



Survey on Outsourcing of Government Activities in 2004

Efficiency Unit

The third biennial survey on government outsourcing activities

- ◆ This is the third biennial survey on outsourcing conducted by the Efficiency Unit (EU) since 2000. It provides a “snapshot” of the government’s outsourcing activities as at August 2004.
- ◆ The survey aims at updating EU’s database on government outsourcing as well as obtaining a better understanding of the outsourcing practices and concerns of departments⁽¹⁾.
- ◆ Information on the outsourcing activities of all departments, with reference date as at 1.8.2004, was collected by means of questionnaires.
- ◆ For the purpose of the survey, an outsourcing activity was defined as a contractual arrangement whereby a department pays a service provider to deliver specified service outputs with a contractual value exceeding \$150,000. Contracts for procurement of goods, leasing or rental of accommodation, or employment of individual staff were excluded in the survey.
- ◆ 77 departments were invited to provide information. Six departments⁽²⁾ reported no current outsourcing activities.
- ◆ Supplementary views on government outsourcing were also collected from selected departments.

(1) This term also covers bureaux, departments, agencies, etc throughout the report

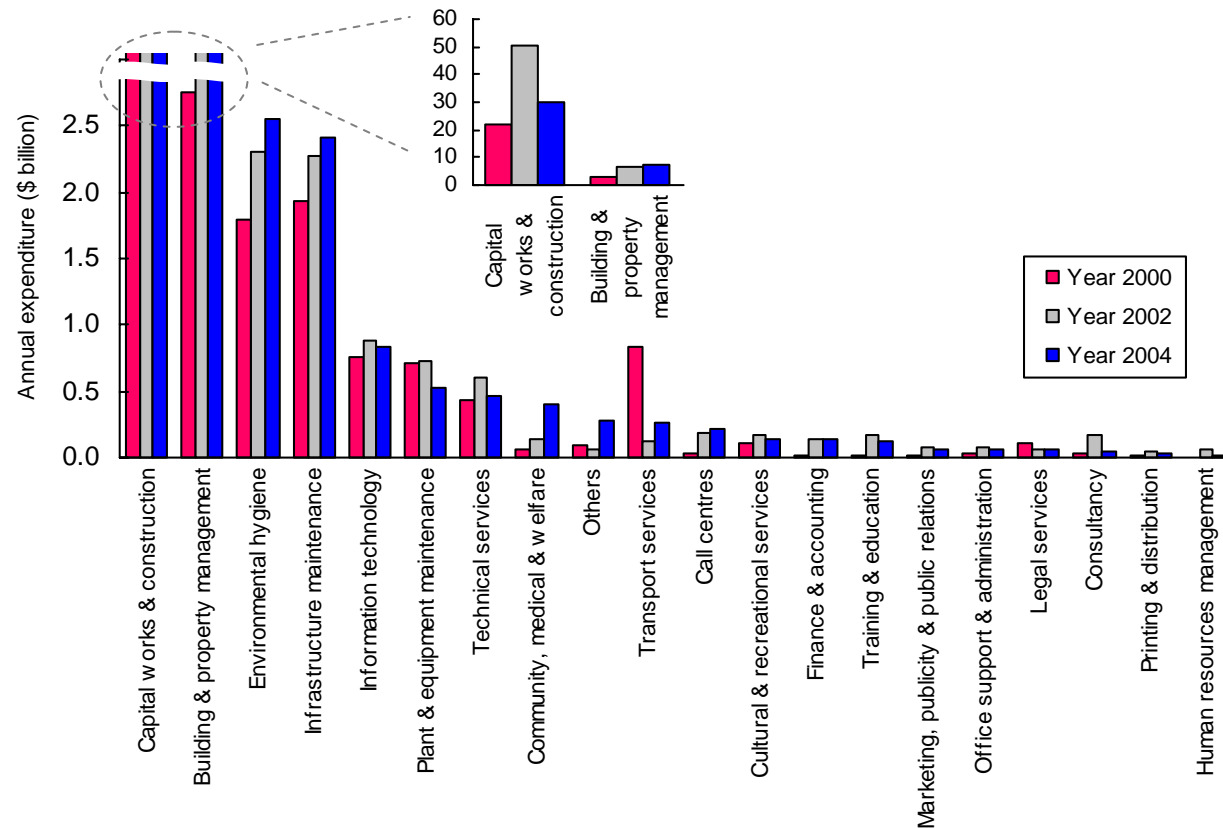
(2) Treasury Branch of Financial Services and the Treasury Bureau, Television and Entertainment Licensing Authority, Independent Police Complaints Committee, Joint Secretariat for the Advisory Bodies on Civil Service and Judicial Salaries and Conditions of Service, Public Service Commission and University Grants Committee



Little change in pattern of annual outsourcing expenditure in 2004

- ◆ As at 1 August 2004, there were 4,512 contracts valued at over \$214 billion. The annual expenditure is \$46.48 billion
- ◆ Capital works and construction, building and property management, environmental hygiene, and infrastructure maintenance contracts continue to dominate
- ◆ In some service categories, there are large numbers of contracts having small contract values. For example, building and property management accounts for 25% of the number of contracts but only 10% of the total contract value. Plant and equipment maintenance accounts for 12% of the number of contracts but only 0.4% of the total contract value

Annual outsourcing expenditure by service category



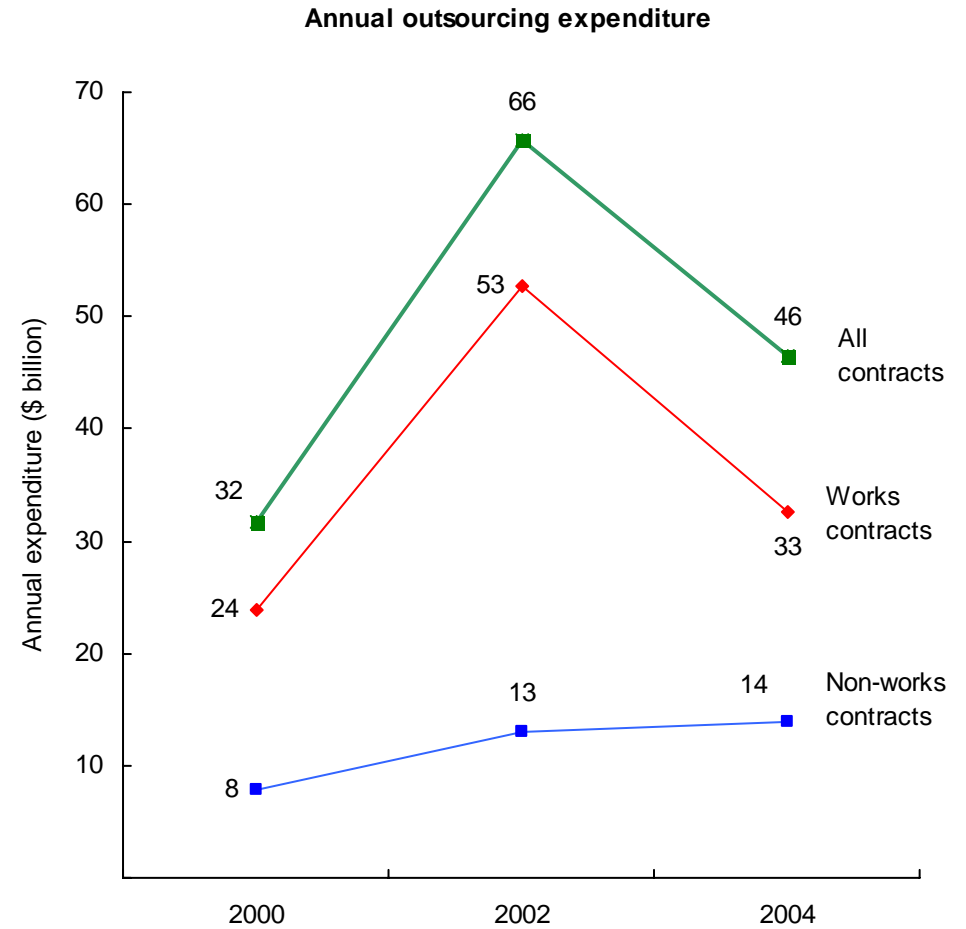
Note

Management of transport facilities (e.g. tunnels), which had been classified as transport services in the 2000 survey, was re-classified as building and property management in the 2002 and 2004 surveys



Significant drop in total annual outsourcing expenditure, mainly on works projects

- ◆ The annual outsourcing expenditure decreased by 30%, from \$66 billion in 2002 to \$46 billion in 2004
- ◆ This is mainly attributed to the 38% fall in expenditure on works and related contracts (i.e. capital works and construction, and infrastructure maintenance contracts)
- ◆ The annual expenditure on non-works contracts increased by 7%



Non-works contracts have increased marginally in size; contracts become longer

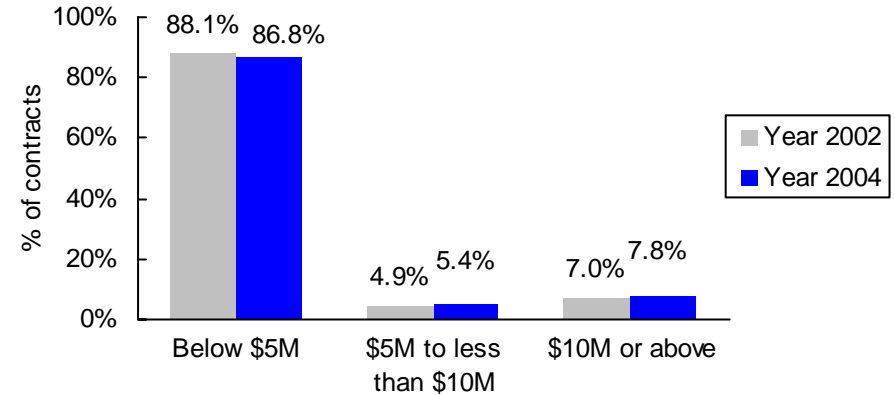
Contract size

- Compared with 2002, the number of non-works contracts decreased from 3,609 to 3,582 in 2004 by 1% whilst the average annual expenditure per contract increased from \$3.6M to \$3.9M by 8%. This suggests that some non-works contracts may have been bundled into larger ones

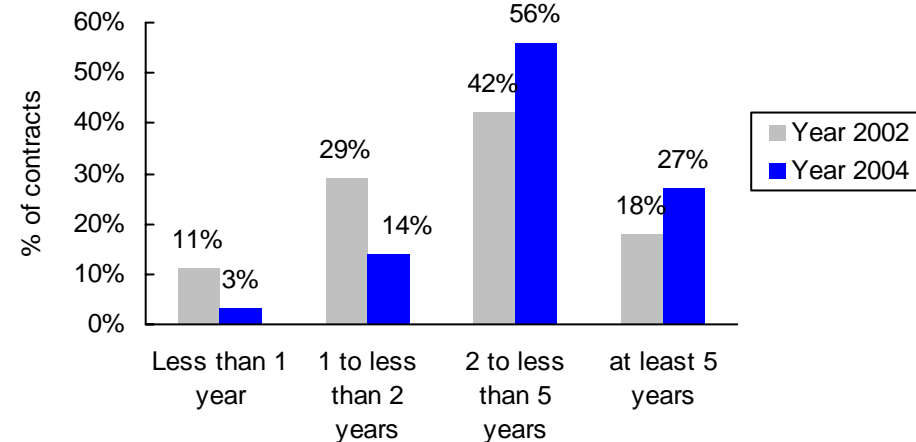
Contract duration

- In 2004, the durations of contracts valued over \$1.3M vary from several months to over 50 years.
- The percentage of contracts lasting 2 years or longer increased from 60% in 2002 to 83% in 2004

Distribution of average annual expenditure of non-works contracts by number



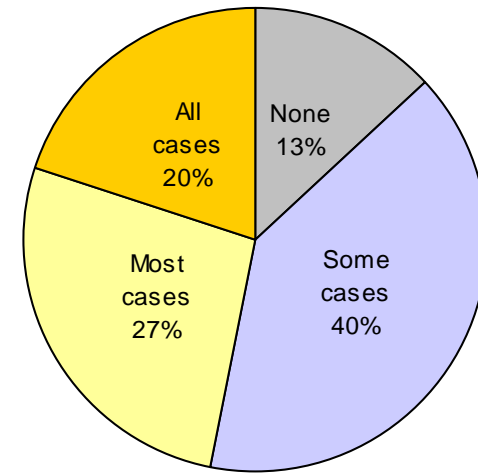
Distribution of contract duration (for contracts valued over \$1.3M)



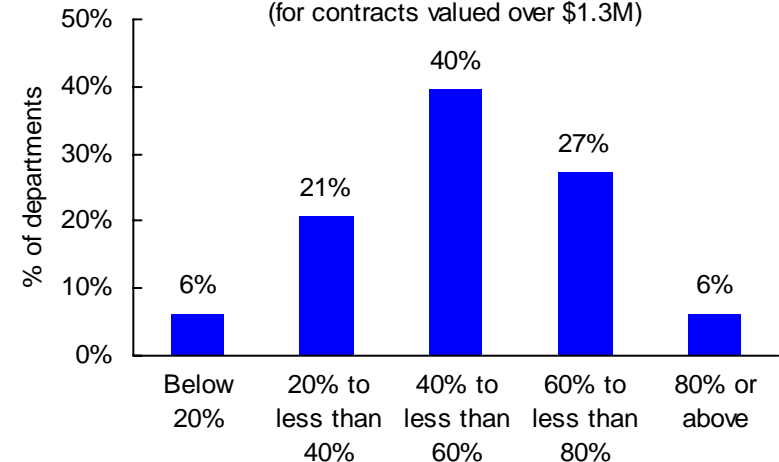
Price dominates in tender evaluations

- ◆ Almost half of all departments use marking schemes in most or all cases when evaluating tenders above \$1.3M; only 13% of departments do not use any marking schemes
- ◆ In some cases, the absence of well-designed marking schemes may lead departments to select low bids
- ◆ When using marking schemes one third of departments use technical ratios of 60% or more, and two fifths fall into the 40% to 60% range. This suggests that quality aspects of tender proposals are given reasonable consideration most of the time. Nonetheless, price is still the dominant factor in most tender evaluations

% of departments using marking scheme
(for contracts valued over \$1.3M)

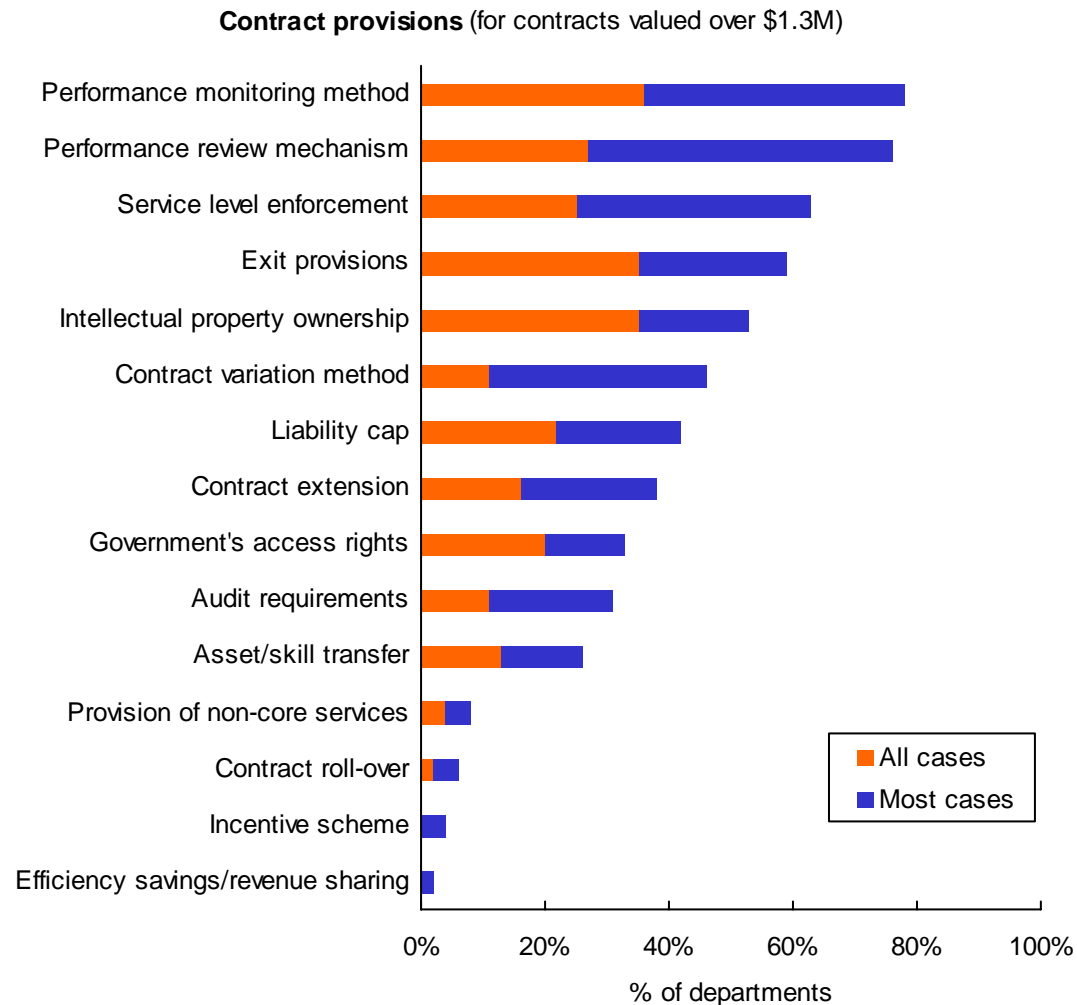


Distribution of technical ratios
(for contracts valued over \$1.3M)



Use of sophisticated contract terms

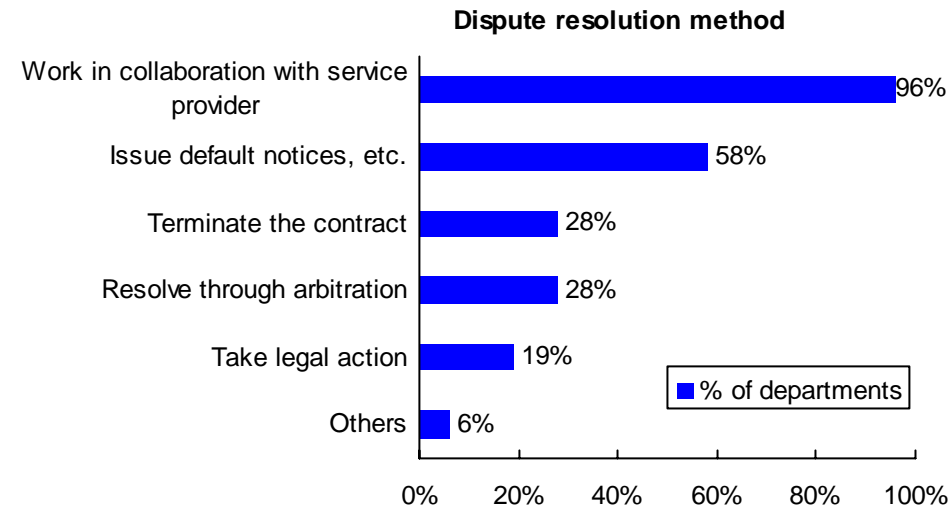
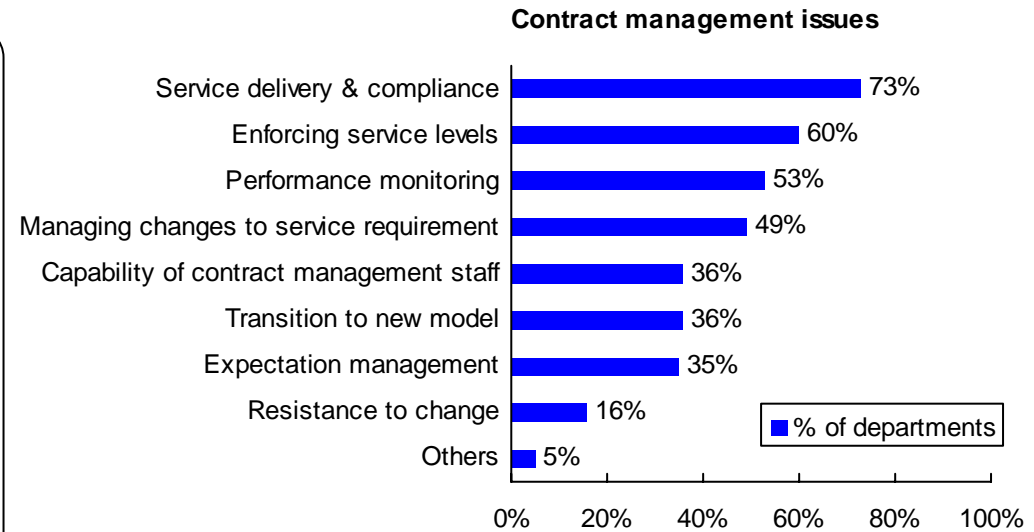
- ◆ Many departments specify the performance monitoring methods, performance review mechanisms and provisions for enforcement against service levels in their contracts
- ◆ Departments utilise practices such as liability caps, provision for negotiating variations, audit requirements and government's access rights
- ◆ Contracts have incentive or efficiency savings sharing schemes in place. Service providers are incentivised to improve service quality only infrequently
- ◆ Most departments adopt a fixed pricing mechanism. Some 60% of departments do not link the payment with quantitative changes in services for all or most outsourcing contracts above \$1.3M. In addition, 78% of the departments do not allow for price adjustments by CPI



Performance management is the major issue in contract management

- ◆ Departments monitor service providers' performance through performance review meetings, performance reports submitted by contractors and on-site inspections/supervision
- ◆ The average contract management cost is about 5%⁽⁴⁾ of the annual outsourcing expenditure
- ◆ Major contract management issues include service delivery and compliance, enforcing performance against service levels, and performance evaluation and reporting
- ◆ Contract management style is moving from rigorous contract enforcement towards relationship management. Almost all departments have attempted to resolve problems in collaboration with service providers, although over half still use traditional methods of issuing default notices, withholding payments, etc.

(4) Based on the weighted average of contract management cost by annual outsourcing expenditure. Two major outsourcing departments are unable to provide figures for analysis



Concern over amount of preparation work required and difficulties in drawing up service requirements

- ◆ The top three concerns about outsourcing are –
 - the amount of preparation work needed (e.g. tender preparation and evaluation)
 - difficulties in drawing up service requirements (e.g. service level agreements, performance measures)
 - difficulties in ensuring quality of work
- ◆ Some departments also experienced constraints in the following areas –
 - lack of market interest
 - lack of in-house expertise to manage the service providers, particularly for IT services
 - complicated outsourcing procedures and regulations, e.g. Stores and Procurement Regulations

