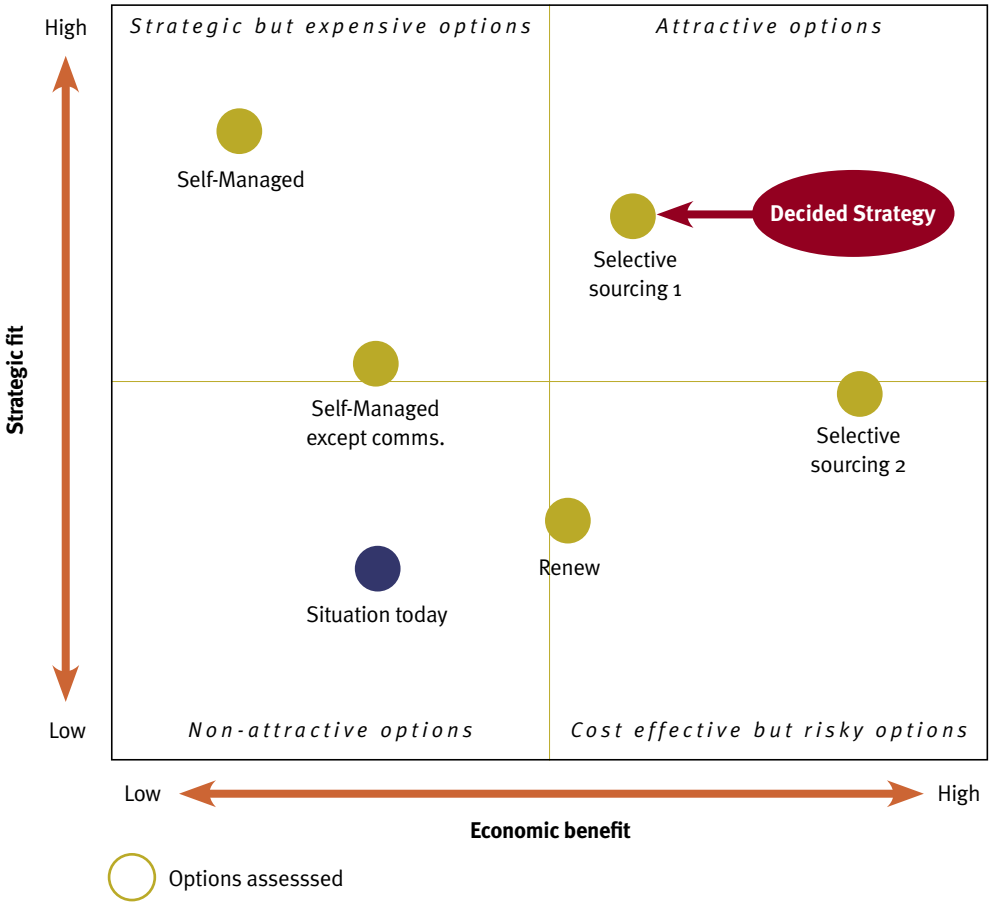
Scenario	Potential benefits	Potential constraints, drawbacks, and risks
No change	• Known performance history for each vendor • Competition across vendors maintains pressure on each one • Established relationships • No procurement costs • Known contract management requirements for multiple contracts • No business disruption	• Increased costs may result from renewed contract • High coordination costs
Continue selective sourcing, but with some new vendors	• Better best-of-breed benefits • Low risk approach • Medium transition costs	• Requires careful transition sequencing to avoid service disruption • New vendors need to be effectively integrated into operational arrangements • May discourage other bidders because of incumbent vendors • New vendors do not know agency business • Need to build new relationships
Change to single vendor	• Reduces coordination and management costs • Better integrated business • Clearer responsibilities	• Careful assessment of transition and termination costs for each vendor • New vendor does not know agency business • Need to build new relationship • Need to establish a risk mitigation strategy • Less transparency of the costs • May increase overall costs
Change to self-managed	• Increases level of control and responsiveness to business requirements • Increases transparency in ICT costs • No RFT procurement costs • Eliminates multiple contract management complexity	• Requires strong business case to justify move (contestability) • Reduced focus on core business • High transition costs to rebuild internal resources and recover asset base • May have high termination costs • Investment in innovation limited to available budget for resources/ training • Complex transition back in-house because of multiple vendors

These tables should provide broad guidance to agencies as they assess their options. In addition, the economic assessment will utilise the real value analysis that was described earlier (and is also detailed in Appendix A), and the strategic assessment should score options against preferred strategic and satisfaction criteria, such as expected service levels, tolerance of risk, constraints, etc. The elements of strategic assessment will vary by agency, as will their weightings.

Based on this analysis, the agency should be able to map each sourcing option on the following matrix, in order to identify the relative priority of each one (Exhibit 14). One of the options could include re-engineering ICT operations, as mentioned earlier.

This portfolio view of the sourcing options, along with the analysis justifying their position on the matrix, will help management rationally decide the most suitable sourcing strategy. This module should result in the selection of the best sourcing strategy for the agency.

EXHIBIT 14



(Illustration only)

Renegotiate existing contract

This section only applies to agencies that have external arrangements in place. If the current contract had been signed several years ago, it may not fulfil today's needs as efficiently as it used to, and there may be significant room for improvement. In this situation, it may be appropriate to investigate the alternatives in the marketplace. First, however, agencies should review existing contracts to identify any provisions and requirements for extending these contracts.

If, after an analysis of the market, the current arrangements represent best Value for Money, agencies should negotiate with the outsourced service provider to renew the contract. The new contract can then be drafted and signed. It should be noted that a contract extension is in itself a procurement, which necessitates its own Value for Money decision. If the negotiation is unsuccessful, the next step is to develop a procurement plan. In either case, the outcome of the renegotiation may change or somehow alter the strategy that was selected in the previous module.

The timing for renegotiation should take into consideration: the extension option deadline; the proximity to the contract end-date; and potential reactions from other vendors and from the incumbent.

Develop procurement plan

As they begin to develop a procurement plan, agencies must be aware of the context in which Australian Government agencies conduct duties in relation to procurement, and of the relevant processes and regulations that they need to comply with. These are briefly described below. Agencies should refer to Appendix B for more details.

- *Financial Management and Accountability Act 1997 (FMA Act)*
  The FMA Act and its associated Regulations provide the legislative framework governing financial management in all FMA agencies, including proposals for spending public money. The Act requires agency Chief Executives to promote the efficient, effective and ethical use of the resources for which they are responsible.
- *Commonwealth Procurement Guidelines and Best Practice Guidance (CPGs)*
  The Guidelines set out Value for Money as the core principle underpinning procurement under the FMA Act, and articulate the policy framework that officials should consider when performing duties in relation to procurement.
- *Agency Chief Executive's Instructions (CEIs)*
  An agency's CEIs provide an agency-specific codification of the financial management framework, including provisions related to procurement. They are the primary source of information on operational guidance for agency officials conducting procurement.
- *Industry Development Requirements for Major ICT Purchases*
  To advance one of the key objectives of the Australian Government's ICT outsourcing policy, there are mandatory participation levels for small to medium-size enterprises in ICT contracts of expected value of $20 million or more. See Commonwealth Procurement Circular 02/2 at http://www.finance.gov.au/ctc/cpc_02_2_id_requirements_for_m.html.
- *Best Practice Policy Guidance*
  The Department of Finance and Administration issues guidance material in relation to various aspects of Australian Government procurement policy. This guidance material is available at http://www.finance.gov.au/ctc/toolkits/procurement_guidance.html.
- *Endorsed Supplier Arrangement (ESA)*
  This process provides pre-qualification for businesses selling ICT goods and services to the Australian Government. It is mandatory for use by all FMA Act agencies for all ICT goods and services to which the arrangement applies. The obligation to use the ESA also extends to outsourced service providers in their engagement of sub-contractors. More information about the operation of the ESA is available at http://www.esa.finance.gov.au.
- *Government Information Technology and Communications Contracting Framework (GITC)*
  This facility is a legal framework developed by the Australian Government in conjunction with industry representatives to provide standard terms and conditions for the purchase of ICT goods and services, including major office machines and telecommunications. Use of the framework is not mandatory, and it is best suited to smaller and less complex procurements. More information is available at http://www.gitc.finance.gov.au.

- *Whole-of-Government Telecommunications Arrangements (WOGTA)*
  The Whole-of-Government Telecommunications Arrangements is a contracting framework managed by AGIMO. http://www.agimo.gov.au/infrastructure/telecommunications.
- *Volume Software Supply (VSS)*
  These are contracts for Volume Software Supply to the Australian Government that have been established and that agencies are free to use. http://www.agimo.gov.au/infrastructure/agreements.

Determine business and ICT service requirements

Once they understand these procurement policies and regulations, agencies should kick off the development of the procurement plan by determining the in-scope requirements. There are two types of service level requirements to consider. Each should be derived from the agency's strategic objectives and should support business priorities defined earlier. They are:

- Business service levels; and
- ICT service levels.
- Mix of both

The type of relationship expected from the vendor – as defined earlier in this phase – will help to determine these requirements. A commodity-type contract will mostly use service level requirements around ICT metrics, whereas a partner-type contract should include more business metrics.

Both types of service requirement should be captured in the form of draft Service Level Agreements (SLAs). An SLA sets out the service provision arrangement between an agency and a vendor, outlining each party's obligations in regard to service provision and identifying how they will work together to achieve the agreed objectives. It is included in tender documentation and refined during clarification/negotiation processes to form a schedule in the Services Contract.

For each service, an SLA should specify at least the following elements:

- Name of service
- Criticality for the business
- Business continuity importance
- Performance metrics
- Minimum service level required
- Business impact and risks incurred if minimum service is not met
- Consequences of non-performance
- Terms for default
- Customer obligations
- Pricing metrics and unit prices
- Likelihood of evolution on client side
- Likelihood of evolution on vendor side
- Exercisable options and pricing
- Conditions and responsibilities in case of unexpected change.

Agencies should include, as part of the SLAs, a requirement for each tenderer to submit a transition plan as part of its proposal. As noted in the list above, the SLAs should also consider the ways in which an agency's mission – and therefore its requirements – may evolve during the contract.

Decide between open tender and restricted tender

Agencies need to decide whether to pursue an open or restricted tender process. The default choice is for an open tender process, which provides the widest range of competition and therefore of potential solutions. The costs and complexity of an open process should be balanced by the improved Value for Money that can be achieved through competition.

Agencies can opt for a restricted tender process when they can provide a defensible short-list of vendors. In short, they must be able to show reasons why they are only requesting proposals from a limited group of vendors – for example, because after an analysis of the market the agency has a comprehensive knowledge of the range of potential vendors, and can easily identify those that can fulfil the requirements and provide the best Value for Money. Whichever procurement method is chosen, agencies should of course document this decision and the reasons for making it.

Define the list of vendors in case of a restricted tender

If the agency chooses a restricted tender process, it should develop a prioritised list of vendors, based on two dimensions: service delivery capability and management capability.

- The assessment of the service delivery capability should consider aspects such as customer references; clarity of services, roles, and responsibilities; SLAs, metrics, and performance measurement programs; and service innovation.
- Management capability should be assessed according to each vendor's management practices, methodologies and processes; financial performance and stability; market position (analyst ratings); and process expertise.

Agencies should then map all potential vendors onto a matrix that includes both of these dimensions (Exhibit 15). Assuming the assessments remain fact-based, this will allow agencies to rationally determine the restricted list of vendors who will be approached.

EXHIBIT 15

Matrix For Selecting Vendors To Continue In The RFT Process

Decide the level of collaboration with vendors in the tender process

Agencies then need to decide the level of collaboration they are comfortable with during the tender process. They can begin by considering two extreme scenarios:

- The 'black box' approach involves a formal tender process, usually based on criteria that emphasise service levels and price differentiation. There are no close interactions with vendors. To push their offer over the winning line, vendors often end up cutting their prices by reducing service levels, rather than improving the underlying business solutions. This approach is usually fair and quick, because the level of interaction is limited, but also higher risk, because the mutual understanding of each other's business is limited.
- The collaborative approach revolves around open discussions to clarify both the agency's needs and the vendor offers. The selection criteria aim to arrive at a mutually beneficial intersection of the vendor's capabilities and the client's requirements. As a result, to push their offer over the winning line, vendors tend to upgrade or customise their solutions rather than cut service levels. This usually results in a less risky outcome but may be more expensive and time consuming. This approach could also entail frank discussions about each party's costs.

In the end, the agency will have to adjust each of the main collaboration parameters (Exhibit 16) in order to both comply with the Australian Government policies and also maximise their Value for Money solution. Agencies may wish to utilise the services of a probity adviser, in order to ensure that all processes are proper and ethical and that tenderers are treated consistently and equitably in accordance with set procedures.

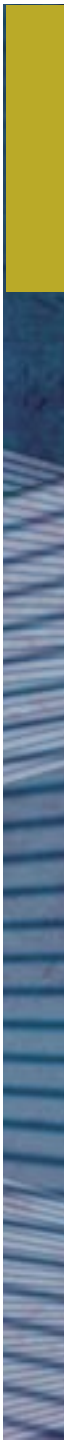
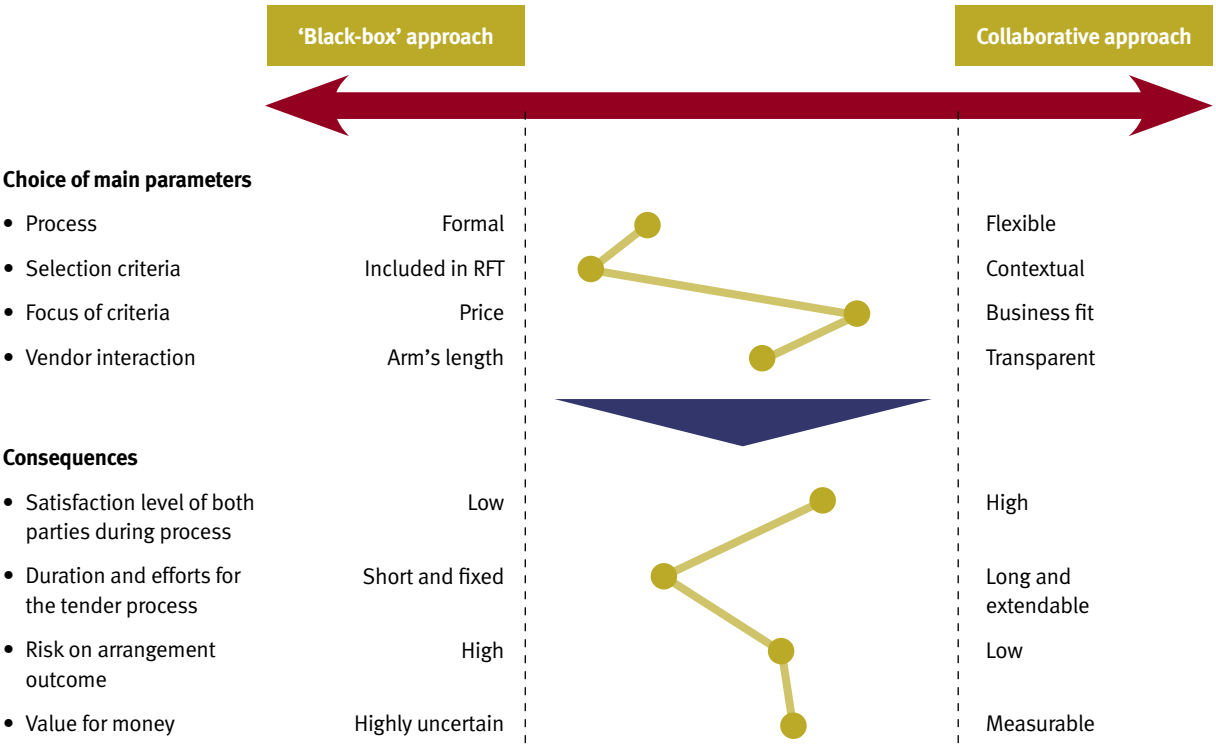


EXHIBIT 16



(Illustration only)

Define selection criteria

At this point, agencies should develop a list of qualitative and quantitative criteria for assessing and scoring vendors. These criteria, along with any relevant weightings, will be included in the RFT. An example of selection criteria is shown in Exhibit 17.

Since many scores will be based on subjective assessments, often by different individuals, an effort should be made to make the scores consistent and equitable. This can be done by discussing and clarifying, as a group, the nature of the criteria, and arriving at an agreed interpretation for each one. Likewise, a common understanding should be reached on rating scales.

Prepare for both-way due diligence

Due diligence is an important process that enables agencies to better understand legal and strategic risks and allows tenderers to better understand an agency's requirements. A well-managed due diligence process leads to improved solutions and fewer qualifications. The more information that tenderers have access to, the more likely they are to submit tenders that are competitively priced (as they do not have to build contingencies into their pricing to cater for risk) and are better able to meet agency requirements. Prior to this process, agencies should refer to their probity plan in regard to managing the provision of information to potential providers. Agencies should also have in place proper procedures for the identification and treatment of confidential information in relation to their tendering and contracting activities.

EXHIBIT 17

Examples of selection criteria

Ability to deliver service
- Quality of infrastructure and operations services; suitability of locations; Australian Government ICT security requirements, etc.
- Strengths and weaknesses

Service levels, metrics, processes
- Approach to delivery of service levels; commitment to service levels; etc.

Transition plan
- Quality of transition plan; risk management approach; quality of staff proposed; etc.

Nature of proposed agreement
- For commercial management interface, service management interface and delivery; etc.

Cost proposal
- One-time and recurring costs for each service package
- One-time transition costs
- Real value analysis

Service management capability
- Internal service management frameworks, compliance with Australian Government service management requirements

Secure Information management capability
- As appropriate, can securely process classified information in accordance with the PSM and ASCI 33.

Capability to support the Australian Government's sourcing environment
- Experience working flexibly and cooperatively in a multi-vendor environment, working in environments of similar size and complexity to that identified in the RFT
- Ability to service out-of-scope requirements as requested by the Australian Government

Compliance with bidding process
- Schedule compliance; provision of required information; etc.
- Pricing, service level and service rebate approaches / structures vendors are comfortable with

Potential for ease of contract negotiations
- Changes proposed to requirements and terms & conditions; etc.

Quality of vendor performance during bidding process
- Professionalism; expertise; content and structure of meetings; quality of proposal; etc.

Quality of proposed staff
- Management transition team; service delivery managers and staff; etc.

Supplier profile
- Focus on sourcing; company financial stability; personnel & facilities; etc.

Added value proposed
- Evidence of demonstrable added value in the technical/ operational solution; etc.

Agencies may want to give an overall weighted score on value for money as it has been stressed as a major criterion by Commonwealth policies

Agencies should begin compiling material and data that is relevant and appropriate for release during due diligence. The information will need to be comprehensive enough to allow tenderers to develop clear pricing bases and technical proposals. It is likely, however, that tenderers will seek access to further information on an agency's ICT environment. To the extent this information is held in a recorded format (electronic or otherwise), it should be collected in a central repository or data room that can be visited by tenderers.

Tenderers may request interviews with agency staff to understand the specific circumstances of an agency's operations. Agencies need to prepare for those interviews by anticipating likely subjects of discussion and ensuring that the necessary resources are available to conduct the interviews (agencies can request that tenderers provide a list of subjects they want to discuss beforehand to assist preparation and ensure that interviews are relevant).

Develop a transition/termination strategy

Excessive termination costs are generally due to unexpected issues concerning intellectual property rights, residual value of equipment, transfer of assets or remaining lease payments, assistance from the incumbent vendor to transition to a third party, and any potential damage costs. As discussed in more detail in the next phase, these costs need to be identified at the outset of the contract, and then factored into the calculation of the real value of the arrangement. However, at this point in the lifecycle, agencies should begin to develop a view of the key elements that will need to be managed in order to keep these costs under control.

Develop a draft contract

Agencies may wish to draft a 'target' contract, which captures the key elements that will ultimately be included in a contract, such as SLAs, selection criteria, and termination clauses (more specific aspects of the contract will only be written once the agency has begun negotiations with its chosen vendor).

These elements may include:

- Overall business & legal agreement
  - Master agreement (including key business success factors and expected benefits from the relationship)
  - Country agreements
  - Complete executable contract document
  - Contract governance arrangements and staffing
- Technical agreement:
  - Statement of work – scope of services
  - Service levels
  - Facilities
  - Third party contracts to be transferred
  - List of transferred equipment and software
  - Termination arrangements
  - Reports and meetings
  - Security and regulatory compliance
- Finance benchmarking and pricing
- Transition plan (IT assets and people)
  - Key stages, phases, activities, and milestones
  - Resources
  - Financial penalties
  - Credits
- HR agreement
  - Key supplier positions
  - Transferred employee offer letters
  - Communications approach.

At the end of this module, agencies should have all the elements to secure the authority to proceed with the new sourcing strategy.

Phase III: Undertake procurement

Agencies should enter this phase with a clear understanding of the value of their current arrangement and the nature of the sourcing solution they are aiming for, with their scope of requirements clearly identified. If the best sourcing strategy is to self-manage, agencies do not need all the details provided in this Phase, but they may need to prepare for a transition (the transition process is described in Phase IV). Where agencies are aiming for an external solution, they will need to follow three modules during this phase:

- Implementing the procurement plan
- Selecting vendors
- Developing contracts.

For large agencies, this phase could take from six to twelve months; for small agencies, it could only take two to three months. This phase should be performed for each tender the agency wishes to pursue.

Implement procurement plan

The outcome of the first module of Phase III is to initiate the market approach, as defined in Phase II, to a number of vendors and to receive their proposals. It involves the following steps.

Proceed with the notification to industry

Agencies may choose to announce an impending release of an approach to market by advertising a notification to industry in relevant newspapers several weeks prior to the release of the approach.

Get confidentiality agreements signed

No confidential information should be provided to interested persons until they have signed an appropriate confidentiality deed/undertaking. It is essential that all third party documents – software licences, contracts, reports or other records – are checked for confidentiality restrictions and cleared with the relevant third parties before being made available to tenderers.

Write and issue market approach documentation

Agencies need to write market approach documentation based on the requirements that were sketched out in Phase II, and then issue it according to the tender process, be it restricted or open. The different market approach alternatives are listed below (a more detailed description can be found in Appendix C):

- Request for Expressions of Interest (REOI)
- Request for Information (RFI)
- Request for Quotation (RFQ)
- Request for Proposal (RFP)
- Request for Tender (RFT).

Agencies should consider their requirements and existing market conditions, and select a procurement method on its merits. They should also consider ways that the process can identify Value for Money solutions and contribute to agency efficiency and effectiveness, while recognising the resource impost of unsuccessful tenders on industry.

In some circumstances it may be appropriate to undertake a staged short-listing through a Request for Expressions Of Interest (REOI), to narrow the field of tenderers or clarify market preferences for bundling of services. Agencies will need to establish clear criteria for short-listing and invite expressions of interest or statements of capability from potential tenderers, from which a short-list can be established. The broad criteria for short-listing should be disclosed to potential tenderers and then applied consistently in the short-listing process.

In circumstances where requirements are clearly identified and time is a critical factor, agencies may choose to proceed directly with a Request for Tender (RFT).

Conduct kick-off sessions or an industry briefing

Agencies may wish to conduct kick-off sessions that provide a detailed, interactive review of the technical and operational environment and SLAs, and of the objectives and expectations for sourcing. These sessions will be informed by the qualitative and quantitative criteria in the RFT, and will better align agency requirements and expectations with vendor capabilities and solutions. Agencies should ensure that they are attended by personnel who have enough knowledge of the technical environment and operations to answer detailed questions.

When the tender process is open, agencies should conduct an industry briefing for all interested vendors.

Conduct pre-proposal due diligence

The market approach should stipulate that tenderers must perform all due diligence before they submit their tenders, and that tendered prices must not be conditional on further investigation or due diligence after the evaluation process is complete. This requirement ensures that the tender process is not prolonged or compromised by ‘indicative’ pricing, which is subject to further review.

Sufficient time should be allocated to this phase to ensure that tenderers have the opportunity to develop carefully considered offerings. Tenderers could need from four to eight weeks from the date of issue of the RFT to conduct due diligence and prepare their proposals, depending on the size, breadth and complexity of the project. Exhibit 18 provides an overview of what tenderers usually expect from agencies during due diligence.

EXHIBIT 18

Data Room	Site Visits	Interviews and Work Sessions
Contains agency data required for vendors to ratify proposals • Asset inventories and book values • Copies of third-party supplier agreements(1) • Technical documentation – Configurations – Technical performance reporting • Organisation structures • Headcount of in-scope employees & contractors by service area and location • Labor agreements, benefit plans, pension plans • Labor and benefits costs	Vendors tour in-scope agency facilities Technical review & validation • Confirm condition of in-scope hardware • Confirm environmental surroundings for in-scope hardware	Vendor meetings with agency representatives to cover various issues, eg • Analyse third party contracts • Value assets and determine transition approach • Validate technical and operational proposals • Collaborate on technical and operational solutions • Define interfaces between organisations • Collaborate on employee transition approach Strict agendas used for all meetings

(1) Sharing third party contracts requires permission from contract signatories

Select vendors

The outcome of this second module of Phase III is to select vendor(s) for the ICT components that will be managed externally.

Review proposals for completeness

Upon receiving the proposals, the first step is to review them for completeness and conformity with the market approach documentation (e.g. RFT) requirements. Incomplete proposals should be sent back to the vendor for revision, or be disqualified.

Screen proposals

The evaluation process generally involves two basic tasks:

- An assessment of the strengths and weaknesses of each tender; and
- A question and answer process to clarify ambiguities and address technical and financial questions raised by the evaluators, before they draw conclusions on the merits of each tender. Unless an agency's ICT requirements are very straightforward, agencies should expect that the question and answer process will take at least a week and possibly several weeks.

It is essential that the evaluation is carried out in accordance with the evaluation plan, and is consistent with the criteria published in the market approach documentation (for example, the RFT). Upon completion of the evaluation process, an evaluation report should be prepared which assesses each tender against the specific published criteria.

As stated in the *Commonwealth Procurement Guidelines*, no conflict of interest should exist in respect of anyone involved in evaluating tenders. In-scope staff should not be included in the evaluation team, or be in a position to influence selection recommendations.

Agencies should also perform an economic evaluation of each proposal, based on the model of real value discussed earlier. Depending on the flexibility of the process, and ensuring proper probity is maintained, agencies may want to reconsider ICT bundles based on this real value analysis – asking several vendors to build a bundled proposal may deliver a better overall outcome.

Conduct vendor due diligence

Once an initial evaluation is complete, it may be appropriate to shortlist one or more finalists to conduct vendor due diligence and engage in a process of parallel negotiations.

When performing due diligence on short-listed vendors, agencies should focus on three key areas (Exhibit 19). The 'financial and business' analysis concerns the financial strength and stability of the vendor, its risk management and accounting practices, and the financial details of the proposal. It is equally important that agencies understand each vendor's technology capabilities, and that they survey the vendor's customers to understand, among other things, the vendor's ability to meet SLAs.

EXHIBIT 19

Financial and Business	Technology and Operations	Customer Interviews
Financial strength and stability • Already part of the endorsed supplier arrangements Risk management • Evaluation of internal controls • Review of business continuity plan • Analysis of third party and other exposure • Review of client prioritisation strategy Accounting policies and practices Financial proposal • Asset proposal and treatment • Human resource proposal and cost	General capability overview • Systems Management • Computer Operations • Help Desk • Desktop Services • LAN/Network • Voice/PBX • security Project capability overview • Capacity expansion/allocation requirements (present and future) • Proposed expansion actions by platform • Detailed review of transition planning (Infrastructure, Human resources)	Commercial management • Overall vendor review • Achievement of related IT goals • Contract negotiation • Transition planning and effectiveness • Pricing transparency Service management • Efficiency of knowledge/skills/ personnel transfer • Reporting timeliness and efficiency • Frequency of employee turnover • Existence and frequency of non-compliance rebates Service delivery • Overall ability to meet SLAs • Results of customer satisfaction surveys • SLA achievement during transition

Negotiate with finalists

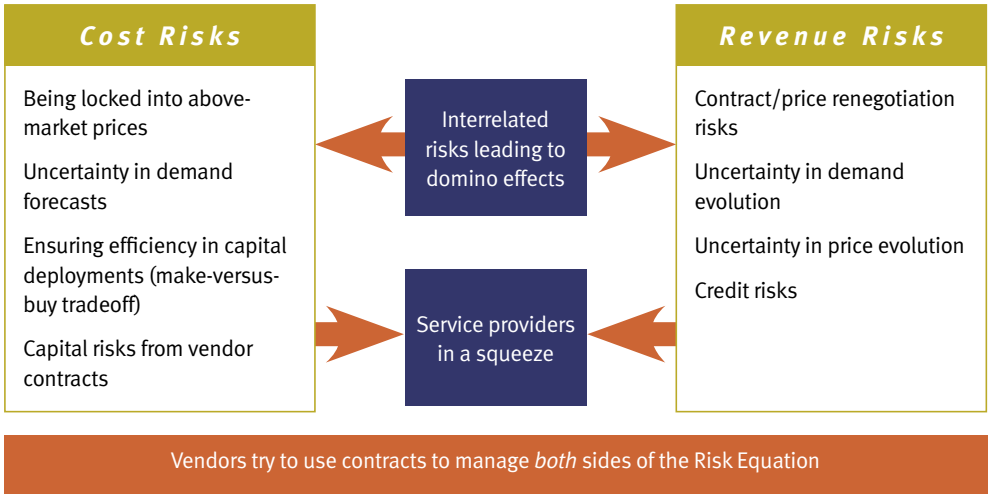
The goal of the negotiations with finalists is to resolve all major financial, technical and legal issues before selecting the successful tender. If an agency elects to engage in parallel negotiations, they may wish to use a 'term sheet' containing the following elements to guide the process:

- The agency's position or statement of each material issue (with RFT item reference or other source citation if appropriate);
- The tenderer's proposal or response, in summary form (with RFT item reference or other source citation); and
- A comments block, which includes the status of each issue (e.g. 'open', 'resolved' or 'vendor to clarify position by [date]').

Basic rules of negotiations suggest that agencies will need to go to the negotiation table with an in-depth knowledge of their target outcomes and their walk-away limits based on the next best alternative solution if negotiations are not successful.

In addition, before negotiations begin, agencies should understand the cost and revenue risks that vendors are trying to manage through the contracting process (Exhibit 20).

EXHIBIT 20



It is also important to carefully assess all conditions when agency bargaining power is greatest. In particular, agencies should assess issues that may lead to high termination costs (described below).

Develop contract

The focus of the third module of Phase III is to write a contract that captures the benefits that were forecast during the sourcing strategy phase and ensures the vendor will be in a position to deliver without being put at risk. There are also certain issues that should be addressed in all Australian Government contracts. Agencies should consult the CPGs and their agency CEIs before drafting any contract, and seek legal advice as appropriate.

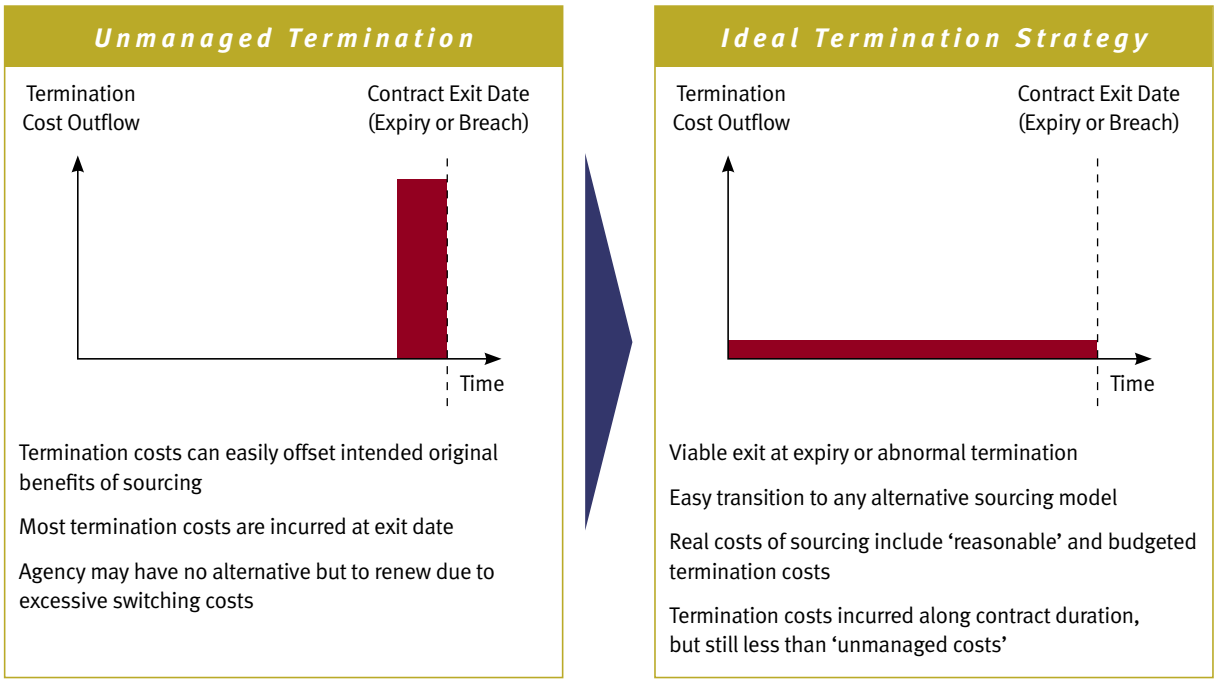
Refine the termination strategy

When developing a contract, agencies should refine their termination strategy to reduce the risk of incurring excessive costs at the end of a contract. Agencies that overlook the significance of termination costs can find themselves faced with no real alternative to renewing with their current vendor, because the costs of switching – materialising as one large cost at the end of the contract – may be too high.

A conservative estimate is that termination costs can easily reach between 15% and 60% of the annual invoice price. As mentioned earlier, this is generally due to unexpected issues with intellectual property rights, residual value of equipment, transfer of assets or remaining lease payments, assistance from the incumbent vendor to transition to a third party, and any potential damage costs. These costs need to be identified at the outset of a contract.

A good termination strategy will spread these costs across the duration of a contract while also reducing their total impact (Exhibit 21). In other words, an agency that manages these costs should end up on the right-hand side of Exhibit 21, with 'no surprises' at the end of the arrangement. An agency that neglects to plan for this could end up on the left-hand side, facing prohibitively high termination costs.

EXHIBIT 21



Write contract

When writing the contract, agencies should bear in mind that both sides ultimately need to benefit from the arrangement. There is no point writing a contract that puts a vendor in an unsustainable position, as it will eventually be reflected in the level of service that the vendor gives, and will be reflected in the agency's performance.

As well as incorporating arrangements for contract governance, agencies should make sure they address three specific contract elements:

- *The transition of in-scope operations to the successful tenderer:* The market approach should require each tenderer to submit a transition plan as part of their proposal. The successful tenderer's transition plan, when agreed, then becomes part of the services agreement. The successful tenderer needs to conduct a final asset inventory at this time.
- *Options to manage volatility in risks and business demand:* Agencies need to be aware that vendors use a number of tools to manage risks and to move contracts more in their favour. These tools are similar to financial instruments used by fund managers when hedging their risks (Exhibit 22). For example, if a vendor believes there is a risk that agency volumes covered by the contract may exceed base platform capacity, they may want to negotiate for a volume cap to be included in the contract. Such a cap could trigger a renegotiation if volumes surpass a certain threshold. This clause passes the risk of excess volume from the vendor to the agency. An agency that is counting on a fixed price contract may be exposing itself to unacceptable levels of risk by agreeing to such a condition.

However, agencies can also benefit from using these tools. For example, Exhibit 23 provides a comparison of two contract clauses covering requirements of mainframe processing power. With a fixed volume clause, the agency faces the risk of paying for the cost of peak demand. If a clause exists that gives the agency the option to exercise incremental volume, it will only pay for what it uses.

- *Incentives and penalties:* Often penalties are used to make sure the vendor has an abiding interest in fulfilling the agency's needs and respecting the contract. However, it is relatively easy for the vendor to recoup penalties from different projects, and in the end, penalties are effectively 'free' for the vendor.

Incentives offer a more sophisticated way of aligning interests, but must be carefully considered. In one instance, it proved useful for a government agency to change the incentives for the vendor's project manager to also include a quantified level of customer satisfaction. The change was significant: the number of customer 'issues' dropped from 40 per month to just 1.

It is difficult to describe precisely how to define the right incentive scheme for every single agency, but the main principle is clear: all stakeholders should be motivated for the benefit of the relationship. A typical incentive system includes a set of measures (profit, customer satisfaction, success rates, cost savings, etc) and a set of financial compensation rules (bonus, shared gains or shared savings, reduced prices, etc) for the different stakeholders (the agency side, the vendor side, key individuals, groups, companies, etc). Agencies have to find the mix of these components that will work best for them and their vendors.

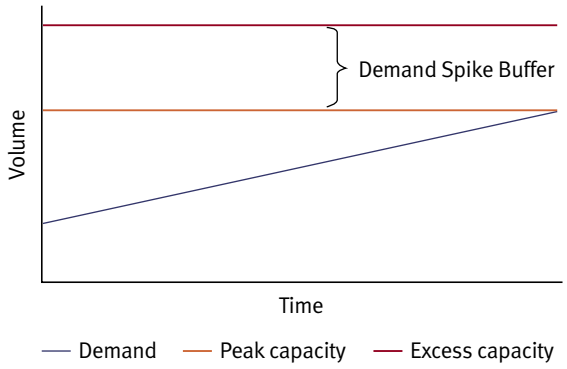
Agencies that have chosen an external sourcing strategy conclude this module, and this phase, with a signed contract.

EXHIBIT 22

Vendor Risk	Contract Hedge	Example	Agency Risk
Agency metric volumes exceed base platform capacity/alter platform economics	Volume Cap	Forced renegotiation if metric volumes surpass maximum contract allowance	Price risk: Changes in business needs cause metrics to exceed cap, destroying fixed price contract
Agency metric volumes fail to cover base platform expense	Volume Floor	Forced renegotiation if metric volumes fail to reach minimum contract allowance	Price risk: Changes in business needs cause metrics to fail to meet volume floor, destroying fixed price contract
Aging technologies fail to perform efficiently	Technology Put Option	Vendor guaranteed right to sell upgraded hardware/ software to agency within prescribed windows	Price risk: Vendor elects to execute hardware upgrade right before agency would otherwise pay to refresh
Insufficient scope to provide sufficient return on fixed price contract	Scope Call Option	Vendor granted scope expansion rights (geographic or platform based) at prescribed performance targets	Business risk: Vendor elects to exercise right to expand scope under sub-optimal business conditions

EXHIBIT 23

Current condition: agency buys fixed volume of mainframe capacity equal to peak deman

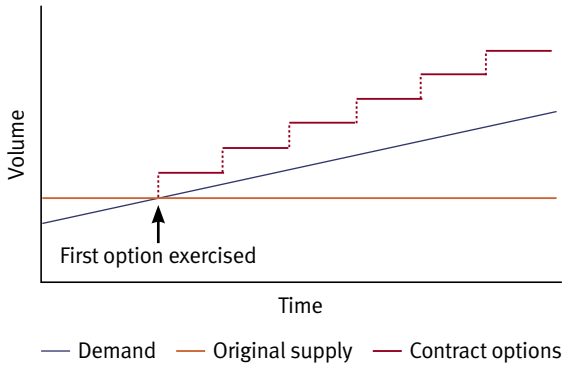


Agency commits to fixed amount of capacity or IT product volume over a certain time period

Seasonal variation in business requires small amount of capacity in Q1 and high volume of capacity in Q4

Large volume of capacity unused during year

Solution: embed call options in contract stipulating right to buy units of incremental volume



Agency increases volume as necessary

- Incremental volume and timing of increase agreed upon at outset of contract
- No purchase obligation if demand does not increase
- Original, underlying contract stands regardless of decision to increase volume

Phase IV: Transition and manage

The purpose of this phase is to transition to, and set up the management of, the new sourcing strategy. While this is relevant to agencies that are changing to a self-managed or external strategy, the vendor management elements in this phase are only relevant to external vendor strategies.

The first step is to set up contract governance. After this, agencies can begin the transition. This is never as simple as turning off the old solution and initiating the new one. The transfer of knowledge, assets and staff, and the migration of work-in-progress could take from three to ten months. One of the key objectives for the agency will be to make this transition as transparent as possible to the business.

Agencies then need to focus on managing ICT, which entails managing the relationship, managing the contract, and managing ICT operations. Finally, agencies need to establish processes to periodically review performance.

As mentioned earlier, there is an assumption that agencies already have knowledge across many of these elements, as well as access to existing Australian Government publications that provide guidance on these issues. As a result, the phase is less detailed than the others.

Set up contract governance

All agencies that manage a vendor need to set up contract governance for their arrangements. This should be encapsulated within the agency's overall ICT governance and have been outlined in the tender documents and specified in the contract, as it affects the overall pricing.

Defining the contract governance structure consists of identifying the ICT roles and responsibilities, the management organisation, the decision making process, a process for escalating disputes, and the rules and incentives for all parties involved with the arrangement, including:

- The agency's top management and the ICT managers
- The incumbent and newly contracted vendors
- Other agencies, in cases of alliances between agencies.

The agency needs to establish three important management roles, each of which is described in more detail in a later module:

- *Managing relationships between all parties in the contract:* This involves building trust and working for win-win outcomes. This role is usually the responsibility of senior people within each organisation.
- *Managing the contract:* The objective of this role is to make sure the services are delivered according to the contract, that the terms and conditions are followed, and that legal requirements are maintained at all times.
- *Managing ICT operations:* This role should be managed by the ICT manager and covers all day-to-day service delivery.

Agencies should establish a team to oversee these roles. Large and complex sourcing arrangements may warrant a dedicated program office.

The team/program office should have overall accountability for the success of sourcing, including budget responsibility. It should report directly to senior management and provide easily understood, reliable, and robust information for decision-making. This will enable senior management to take ownership of the overall ICT sourcing strategy, ensuring sourcing gets the attention it deserves and that issues raised are quickly resolved.

Transition

This transition step is a one-time effort that occurs each time a new element of the sourcing strategy is put in place. When this module is done, agencies should be ready to make the cut-over to the new arrangement.

The transition needs to be managed as a project. It should have clearly articulated milestones, deliverables, and roles and responsibilities, together with a management and communication process. Suggested milestones include:

- Team established and 'ready, willing and able'
- Detailed migration plan agreed, possibly including ICT re-engineering
- New equipment ordered, if required
- People resources sourced, if required
- All resources (equipment, software and staff) transferred and operational
- Modifications frozen, except for critical changes (bug fixes, etc)
- Work in progress transferred
- New environment tested
- Official cut-over
- Integration validated (after the cut-over, agencies may require assistance from the incumbent).

Three of these milestones deserve particular attention:

- *Defining the best timing for official cut-over:* It is critical to choose this date carefully. Ideally, it should take place during a period of low business activity of the vital business functions, usually during the last three months of the incumbent contract.
- *The transfer of knowledge from incumbent vendor:* It is critical that incumbent vendors transfer their knowledge to the new vendors and (potentially) to the agency. However, their incentives are not usually aligned with this task. They may need to write or at least gather a large amount of documentation such as reports, billing information, procedures manuals, source and object codes, job listings, work volumes, etc. Given the amount of

work required and the importance to the overall outcome, agencies must ensure they closely control this process. Agencies should start assembling this knowledge well before the end of the contract.

- *The lead-time to source the project and get the final IT staff:* Internal skills must be resourced. They will either be taken from other functions or external sources. Agencies should plan ahead where recruitment is going to be necessary.

The most important factors to understand before a transition are business risks, especially when the transition involves moving away from an incumbent vendor, which often takes more than six months from hand-over to take-over. This represents one of the biggest changes the agency will face, and it must be done carefully. This change should be transparent to the business, and there should be no business deterioration during the transition.

Any agency facing such a change should minimise business risks and define this as a first priority. In some instances, it could be so important that an agency is willing to opt for a less appealing alternative in the long term if it provides a safer transition.

At the end of the module, agencies should be in a position to cut-over to the new sourcing arrangement.

Manage relationship

This guide does not address this topic, as it has a strong link to the individual culture and management style of each agency.

It is worth noting, however, that managing the relationship is a key element of the sourcing lifecycle and requires careful attention by agencies and vendors. All agencies, whether coming from a transition exercise or not, should make sure they maximise control over their current relationships.

It is important to distinguish the relationship from the contract. Managing the relationship is all about maximising the overall business outcomes of the arrangements. Keeping the relationship separate from the contract will ensure agencies maintain a business perspective over all arrangements, and will help mitigate the legal difficulties that usually occur during the life of the contract.

Agencies can refer to the Source IT website for up-to-date guidance for these activities.

Manage contract

This guide does not address this topic; it is a very specific area that requires legal expertise. However, it is important to provide some business context.

From a business perspective, agencies should recognise that the aim of managing the contract is to:

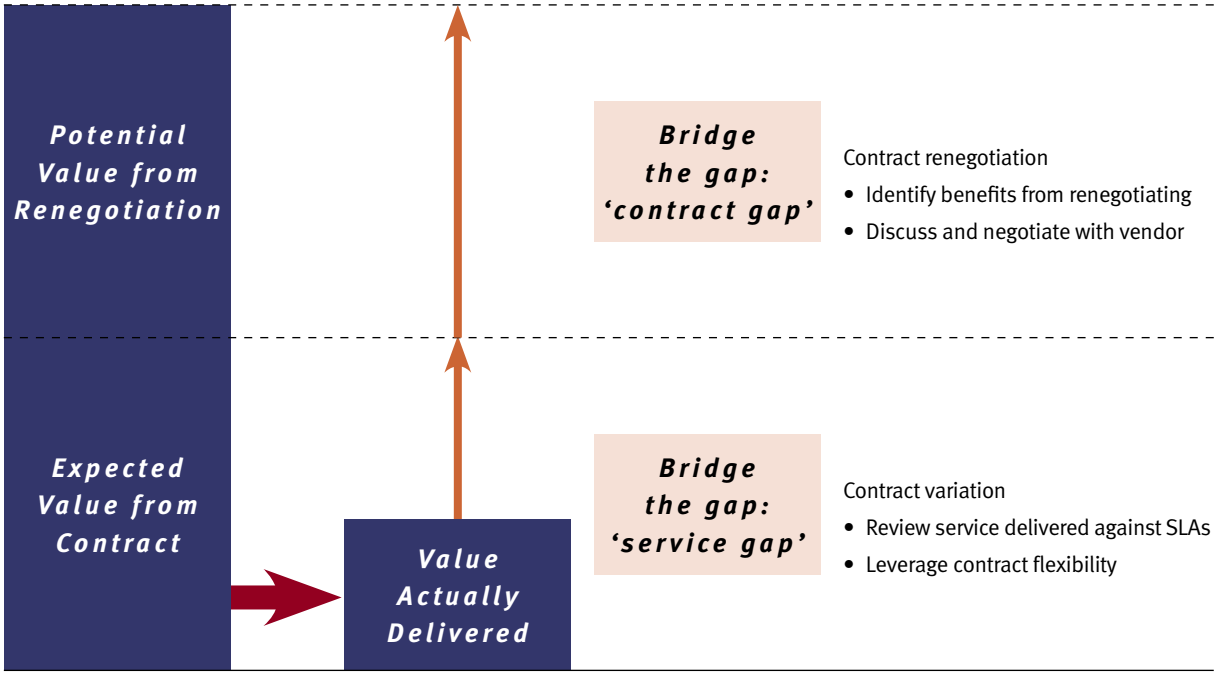
- Ensure all parties included in the contract perform to minimum requirement levels
- Ensure the contract continuously reflects the best possible outcome for the agency.

A service gap exists if all parties are not performing according their minimum requirement levels. If this is the case, steps should be taken to close the gap by reviewing existing service levels against the Service Level Agreements (SLAs), or by using the flexibility built into the contract to make a variation.

A contract gap exists if the contract does not reflect the best possible expected outcome for the agency. In order to close this gap, agencies need to consider whether to renegotiate the contract in order to establish updated arrangements, recognising that opportunities and constraints may have occurred since the previous contract was signed. However, signalling a renegotiation is a serious step, and agencies need to clearly establish the benefits and risks of doing so.

Exhibit 24 shows both the service gap and the contract gap.

EXHIBIT 24



Manage operations

As with the previous two modules, the guide does not focus on this area. But, again, it is worth mentioning some observations.

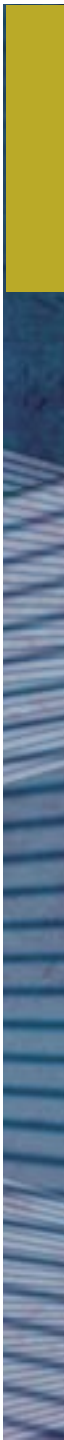
Managing ICT operations is the day-to-day role of the agency, which must ensure that the ICT services support the agency's business requirements. The team accountable for this role should be knowledgeable about relationship and contract management. However, keeping these roles – contract, relationship and operations management – separate allows each team to focus on the highest quality service delivery.

Experience shows that contracts are most successful when there is close integration between vendor and agency, regardless of whether the vendor is providing commodity processing or highly specialised services. Among other things, this will help ensure a certain degree of flexibility for adjusting the level of ICT service if and when agency requirements change. For further information on this topic, please refer to the Source IT website.

Review periodically

The most carefully considered ICT sourcing arrangements could fall short of delivering expected benefits. Moreover, even arrangements that are performing to plan need to be reassessed from time to time to determine whether more value can be delivered.

It is important to set up ongoing reporting processes for measuring the performance of a sourcing arrangement. Agencies should establish scorecards to track performance against plan and to track current market circumstances. It is also important to track any changes made to the contract itself. Tools and templates for ongoing tracking and reporting are provided on the Source IT website.



Conclusion

Agencies should approach ICT sourcing with an understanding of the significant role it plays in fulfilling key business priorities. An agency's top management must recognise that, at a minimum, an ICT sourcing strategy needs to support these priorities in the most cost-effective manner.

Agencies must also understand the risks and challenges of ICT sourcing – the experiences of many public and private sector organisations have proven that ICT sourcing is risky. Given this, how can an agency ensure that it selects the best ICT sourcing strategy and executes it well? How can it be certain that it has done all the right analysis and asked all the right questions about ICT sourcing? How can it get the best Value for Money from these arrangements?

This guide, with its four-phase lifecycle, should provide agencies with the strategic support they need to meet these challenges. It details a number of frameworks that should prompt agencies to ask the right questions and perform the right analysis. In particular, the economic diagnosis tool – the key to understanding the real value of existing and potential ICT sourcing arrangements – will help them assess the value created by an outsourcing arrangement.

In addition to using this guide, agencies should also turn to the Source IT website, other government publications on sourcing, and to each other to learn more about developing and executing effective sourcing strategies.

Appendix A: Economic diagnosis tool

To complement the guide, we have developed a tool that helps agencies understand the real value of an arrangement with an outsourcer. The logic of the tool is described below to show how it works and also to underscore the value of having this type of analytical approach.

The tool is described from the perspective of an agency whose current ICT sourcing strategy is external. This means that:

- Agencies that have an external sourcing strategy can apply the tool directly.
- Agencies that self-manage ICT can still apply the logic of the tool to understand their arrangement and how it compares to alternatives, but they may need to reverse the order of some steps in the model.

The economic diagnosis tool is an essential aid to Phase I of the sourcing lifecycle. The purpose of the tool is threefold. First, it will help agencies understand the real value of their current sourcing contract, including the discrete sources of value. Second, it will provide a reference point for assessing alternatives. Third, it will help define the expectations of the next sourcing strategy and focus it on the most relevant options.

The tool is structured around six important questions relating to the real value of a sourcing contract (Exhibit 25). The assessment uses a yearly snapshot of the economic costs for the past year.

EXHIBIT 25

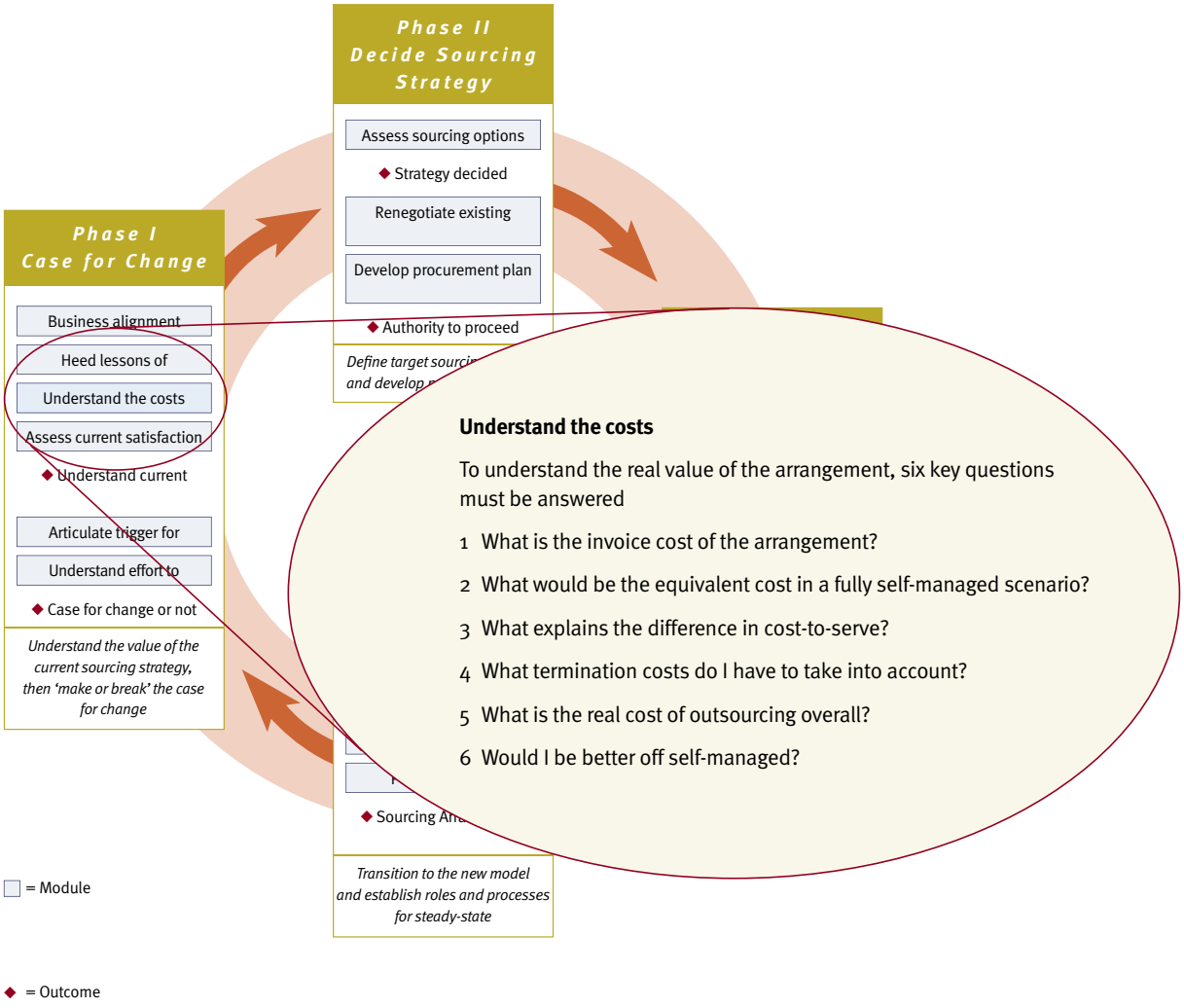
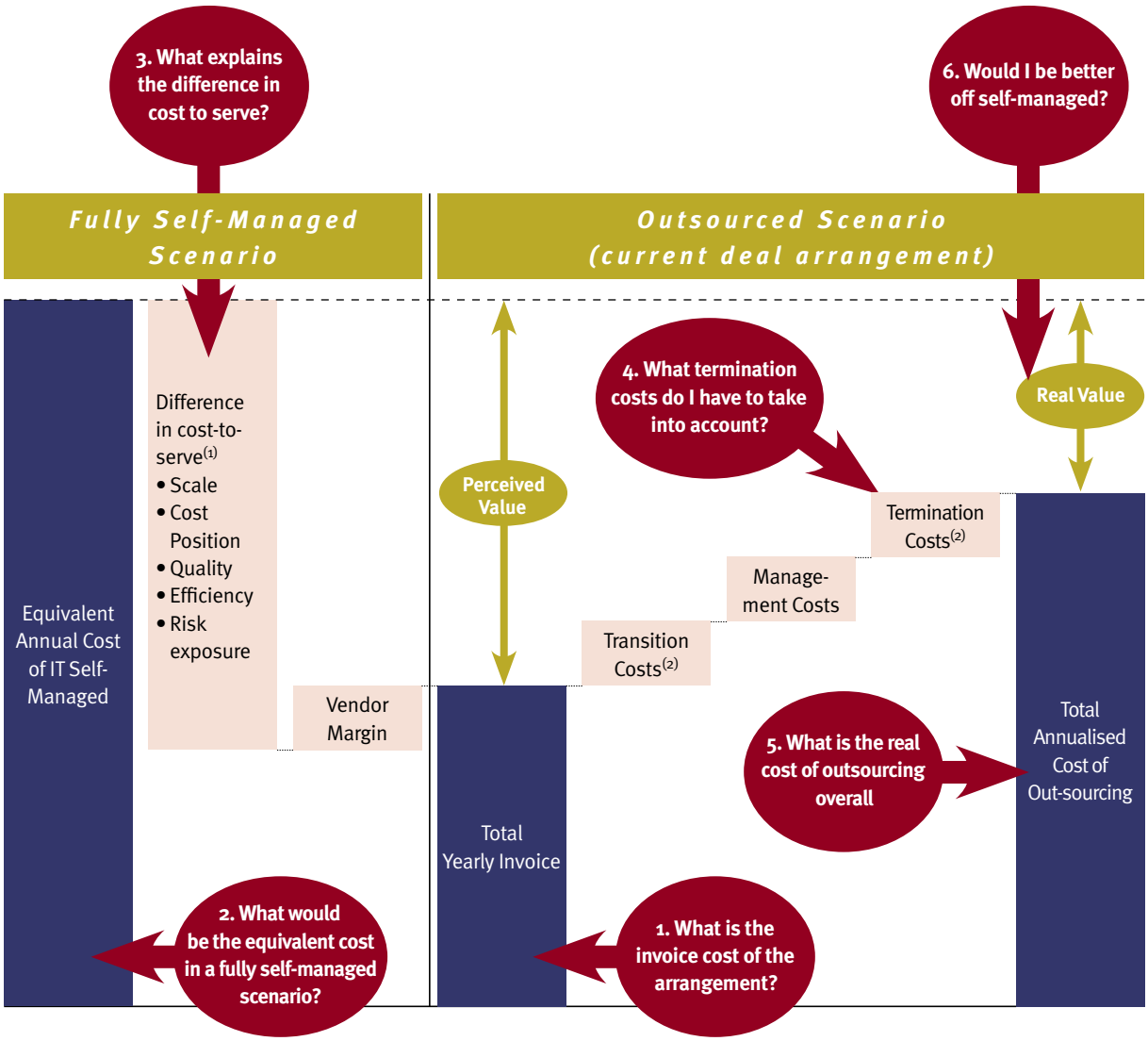

Phase II
Decide Sourcing Strategy
Assess sourcing options
Strategy decided
Renegotiate existing
Develop procurement plan
Authority to proceed
Define target sourci
and develop
Phase I
Case for Change
Business alignment
Heed lessons of
Understand the costs
Assess current satisfaction
Understand current
Articulate trigger for
Understand effort to
Case for change or not
Understand the value of the current sourcing strategy, then 'make or break' the case for change
Sourcing Ar
Transition to the new model and establish roles and processes for steady-state
Understand the costs
To understand the real value of the arrangement, six key questions must be answered
1 What is the invoice cost of the arrangement?
2 What would be the equivalent cost in a fully self-managed scenario?
3 What explains the difference in cost-to-serve?
4 What termination costs do I have to take into account?
5 What is the real cost of outsourcing overall?
6 Would I be better off self-managed?
= Module
= Outcome

EXHIBIT 26



(1) Cost-to-serve: total cost necessary to run and maintain the IT operations that serve business activities
(2) Distributed over the contract duration

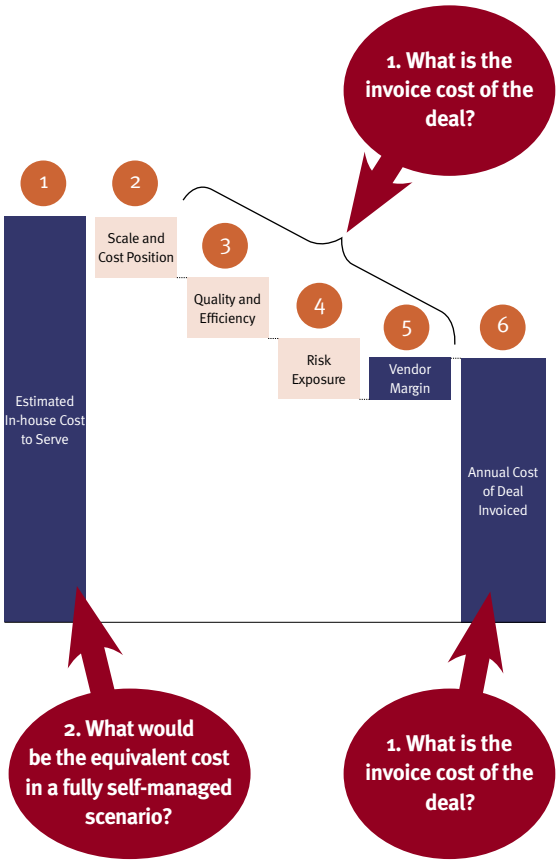
Exhibit 26 shows how these questions relate to the perceived value and real value calculations described earlier in this guide.

Question 1: What is the invoice cost of the deal?

The invoice price from the vendor will provide the basis for calculating the perceived value of an arrangement (Exhibit 27).

EXHIBIT 27

Framework



Main Cost Components

Question 1:

6. Annual Cost of Deal Invoiced
   - Invoice price from the vendor limited to the scope of the contract, including costs overrun

Question 2:

1. Estimated self-managed cost-to-serve
   - Result of Top-Down, Bottom-Up or mixed approach

Question 3:

5. Vendor Margin
   - Net profit margin before tax out of revenues, applied to the invoice price of the contract

2. Scale and Unit Cost position
   - Cost difference for the same volume in infrastructure and operations
     - mainframe processing power (MIPS) and storage (DASD, tapes)
     - midrange servers (number of servers)
     - distributed infrastructure (number of desktops and laptops) and printers
     - help desk (number of calls)
     - voice/video infrastructure (number of ports)
     - data infrastructure (number of ports)
     - data communication WAN (bandwidth in kbs/seconds)
     - voice/video communication (long distance, local) (number of seconds)
     - Internet communication
   - Cost difference for the same output in developments
     - labor
     - development platforms if not included above

3. Quality and Efficiency
   - Cost of difference in FTEs required to deliver same output
   - Cost of internal free-up resources
   - Cost to maintain same level of service or cost impact of a lower service level

4. Shared Risks
   - Additional self-manage costs to cover peak demand
   - Additional disaster recovery, security and confidentiality costs
     - includes compensatory costs or cost of additional damages
   - Cost to provide same geographical business coverage

Question 2: What would be the equivalent cost in a fully self-managed scenario?

There are three approaches that agencies can use to answer this question.

- *A top-down approach using benchmarks:* Consider a simple example of an agency whose primary ICT requirement is the operation of PCs. If the agency's overall ICT cost for self-managing PCs is $7000 per PC, and if benchmarks or best practices from other agencies indicate a comparative cost of $5000, then the agency could assume that these alternative scenarios offer a perceived value of 28% ($2000 of $7000).
- *A bottom-up approach that rebuilds the existing ICT infrastructure:* In this approach, agencies would rely on new market prices and current knowledge about practices and costs. Using the example above, the agency would disaggregate all the cost components involved in operating PCs, then seek current market prices on each component. Based on the potential cost of these components, the agency would build up an overall cost of operating PCs, multiply by the number of PCs, and compare this with the current cost. The difference represents a broad estimate of perceived value of an alternative.

For this approach, agencies should reference cost data. An example is shown in Table 6 on the following page.

- *A mixed approach that combines top-down and bottom-up analyses:* Here, agencies would go beyond the basic top-down approach, but not as far as a detailed bottom-up approach, by looking at the major elements of ICT and comparing them to benchmarks. Agencies would understand perceived value and how it relates to some of the main categories of ICT spending, but the analysis would not have the same level of granularity as a more time intensive bottom-up assessment.

Question 3: What explains the difference in cost-to-serve?

In short, the value of the arrangement comes from the difference in the cost to serve between the vendor's offer and the self-managed option. As discussed earlier, there are four major components that account for this difference – three types of benefit are partially offset by the vendor's margin to yield the perceived value of the deal.

Agencies need to disaggregate perceived value, regardless of how it was calculated, into its four drivers: scale and cost position; quality and efficiency; risk exposure; and vendor margin. The specific cost elements that typically make up these drivers are described in Exhibit 27, above. With this breakdown complete, agencies should have a clear view of the magnitude of perceived value, along with its key sources.

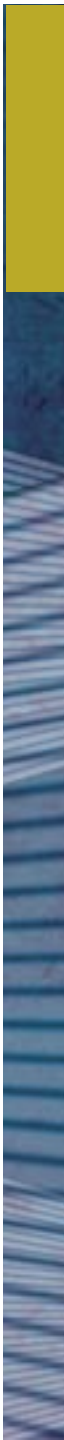


TABLE 6: EXAMPLE OF COST ASSESSMENT IN A BOTTOM-UP APPROACH

Prices Based on 3 year life cycle.		Quantity per year			Unit Price	Cost per year			Already owned or paid for directly by the Agency
Item Description		Yr 1	Yr 2	Yr 3		Year 1	Year 2	Year 3	
Capital expenditure									
Hardware									
PC's	Pentium 3-4 Class Machines	100			$1,200	$120,000	$0	$0	
Laptops		40			$4,500	$180,000	$0	$0	
Printers	Mono Laser Printer	10			$5,242	$52,420	$0	$0	
	Color Laser Printer	4			$3,100	$12,400	$0	$0	
etc									
Total Hardware						$364,820	$0	$0	
Software and Licences									
Desktop	Desktop Software	232			$300	$69,600	$0	$0	
etc									
Total Software and licences						$69,600	$0	$0	
Total Capital Expenditure						$434,420	$0	$0	$0
Recurrent Expenditure									
Support									
EL2		1	1	1	$180,000	$180,000	$180,000	$180,000	$180,000
SysAdmin		4	4	4	$160,000	$640,000	$640,000	$640,000	$80,000
Support		4	4	4	$120,000	$480,000	$480,000	$480,000	
						$1,300,000	$1,300,000	$1,300,000	
Communications									
Internet environment	ICON Data subscriber fee	1	1	1	$10,000	$10,000	$10,000	$10,000	$10,000
etc									
						$10,000	$10,000	$10,000	
Consumables									
Toner	colour	14	14	14	$1,200	$16,800	$16,800	$16,800	$1,200
	black	80	80	80	$150	$12,000	$12,000	$12,000	$150
						$28,800	$28,800	$28,800	
Total Recurrent Expenditure						$1,338,800	$1,338,800	$1,338,800	$271,350
Grand Total						$1,773,220	$1,338,800	$1,338,800	

Cost per year		Year 1	Year 2	Year 3
Capital Expenditure	Hardware	$364,820	$0	$0
	Software and Licences	$69,600	$0	$0
Total Capital Expenditure		$434,420	$0	$0
Recurrent Expenditure	Support (Employee expenses)	$1,300,000	$1,300,000	$1,300,000
	Communications (ICON & WAN)	$10,000	$10,000	$10,000
	Consumables	$28,800	$28,800	$28,800
Total Recurrent Expenditure		$1,338,800	$1,338,800	$1,338,800
Total Expenditure		$1,773,220	$1,338,800	$1,338,800
Less equipment or services already owned or paid for directly by the Agency				
Capital Expenditure	Total Capital Expenditure	$434,420	$0	$0
	Less previous Capital Expenditure	$0	$0	$0
New Capital Expenditure		$434,420	$0	$0
Recurrent Expenditure	Total Recurrent Expenditure	$1,338,800	$1,338,800	$1,338,800
	Less existing Recurrent Expenditure	$271,350	$271,350	$271,350
New Recurrent Expenditure		$1,067,450	$1,067,450	$1,067,450
New Total Expenditure		$1,501,870	$1,067,450	$1,067,450

Question 4: What termination costs would be incurred at the end of the arrangement?

Termination costs represent the cash outlay that would be incurred before moving to another sourcing option; they do not include the costs that would be required to transition to the alternative.

A conservative estimate is that termination costs are typically between 15% and 60% of the annual invoice price. This is generally due to unexpected issues with intellectual property rights, residual value of equipment, transfer of assets or remaining lease payments, assistance from the incumbent vendor to transition to a third party, and any potential damage costs. The top figures of the range generally occur during a difficult transition to the next sourcing arrangement, early termination (before end of contract), or when equipment has recently been refreshed.

If termination costs have been managed during the contract, there should be no surprises in the lead up to renewal. For instance, if an agency is relying on the vendor to develop and customise a specific application that runs the vital functions of the business, termination costs – if left unmanaged – could be significant. A termination strategy should ensure that the vendor's control over this application progressively diminishes long before the end of the contract.

Question 5: What is the real cost of outsourcing?

This calculation describes the difference between the face price (and perceived value) and the real cost (and thus the real value). It should capture all the costs that would not be incurred if there were no contract; for example, the cost of ongoing contract management, and the expected termination costs spread across the duration of the contract. The components of this analysis are shown in Exhibit 28.

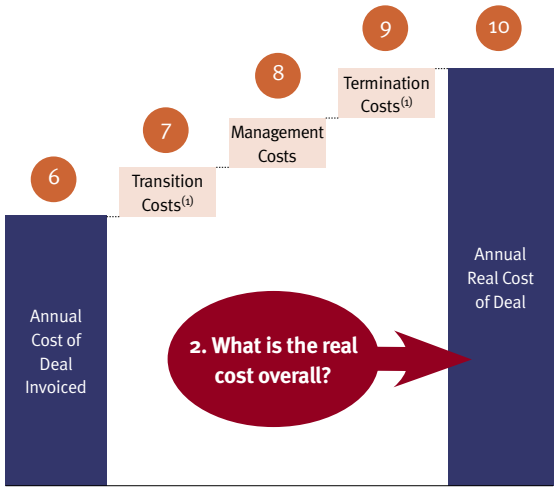
The calculation is made on an annual basis using the current-year information. It assumes that the current year is representative of the average year for the contract.

The sources of information are the historical data for the transition costs, the current accounting information for the management costs, and an estimate, based on the contract, for the termination costs. Agencies can use the checklist provided by the exhibit to look for the information.

When detailed historical information for transition costs is not available, which often happens, an estimate has to be made.

EXHIBIT 28

Framework



Main Cost Components

6. Annual Cost of Deal Invoiced
   - Invoice price from the vendor limited to the scope of the contract, including costs overrun

7. Transition Costs (added and divided by contract duration)
   - Internal project cost and transitions expenses (includes lease/maintenance payments on hardware and software awaiting transition)
   - One time costs from vendor (usually includes Initial hardware/software refresh, hardware re-location, transition labor)
   - Staff severance costs (salary, retention and severance packages for retained and released employees)
   - Losses for business outages and for drop in service level and other compensatory costs

8. Management Costs
   - FTE costs for governance and monitoring dedicated to contract
   - Losses and compensatory costs due to unmet SLAs
   - Additional costs to retain internal IT staff

9. Terminations Costs (added and divided by contract duration)
   - Cost to recover work in progress (internal knowledge management systems, intellectual property on code, data and documentation, vendor due diligence cost)
   - Cost to recover asset ownership
   - Cost of acquiring support to transition out of vendor (varies depending whether it is contractual or not)
   - Cost to prepare internal staff and new IT staff, whether self-manage or within new vendor (setup, training, etc)
   - Increased workload and drop in IT process efficiencies between notice served to vendor and end of contract
   - Termination fees, if any
   - Damage cost, if any

10. Annual real cost of deal = sum of items (6) to (9)

(1) Distributed over the contract duration

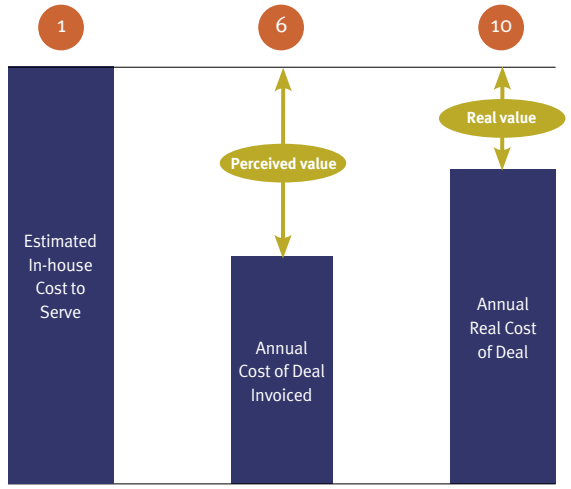
Question 6: Would I be better off self-managing?

If the self-managed estimate is close to the current real cost of the deal, then this option should be considered as an alternative (Exhibit 29).

At the end of the data gathering, when adding up all the elements, a sensitivity analysis is useful to stabilise the overall results. It allows agencies to identify the cost drivers that have the biggest impact on the total value and therefore refine them if the estimated range is too wide.

EXHIBIT 29

Framework



Logic

At this stage, the estimate excludes the transition costs to move towards a self-managed solution

This alternative should be considered if the estimated self-managed cost to serve is lower than the real cost of the arrangement

Main Cost Component

Annual real cost of the deal (10)
- From previous analysis

Estimated self-managed cost (1)
+ Invoice (6)
- margin
+ unit cost impact
+ efficiencies
+ risk
= Total

Real value of the deal over the self-managed alternative

Appendix B: Relevant legislation and policies

Financial Management and Accountability Act 1997 (FMA Act)

http://www.finance.gov.au/finframework/fma_legislation.html

The Financial Management and Accountability Act 1997 (FMA Act) and its associated Regulations provide the legislative framework governing financial management in all FMA agencies, including proposals for spending public money.

The framework comprises legislation, regulations, orders and guidelines which set out the financial management, accountability and audit obligations on agencies, including Departments, which form part of the Government sector. It covers:

- The efficient and effective management of public resources
- The maintenance of proper accounts and records of expenditure of Australian Government monies.

Under the FMA framework, an example of a Department (of State) is the Department of Communications, Information Technology and the Arts (DCITA), while an example of an agency is the Australian Customs Service. All FMA Act departments and agencies must have regard to the CPGs when carrying out activities relating to the procurement of property and services.

Commonwealth Procurement Guidelines (CPGs) and Best Practice Guidance

http://www.finance.gov.au/ctc/publications/purchasing/cpg/commonwealth_procurement_guide.html

The CPGs set out Value for Money as the core principle underpinning procurement under the FMA Act, and articulate the policy framework to which officials should have regard when performing duties in relation to procurement. Agencies may determine their own specific procurement practices within this framework of general principles and policies. Where an official takes an action that is inconsistent with the Guidelines, he or she is required to make a written record of their reasons for doing so.

Officials undertaking procurement-related activity are expected to:

- Act in accordance with the Guidelines;
- Ensure their procurement reflects the policies and principles contained in the Guidelines;
- Ensure their actions meet any additional requirements addressed in their CEIs; and
- Recognise that they are accountable, within the framework of Ministerial responsibility, to the Government, Parliament and the public.

The CPGs address issues such as:

- Value for Money;
- Efficient, Effective and Ethical use of Resources;
- Accountability and Transparency;
- Industry development; and
- Other policies that interact with procurement.

Agency Chief Executive's Instructions (CEIs)

An agency's CEIs provide an agency specific codification of the financial management framework, including provisions related to procurement. They are the primary source of information on operational guidance for agency officials conducting procurement.

Industry Development Requirements for Major ICT Purchases

http://www.finance.gov.au/ctc/cpc_02_2_id_requirements_for_m.html

As one of the primary objectives of the Australian Government's ICT outsourcing policy, there exist mandatory participation levels for small to medium enterprises in ICT contracts of expected value of $20 million or more. In summary, the minimum participation levels for each contract type are:

- hardware, for example, personal computers, network equipment, mainframes, and printers - minimum SME participation level of 10% of contract value; and
- services, for example, systems integration, software, software development/support, services provision, consultancies - minimum SME participation level of 20% of contract value.

Where a project contains elements falling under both of the above categories then the minimum SME requirement should be a weighted average of these minimum levels based on each category's share of the total contract value.

Best Practice Policy Guidance

http://www.finance.gov.au/ctc/toolkits/procurement_guidance.html

The Department of Finance and Administration issues guidance material in relation to various aspects of Australian Government procurement policy. Aspects of the policy covered include:

- Value for Money
- Industry Development
- The Role of Chief Executive's Instructions (CEIs) in Procurement
- Limitation of Liability and Risk Management

- Information Technology Outsourcing
- Confidentiality of Contractors' Commercial Information

Endorsed Supplier Arrangement (ESA)

http://www.esa.finance.gov.au/

This process provides pre-qualification for businesses selling ICT goods and services to the Australian Government. It is mandatory for use by all FMA Act agencies for all ICT goods and services to which the arrangement applies. The obligation to abide by the requirements of the ESA also extends to outsourced service providers in their engagement of sub-contractors.

Management of Security Accountability

http://www.ag.gov.au/www/protectivesecurityHome.nsf/

http://www.dsd.gov.au/library/acsi33/acsi33.html

The management of security accountability is a key consideration in the lifecycle of ICT sourcing. Paragraph A2.8 of the Commonwealth Protective Security Manual (PSM), states in part, that 'when outsourcing a function, agencies remain accountable for the efficient and secure performance of that function'. Part F provides further policy and guidance on the security framework for competitive tendering and contracting. In general terms, the outsourcer should be expected to meet the same security requirements for the protection of classified information and ICT systems as the Australian Government agency should the function remain in-house.

GITC - Government Information Technology and Communications contracting framework

http://www.gitc.finance.gov.au

This facility is a legal framework developed by the Australian Government in conjunction with industry representatives to provide standard terms and conditions for the purchase of ICT goods and services including major office machines and telecommunications. The GITC has been widely adopted by State Government agencies as well as the Australian Government, and although not mandatory its use is encouraged for appropriate purchases.

The GITC is a plain English approach to contracting, simplified processes and more equitable distribution of risk between parties. It provides a Head Agreement, terms and conditions, contract details and appendices. These modules allow government officers and vendors to 'build' a contract based on agreed terms and conditions. The framework is best suited to smaller and less complex procurements.

International Commitments – SAFTA and ANZGPA

http://www.finance.gov.au/ctc/pc_03_2_safta_and_the_anzgpa.html

The Singapore – Australia Free Trade Agreement and the Australia New Zealand Government Procurement Agreement impose the specific requirement on FMA Act agencies not to discriminate against suppliers from these countries, which is consistent with the non-discriminatory practices outlined in the CPGs.

Whole-of-Government Telecommunications Arrangements (WOGTA)

http://www.agimo.gov.au/infrastructure/telecommunications

The Whole-of-Government Telecommunications Arrangements (WOGTA) are a contracting framework managed by the Australian Government Information Management Office (AGIMO). Under WOGTA, carriers and carriage service providers licensed under the Telecommunications Act 1997 are required to sign a WOGTA Head Agreement.

Under this arrangement, the Australian Government is treated as a single customer and uses competitive processes wherever practical to seek access to new and innovative telecommunications services.

Volume Software Supply

http://www.agimo.gov.au/infrastructure/agreements

Contracts for Volume Software Supply (VSS) to the Australian Government have been established. The VSS arrangements are not mandated, and agencies are free to choose whether or not they use the VSS for purchase of products. However, where agencies access the contracts through the 'standing offer', provided by the VSS Head Agreements, access is through direct contact with the vendor.

Copies of the contracts with the current vendors are available, though it should be noted that the pricing schedules remain 'Commercial-in-Confidence' and should be obtained directly from the vendors.

Risk Management Standard AS/NZS 4360:1999

http://www.standards.com.au/catalogue/Script/Details.asp?DocN=stds000023835

According to Standards Australia, the risk management standard 'provides a generic guide for the establishment and implementation of the risk management process involving the identification, analysis, evaluation, treatment and ongoing monitoring of risks'. It also notes that this standard 'may be applied at all stages in the life of an activity, function, project or asset. The maximum benefit is usually obtained by applying the risk management process from the beginning'.

Appendix C: Market approaches

This section describes the various market approaches agencies can use to execute the procurement plan in Phase III of the sourcing lifecycle.

Request for Expression of Interest (REOI)

REOIs are generally used by an agency to set up panels of vendors to meet a specific need over a set timeframe. Sometimes it can be used to gauge the level of interest in the market regarding a particular ICT requirement. If the level of interest is low, the agency may determine that it is not worth trying to obtain the ICT goods and services using the tendering method, or at all. But as this process is fairly detailed, most agencies will expect an outcome from their efforts.

After setting out some background on the requirement and the broad evaluation criteria, the REOI will generally seek basic information from vendors, such as:

- Organisational details
- Product and service lines/personnel you will dedicate to the project
- Any conflicts of interest they may have (if relevant)
- Financial information/viability
- Relevant reference sites.

The REOI may include draft Terms and Conditions of the contract (or at least the conditions under which the agency will enter into a legal relationship with a vendor), which reflect the agency's preferred method of contracting.

Request for Information (RFI)

This method is used to obtain basic information about the types of vendors in the marketplace, and how many vendors may supply solutions in specific product/service areas. It may form the basis of an information database inside the agency, which allows the agency to 'map' the state of the market and the breadth and depth of the supply chain.

Request for Quotation (RFQ)

This method is similar to an RFI, with the additional requirement that vendors quote a price for the stipulated good or service. An agency will probably obtain quotes from several vendors and it will expect quotes to be vendors' best and final prices.

Agencies are not obliged to accept any quotes as a result of this process.

RFQs generally set out quote conditions such as evaluation criteria (the key one should be Value for Money), confidentiality requirements, ownership of quotes and the minimum time quotes must stay open (usually three months). Sometimes a draft contract is also included.

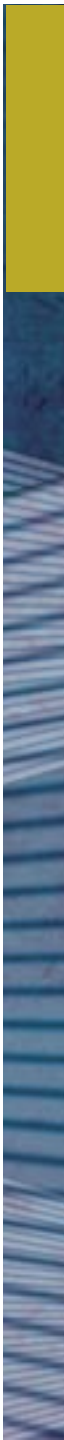
Request for Proposal (RFP)

This method is usually used where an agency seeks proposals from suitably qualified vendors with specialised skills such as the operation of community health facilities and similar activities. Generally, proposals may be linked to Government grants available to the eventual vendor to operate the required service. RFPs are not often used in the acquisition of ICT goods and services.

Request for Tender (RFT)

This method is the most common one used by the Australian Government to acquire ICT (and other) goods and services from vendors. RFTs can be used for small panels of vendors, consultancy or audit services, provision of basic ICT goods such as desktops or large requirements covering (perhaps) the entire range of an agency's ICT needs. The information provided above under REOIs is equally relevant to RFTs.

RFTs are rarely restricted to a select number of vendors because of the need to ensure effective competition and to obviate any chance of criticism of bias. Agencies must not include evaluation criteria in their RFTs that discriminate against SMEs.



Notes: