National Audit Office

Improving corporate functions using shared services

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SUMMARY

1 Corporate services provide vital support to the delivery of effective and efficient public services that meet citizens' needs. They include activities such as finance and accounting, human resources, procurement, information technology, facilities management and estates management. These activities are usually not highly visible at the front line, but they have a major impact on the quality of public services. Corporate services are often least visible to the citizen when they are at their most effective.

2 Mechanisms to improve the efficiency and effectiveness of corporate services include more streamlined processes, better performance data, dissemination and adoption of best practice, and outsourcing, in addition to shared services, which form the subject of this report. Shared services involve the combination of activities across different parts of an organisation, or across separate organisations, in order to bring efficiency savings and improve service. They require a customer focus and they give organisations the opportunity to provide services to other organisations. They do not represent an end in themselves, but they provide a means, alongside other mechanisms, to greater efficiency and effectiveness.

3 The Cabinet Office estimates there is scope to save £1.4 billion from annual expenditure on finance and human resources functions, and to improve service quality, by implementing shared services across the public sector. The figure is not a target for departments and it does not form part of the £21 billion Efficiency Programme target. It represents 20 per cent savings on an estimated annual expenditure of £7 billion, which is in line with what other organisations, mainly in the private sector, have already achieved. There is a wide range of implementation options for shared services, from provision that is in-house or shared among related public bodies to fully outsourced arrangements.

4 Shared services and streamlined processes are closely linked. Some organisations use a move to shared services as a mechanism to drive the streamlining of processes. The risk is that inefficiencies can then become entrenched. Other organisations find it sensible to streamline their processes before moving to shared services. A combined approach, adopted for example by NHS Shared Business Services, is to streamline as part of the process of migration to shared services.

5 We decided to report on shared services now because the transition from the 2004 Spending Review to the 2007 Comprehensive Spending Review[4] is a critical point in the development of shared services. Our report focuses mainly on finance and human resources, which are the more developed shared service areas in the public sector.

Shared services are progressing across government but reported savings to date are relatively small

6 Central government as a whole made slow progress initially in taking shared services forward after Sir Peter Gershon identified their potential in 2004. Momentum has picked up over the last year and there are various programmes under way, many not yet sufficiently established to start delivering savings.

4 The Comprehensive Spending Review is a long-term and fundamental assessment of government expenditure, including the identification of departmental spending allocations for years 2008-09, 2009-10 and 2010-11.

7 The Cabinet Office has divided government into sectors in order to provide focus in developing shared services. The sectors have published plans for shared services. Most sectors now have some level of operational shared services. A large number of local arrangements dominate some sectors. In other sectors the emerging pattern is of a single shared services centre being steadily extended to cover more bodies within the sector. The least developed sector is the central government sector of small departments which includes, for example, the Department for Culture, Media and Sport and the Foreign and Commonwealth Office.

8 At March 2007, departments had reported savings across all corporate service functions of £1 billion, of which £315 million relates to finance and human resources. Some element of this has been achieved through shared services but it is not possible to determine how much because in many cases shared services form part of broader corporate services transformation programmes. The savings reported to date are relatively small and suggest that there is substantial untapped potential for securing savings through shared services and other means.

The Cabinet Office has promoted shared services but lacks a clear overview of the benefits being secured by departments

9 The Cabinet Office promotes shared services across government. The Head of the Home Civil Service puts shared services on the agenda of the Civil Service Steering Board when decisions need to be taken across government and he has written to all Permanent Secretaries to emphasise the need to move forward on shared services. The Shared Services Team has played a key role in promoting the development of shared services across government by working with OGCbuying.solutions to enable some software licences to be transferred cost effectively across government, providing an internal consultancy service for government, building a cross-government network of shared services professionals, identifying and tackling barriers to shared services and allocating central government bodies to sectors to provide focus. The Cabinet Office does not have powers to force departments to adopt shared services because accountability for generating savings through measures like shared services rests with departments' Accounting Officers, there being no separate Accounting Officer for shared services. The Cabinet Office has not prescribed any particular models, for example on payment mechanisms or on whether participation is voluntary or mandatory in any scheme that is made available.

10 The Cabinet Office Shared Services Team has systematically identified a range of barriers to shared services in government and has successfully tackled some of them. The most significant barriers concern VAT and issues around buying and selling services.

- Under fundamental VAT rules reflected in EU agreements, buying services rather than providing them in-house may incur a VAT cost that can reduce the attraction of shared services. This is not an issue for government departments and local authorities because, as a result of measures introduced in the past to remove disincentives to outsourcing or to ensure that VAT is not a cost on local taxation, they can reclaim VAT in appropriate circumstances. For other bodies, principally non-departmental public bodies and the higher and further education sectors, VAT incurred on buying in services may be an irrecoverable cost. The Cabinet Office estimates that the VAT barrier is potentially inhibiting £70 million in annual savings for non-departmental public bodies. The potential benefit from removing the VAT barrier for higher education and further education bodies is believed to be tens of millions of pounds per year. Further work is being carried out in the sector to provide a better estimate.
- There has been confusion, particularly in the central government sector of small departments, over which departments will buy and which will sell. This was clarified in April 2007 when the Civil Service Steering Board designated the Department for Work and Pensions and HM Revenue & Customs as selling departments. There are no clear financial incentives for organisations to choose to sell services because, under rules designed to ensure departments receive funding only as allocated by Parliament, surpluses are not allowed to be made from transactions between departments, although departments may gain by reducing their own average costs through selling services. The designated selling departments have not yet determined how they will set prices, nor whether they will compete against other organisations, such as existing public sector

shared service providers. The Cabinet Office has resolved some incentive issues, notably over who can claim headcount reductions. It has also started a process potentially leading to the Cabinet Office buying services from the Department for Work and Pensions. This, however, is the only example of a commitment from a smaller department to buy services from another department. It will be the first test case of how a large department gives a good service to a much smaller department buying its services. Some issues remain. There are no clear mechanisms to push departments to buy or sell shared services, so there is a risk of failing to benefit fully from the economies of scale that exist within large departments.

11 The Cabinet Office's figure of £1.4 billion for potential annual savings from shared services is derived as 20 per cent of an estimated expenditure of £7 billion on finance and human resources and is not broken down into departmental elements. This makes it difficult for the Cabinet Office to track meaningful progress towards the overall figure. Sector plans do not contain sufficient financial detail for the Cabinet Office to assess whether the sum of individual projects will deliver savings on the scale required. There is a lack of transparent data about the costs of public bodies' existing corporate services.

Shared services in the NHS and Prison Service are on course to deliver savings but experienced early problems with customer satisfaction

12 Two of the more established public sector shared services are NHS Shared Business Services, operational since April 2005, and the Prison Service Shared Service Centre, in place since April 2006.

13 From our analysis of results and forecasts, we estimate that NHS Shared Business Services will potentially deliver net present value savings of £250 million over eleven years, of which £160 million is likely to occur over the first nine years, breaking even after five years. On the same basis, we estimate that the Prison Service Shared Service will deliver net present value savings of £120 million over nine years, with a break even point after five years. Customers of NHS Shared Business Services are guaranteed initial gross savings of at least 20 per cent in the cost of their corporate services with further guaranteed cost reductions of two per cent each year. The Prison Service Shared Service will release savings ultimately equivalent to just over 30 per cent of the gross costs of corporate services. Both sets of forecast business results are estimates of future performance based on existing evidence and are therefore subject to some uncertainty.

14 Organisations receiving these shared services reported early problems. This is a common experience with large transformation programmes. Difficulties stem mainly from operational problems associated with the challenge of implementing large and complex systems and from the cultural changes necessary in customer organisations. Evidence from NHS Shared Business Services is that customer satisfaction levels rise over time.

15 Shared services have brought other benefits. Those most common non-financial benefits cited by customers of NHS Shared Business Services are better management information, paperless transaction processing, faster transaction processing and a step change in the robustness of processes. Customers have also seen substantial savings in procurement costs.

16 Neither of the shared services are yet performing at leading practice standards of efficiency but they are constantly pursuing improvements. Leading practice performance standards rely on characteristics such as invoices being consistently accompanied by purchase orders, automatic approval of low value invoices with retrospective audit checks, and 'passive authority' where larger invoices are paid automatically after an agreed period in which there is no response to requests for authorisation. The Department of Health is currently investigating the scope for automatic payment of low value invoices that have had prior purchase approval.

Value for money statement

17 Existing shared services are on course to deliver substantial financial savings but they need to make further progress in tackling problems with customer satisfaction in order to demonstrate value for money. It is not clear that wider shared service activity across government is on a scale sufficient to deliver value for money savings approaching the £1.4 billion potential estimated by the Cabinet Office.

Recommendations

To improve the broader management of corporate services

1 *Issue: Public bodies will miss potential efficiency savings if they do not streamline their processes, whether or not they move to shared services.* **Public bodies should streamline their corporate service processes in line with best practice and their own specific requirements.** They should identify and remove processes and aspects of processes where costs outweigh benefits. Streamlining will bring direct financial benefits regardless of any subsequent action and will put public bodies in a strong position to move to shared services if appropriate.

2 *Issue: Public bodies cannot quantify potential savings from sharing corporate services when they lack cost and performance data. They are unable to gauge whether their corporate services are improving over time.* **Public bodies should improve how they analyse the performance of their corporate services.** Management Boards should expect to receive clear information on the cost and performance of corporate services, drawing on performance indicators such as those published by the public sector audit agencies.[5] As part of this, bodies should regularly benchmark their performance, with support from the Cabinet Office to encourage consistency and comparability.

3 *Issue: Public bodies cannot assess whether their corporate services are delivered in the most cost-effective way if they do not make comparisons with alternative options.* **Public bodies should review regularly whether there are more cost-effective ways to obtain their corporate services.** They should carry out rigorous reviews of performance against what is possible through alternative approaches such as shared services. They should plan future corporate services provision in line with the results of these reviews. If public bodies choose not to adopt shared services, they should demonstrate clear business cases showing why shared services are not the most suitable option. This approach could be termed 'share or explain'.

4 *Issue: The Cabinet Office is not well placed to drive improvements on corporate services through the use of shared services when there is a lack of clear information on the relative performance of departments' existing corporate service provision.* **Departments should increase the public transparency of corporate service performance.** Departments should publish an overview of their corporate services performance, including analysis of costs by corporate function, and showing performance against centrally agreed benchmarks in either their annual report or Autumn Performance Report. Such reporting would help the Cabinet Office, for example which leads on the information technology and human resources professions, to become a broader force for corporate service improvement, extending beyond the shared service agenda. Based on the Cabinet Office's estimate of spending on finance and human resources alone, a 10 per cent improvement by the least efficient 10 per cent in central and local government would release annual savings of £70 million.

To improve the take-up of shared services

5 *Issue: Recent machinery of government changes have split some previously existing departments. It is important that these changes do not result in a proliferation of corporate services.* **The Cabinet Office should work to encourage newly formed departments to adopt shared services unless they can present compelling business cases for not doing so.** Departments and other public bodies affected by machinery of government changes should review their corporate service provision and identify opportunities to share services.

6 *Issue: Smaller departments are not yet buying their corporate services from larger departments that can bring economies of scale such as HM Revenue & Customs and the Department for Work and Pensions.* **Departments within the central government sector of small departments should perform a business case evaluation of buying corporate services from one of the two designated sellers, or provide clarity about their way forward towards shared services.** Preparing such a business case is a significant undertaking and

5 *Value for Money in public sector corporate services*, a joint project by the UK Public Sector Audit Agencies, National Audit Office, 2007.

the capacity to undertake the work in both buying and selling departments will need to be taken into account. The estimated annual cost of finance and human resource corporate services within the central government sector of small departments is £130 million. If two thirds of these services by value moved to one of the designated sellers and secured 20 per cent cost savings, this would release around £17 million of annual savings. The selling departments consider this level of savings to be conservative, particularly when wider benefits such as improved management information and process control are taken into account.

7 *Issue: HM Revenue & Customs and the Department for Work and Pensions facilities could increase their capacity enabling them to sell shared services to smaller public sector bodies but there is some uncertainty around their incentives to do this.* **The Cabinet Office and HM Treasury should examine whether existing incentives to sell shared services are sufficient and whether further action is required.** The market for shared services has not yet developed across departmental boundaries, leaving untapped a potentially large source of savings. Providing greater incentives may encourage departments designated as sellers to be more active in designing products to attract customers.

8 *Issue: Despite rapid growth, the majority of NHS bodies are not using shared services.* **Where service provision is retained in house, boards of NHS organisations need to be clear that this represents better value for money than alternative options such as NHS Shared Business Services or outsourcing.** This approach would respect devolved responsibility and accountability while explicitly emphasising the requirement on every NHS body to secure value for money. It would challenge reasons for resisting change that are based on perception or anecdote rather than careful analysis. A business case evaluation would quantify the financial and non-financial benefits that could be secured by a move to Shared Business Services and provide the criteria from which a decision can be made. Shared Business Services' current market share, at 21 per cent, is forecast to deliver £16 million annual financial benefits in 2007-2008. An increase in market share to 30 per cent would realise additional annual benefits of £7 million.

9 *Issue: For some organisations, buying shared services incurs irrecoverable VAT. This provides a potential disincentive to moving to shared services.* **HM Treasury's current financial evaluation of the VAT barrier should assess the degree to which irrecoverable VAT is preventing sharing of corporate services across government and the cost of removing the barrier.** HM Treasury should take firm action in the light of that cost benefit analysis. Any solution would need to be consistent with EU law, the normal principles of public funding and the Government's wider position on irrecoverable VAT.