

Newcastle ITRS

CENTRE for PUBLIC SERVICES

Research • Strategy • Planning • Evaluation

Analysis of BT's proposals

June 2002

The following analysis is based on Part 2 of BT's proposal.

The in-house project must be completed as a matter of urgency and must produce a contestable proposal which will withstand full evaluation alongside the BT proposal. It must score well against all of the key aspects of BT's proposal ie the weaknesses identified in this briefing paper must be strengths in the in-house proposal.

BT's claimed competitive advantage

BT's advantage rests on two key issues:

1. Investment of £12m in years 1 – 4 ie upfront investment at a potentially faster rate than the in-house proposal may be able to offer. BT is potentially offering early access to capital. However, the investment profile shows that the bulk of the investment, £17.1m, will occur in years 5 – 8 and a further £12.9m in years 9 – 12.

- but this could be countered by the in-house proposal going for some quick wins in years 1 – 4 and making some similar savings which would be entirely ploughed into capital investment.

2. Change management capacity and a contract which is more enforceable than that offered by the in-house service.

- but much of the change management in BT's bid is not rocket science, it is just 'good management' practice and it remains to be seen whether it constitutes good public management.

BT is not offering anything different in ICT technology and its application than the in-house service because:

- the service Improvement Plans are very similar;
- BT will be offering off-the-shelf software packages and imposing a 'no customisation' policy to reduce ICT support costs.

Financial analysis

Savings in staff costs starting at 26 in October 2002 and rise to 177 from April 2005 will save approximately £45.7m (calculated from staff costs in Strategic Support Directive for 2000/01 which includes ICT and Finance staff of £23,600 uprated by 8% to cover

the two year period to 2002/03. This covers all employment costs to the city Council and is based on the number of jobs, not FTE). This saving could finance the entire capital investment budget over the contract period and still leave £3.6m savings.

Financial data in Part 2 of BT's proposal is very poor and inadequate. It does not provide a basis for evaluation. The in-house proposals must be more comprehensive, it must not allow the BT proposal to set the standard.

BT profit

BT profit is shown after taxation and is therefore much higher in terms of the pre-tax level which is the key indicator used in all financial market analysis. It will also be using the losses in the early years to reduce taxation later on or BT Group's overall taxation position. The city council should demand a pre-tax profit profile.

The overall profit of £10.4 on turnover of £251.3m is a low at 4.1% compared Hyder and Amey claims of 6% and 8% to 10% in bids submitted in other local authorities. However, these latter figures are misleading because they are based only on the *operating* expenditure and not capital expenditure where the return is normally 15%.

I consider that additional profit is built into BT's financial model which they have not disclosed – see section below on BT management, overheads and contingencies. Also the return on management consultancy is likely to be high on a contract where they are effectively acting as client and contractor with lower than normal external costs (ie they don't have procurement costs to obtain the work).

BT will also be making profiting from:

- Enhancing off-the-shelf software packages – this is not included in the financial model.
- Use of change management/Business Process reengineering and ICT consultants – their charge out rate of up to £1,600 per day. This is hidden in the financial model and must be transparent. Need to know the volume, type and scope of this work and the estimated annual cost.
- BT will want to widen the scope of services included in the JVC – all at extra cost. For example, they are likely to be keen to take over HR policy, property management and other services but they will all be at extra cost. BT clearly state that the vision model permits the JVC to extend the scope of services beyond the existing base services.
- All references to 'outside the scope' means that BT has not included the cost of that activity in the financial model. It is essential that these costs are identified before the evaluation process begins.
- The large reduction in ICT staff in years 0-4 (a period of substantial ICT change) will result in BT engaging more consultants. Full-time council staff will be redeployed to make room for the high costing consultants.
- The cost of redeployment and retraining has NOT been costed. This is a cost to the council which will reduce the level of BT's planned savings. HR could not supply us

with an average cost of redeployment and retraining because this is a Directorate responsibility and no information is available centrally.

- This is an entire council responsibility which will include:
 - Administrative costs of redeployment such as HR time in relocating staff, skill assessment, organising training placements and so on.
 - Retraining costs
 - Redundancy costs
 - VER costs
 - Salary costs of all staff redeployed by the JVC from the day they leave the JVC
 - until they have obtained another job or leave council employment.
 - (based on an HR administrative cost of £500 per worker, retraining costs for 140 staff of an average £2,000, 37 staff take redundancy/early retirement at an average additional cost of £7,500, and salary costs of 177 staff for an average of 2 months, the total cost will be a minimum of £1.4m. Council savings will thus be reduced by this amount).

In-house proposal will have a cost advantage over the BT proposal because the level of redeployment is likely to be lower and phased over a slightly longer period. This differential must be costed and taken into account in the evaluation process.

- HR system is another council responsibility – the cost of the software is assumed to have been taken into account but there may well be additional implementation costs which BT are stating are a sole council responsibility. Yet BT is claiming the savings from the reduction in posts.
- The cost model also states that any increase in seconded staff costs and any increase in other council retained costs are the sole responsibility of the city council.
- Any cancellation or transfer charges connected with existing contracts taken over by BT are also the responsibility of the city council.

High level of BT management, overheads and contingencies

The financial model shows that expenditure on BT management, overheads and contingencies is forecast to be £13.4m of which £6.4m (48%) will occur in years 1 – 4. A number of issues arise:

- a breakdown of these costs is essential:
- is it a coincidence that these costs are front loaded in the very years that BT's cumulative profit is negative.
- what is level of contingencies, what do they cover and who retains them if they are not spent ie is this not hidden BT profit.

Costs excluded from the BT proposal

Elected Members need to understand that many systems/ICT applications and costs are **excluded** from the BT Base Proposal:

e-procurement – potentially large savings which could be harnessed by the city council.

Customer Relationship Management (CRM) BT argue why they should be involved in this work but it is not part of the base package and has not been costed by BT. Hence all BT work on CRM will be at additional cost.

Customer Service Centres – council is proposing that they are financed by a joint PFI project with North Tyneside. This is another separate cost not included in the BT proposal.

Financial transparency

The lack of transparency is a major weakness of BT's proposals:

- more detailed financial analysis;
- lack of clarity about what is included/excluded within BT's proposal;
- the level of additional costs which will be imposed for functions and activities which are 'not in scope' and where there is a difference between the current level of service enjoyed by the council and that proposed by BT, for example, the supply of standardised software and the additional cost of enhancements;
- The financial impact of these additional costs on the savings model.

The fact that BT will generate savings on such a broadly structured financial model means that they are almost certain that they are deliverable. Furthermore, the savings are likely to be at the low end of their expectations in order to provide a 'cushion' if things do not go according to plan. BT carries the risk where numbers of staff available for redeployment is less than agreed ie fewer staff = higher cost for the JVC. But BT are "confident that the proposals do not represent significant risk", in other words the margins are strong, ie it is a poor deal for the council.

If the levels of redeployment are higher than those predicted by BT, the savings will be larger and shared between BT and the city council. However, for the city council, the higher the number of staff requiring redeployment, the higher the cost which will eat into the council's savings. For BT, every 25 staff represents a saving of about £640,000, which if shared equally, means that BT gains £320,000 additional profit and no other liability whereas the council must fund the additional cost of redeployment and retraining from its share.

Reduction in IT staff and use of consultants: the big reduction of IT staff (52 by October 2004) within years 0-4 will almost inevitably mean that BT will have to rely more heavily on consultants. Full-time council staff will be redeployed at a cost to the council whilst BT replaces them with consultants at daily rates of up to £1,600. This is another hidden way in which BT will gain financially.

HR system: The council has responsibility for the cost of software but other costs have not been taken into account.

Cost benefit analysis: BT propose that cost benefit analysis should be used in the investment appraisal, however, we strongly recommend that a fuller impact assessment is carried out which puts the costs and benefits in a wider framework of social and

economic issues. This would also assess the costs and benefits but in a wider framework of social and economic issues, equalities and the social value of ICT ie securing investment which also has a social and economic purpose and is not simply driven by BT and its suppliers or by a fetish for ICT.

Pension costs: All pension costs related to redundancy and VER must be transparent in the investment appraisal. Council staff do not want to discover in a few years time that pension costs have been concealed and later put in jeopardy the viability of the pension fund.

Risk analysis

Need to emphasize that the council is taking much of the risk.

- The council is committed to paying £21.8m per annum (less savings) for 11.5 years for the base package.
- The council bears the operational and financial responsibility for redeployment and retraining. There is a substantial risk for the city council and the costs could vary widely depending on the state of the economy and the labour market, future financial annual settlements for local authorities, and opportunities in the rest of the city council (which are also subject to increasing outsourcing and partnership liabilities).

Service Improvement Plans

Significant issues:

- similarity with in-house Service Improvement Plans
- some service quality reductions ie cashiers
- limited detail provided

BT's 'High level'

BT makes several references to 'high level' in their bid. Everyone should be made aware that this is modernisation-speak for broad estimates or low quality analysis and date. It means the reverse of what it is trying to imply. In other words, they have missed out or never reached more detailed levels of analysis.

It would appear that BT has made a conscious decision to limit it's bid investment in Newcastle because of the existence of the in-house bid which reduces their chances of winning the contract. They gained the Liverpool, Edinburgh and Essex contracts and are preferred bidder in Barnsley, Rotherham and Walsall with no internal competition.

Regional Business Centre

It is significant that the 'growth' element of the project is on the last page. Either they have not got much idea about how growth will be achieved since no forecasts are supplied, unlike other strategic partnership bids which are bullish on 'job growth' claims, or they have taken the decision or been advised to accordingly to keep this aspect of their proposal 'low key'. As it stands, this section is very weak, concentrating on the location of a new building. They refer to a business case being forthcoming in June – but does this refer to the building or to a growth strategy and forecasts?

If additional information is supplied on a 'growth strategy' this must be subjected to rigorous analysis since the 'business centre' model in strategic partnership has been consistently exaggerated to attract Elected Member support but has failed so far in practice.

Service Directorate Partnership

This is the Barnsley model which BT has suddenly introduced in the Newcastle project. I strongly recommend that this proposal is ignored and focus placed on the JVC model.

BT change management

The section on change management describes a standard approach to change management and Business Process Reengineering (BPR) methodology. There is indication that they offer anything distinctive should the city council could not apply itself or with the support of its own external advice. The section describes the approach to change management, the capabilities required, the different stages involved and the benefits which may be obtained but there is little detail on actual methodology both for BT commercial reasons and because there is much less 'science' involved. No indication of who consultants will be

In-house proposal

The ability to fund some initial capital investment and to use savings to finance investment in the early years of the project must be a key part of the in-house bid.

Selective use of external ICT, BPR and change management expertise as and when required under direct council control and using best practice procurement process. Some managers will be leaving as part of the normal turnover of staff and other will be leaving through retirement. This will create an opportunity to reskill and increase capacity of the city council.

UNISON commitments

The issue of Elected Member's and senior management's uncertainty over UNISON's and staff commitment to achieving radical ICT change could be resolved by developing a set of commitments (which could be combined into a charter of some sort). This would not be signing an agreement or entering into a labour/management partnership but setting out the terms of cooperation, negotiation and involvement in the change management process. UNISON should consider making a commitment to:

1. The application of ICT for service improvement, community benefit and reducing social exclusion.
 - UNISON's understanding of the change management process
 - Public service principles and values ie the context in which change management will be applied.
 - Redeployment and retraining programme
 - Participation in the change management process – how UNISON wants to be involved.
 - How staff and trade union ideas and proposals should be evaluated.
 - The type of impact assessment required as part of investment appraisal.