

Report by the
Comptroller and Auditor General

**Inland Revenue/
EDS Strategic
Partnership:
Award of
New Work**

Ordered by the
House of Commons
to be printed 27 March 2000

Executive summary

1 From the 1960s onwards the Inland Revenue developed increasing levels of computer support for its business activities until it was running one of the largest administrative computer networks in Europe. By the early 1990s, its Information Technology Office, which developed and ran the Department's systems, employed over 2,250 and had an annual budget of £250 million.

2 After testing the market and taking external advice, the Department concluded in 1992 that fundamental improvements were required to its information systems and information technology, and that a strategic partnership with a single private sector provider would best meet the objectives of:

- gaining rapid access to modern information systems and information technology skills, tools and technologies;
- achieving substantial improvements in cost-effectiveness;
- improving significantly the speed of response in the development and enhancement of systems;
- optimising career opportunities for Information Technology Office staff.

Following a competition, a ten-year contract was let to Electronic Data Systems Limited (EDS). The work, staff and assets of most of the Information Technology Office were transferred to EDS in two tranches, in July 1994 and January 1996, with some staff remaining with the Department to manage the contract.

3 The Department and EDS run the contract as a partnership, from board level downwards, with both parties putting considerable effort into making the structures work and delivering the high service levels required. Fundamental to the success of the partnership are a clear vision and strategic direction, and a common recognition that it is the objective of both parties to secure benefits under the arrangements. Such an approach requires active management. To assist this, the Department established a risk management strategy, which is reviewed on a regular basis, so that important issues can be drawn to senior management's attention on a timely basis.

4 The contract with EDS is not a fixed price contract because the information systems and information technology needs of the Inland Revenue are constantly developing and changing in response to external factors, such as government policy and Budget changes, and internal factors, such as initiatives to improve the administration of the tax system. New work will account for about a quarter of the forecast £2 billion revenue spend on the EDS contract. The management of the risks of new work is a challenging area for value for money, particularly as the information technology systems developed by EDS will contribute to the future efficiency and effectiveness of many aspects of the Department's operations. This report focuses on the way that new work is commissioned by the Department.

5 In considering how the Department manages the risks associated with the procurement of new work, the report examines three main issues:

- the Department's process for commissioning new work;
- the maintenance and development of the skills necessary to assess the proposals and performance of EDS; and
- how the cost of the service is compared with what is being achieved elsewhere.

The process for commissioning new work

6 The framework which the Department uses to manage the risks associated with commissioning new work from EDS is basically sound and should ensure that value for money is achieved if the steps in the process are followed consistently. Pressure to deliver an increasing workload to demanding timetables has led to closer working with EDS on the development of information technology solutions to business requirements and has increased the importance of effective risk management. The Department has identified, and is addressing, most of the key risks.

7 Recommendations for further improving the Department's management of risk include:

- making a formal assessment of the risks attached to closer working with EDS in the rapid development of information technology solutions;
- formalising the criteria for deciding when to refer EDS proposals to the Department's information technology experts for scrutiny;

- improving project managers' understanding of the contract's complex pricing mechanism to reduce the risk of nugatory expenditure; and
- tightening up post-implementation and hand-over procedures to ensure that live running of new systems can be monitored effectively.

Skills

8 To operate the partnership effectively and to contribute to strategic issues senior staff in the Department need to maintain an independent knowledge of current developments in information systems and information technology. This knowledge depends on key individuals building and maintaining a network of contacts, reading relevant technical publications, attending events and seminars, visiting suppliers and other organisations, as well as purchasing market reports and analyses from specialist information technology research organisations. The Department's framework for staff development has helped to ensure that these activities take place and the Inland Revenue is widely regarded as a source of information on the successful management of information technology outsourcing.

9 There has been very low staff turnover in some small technical units in the Department critical to the operation of the partnership and to the award of new work, resulting in a concentration of skills and knowledge in a small number of people. This had some advantages in the early stages of the contract, but it is important for the Department to have the human resources to remain an intelligent customer and to have a sufficiently large pool of trained information technology staff to secure a reasonable rotation for career development and skill enhancement, as well as to be able to fill vacancies if experienced people leave the Department.

10 Recommendations to the Department on the maintenance and development of skills include:

- reviewing the role of the specialist Information Technology Technical Unit to ensure that its important work on strategic information technology issues is not put at risk by increasing involvement in the detail of projects; and
- improving succession planning and increasing the rotation of staff in specialist units working in partnership with EDS.

External comparisons

11 While the Department's active management of the risks associated with the commissioning of new work and the effective operation of the partnership by skilled staff increase the likelihood of securing value for money, they do not guarantee it. For example, the incentives in the contract to improve efficiency may be insufficient to keep pace with the market. External perspectives can provide assurance about the comparative value offered by EDS.

12 The Department has used benchmarking to compare aspects of the contract with performance elsewhere. Difficulties were encountered, and were to be expected, in making the comparisons, and the results contain significant caveats. Nevertheless the Department concluded that, overall, the parts of the contract studied were competitive with the market. The chief area of concern was a low, but improving, level of software development productivity.

13 The contract allows existing services provided by EDS to be market tested if there is evidence, for example from benchmarking, that the service provided is uncompetitive. Before the Department can proceed to a full market test, EDS is entitled to match or better any indicative price. So far, no existing service has been market tested and one new requirement, the provision of an Internet capability, has been subject to open competition and let to another organisation. Market testing, therefore, has provided little direct evidence of the comparative value offered by EDS.

14 In view of this, recommendations to the Department on making external comparisons focus on benchmarking and include:

- increasing the use of external expertise to help address difficulties in obtaining useable comparative information from other information technology providers; and
- extending the use of benchmarking to other services provided under the partnership with EDS.

Overall conclusion

15 The Inland Revenue's strategic partnership with EDS has, by comparison with many other major projects in the information technology field, been successful in helping the Department deliver significant changes in taxation policy to demanding timetables, thus meeting an important objective of the outsourcing. From the Department's experience, important ingredients of successful management of such partnerships include active involvement by top management, a recognition that both parties need to secure benefits, active management of the risks associated with this type of procurement approach, and a commitment to resolving issues arising in a positive, constructive manner.