Outsourcing Acquisition and Procurement Shops

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When it comes to information technology (IT), procurement and acquisition shops have often suggested to program managers (PMs) that a function be competitively sourced. Now, procurement and acquisition shops are themselves being competitively sourced. Competitive sourcing euphemistically refers to outsourcing, or the emigration of in-house functions to an outside provider. Contracting officers (COs), often considered the rainmakers in both public and private organizations, survive by the award and administration of pacts with service providers. Consequently, procurement chiefs are quick to remind PMs that limited permanent staff and scant indigenous IT talent connotes an outsourcing solution. For the federal government, Congress authorizes a set number of employees, or full-time equivalents, making contracting-out indispensable for mission accomplishment.

The age of public sector outsourcing has given redoubled importance to statements of work, the procurement shop, and to contracting officers and their on-site representatives. This has been particularly the case in acquiring IT services since the mid-1990s. The Office of Management and Budget's A-76 guidelines for agencies to evaluate whether to keep noncore functions in-house or outsource them has been applied to all elements of IT. Of particular interest to military planners has been outsourcing hardware and software configuration, help desk support, visual information, records and mail management, telecommunications, and all installation and maintenance of computer wherewithal. With online procurement increasingly in vogue and Department of Defense aggressively planning to complete $2 billion worth of IT functions during the next three years according to McLean, Va.-based Federal Sources Inc., what must be considered by the procurement and the funding program when outsourcing?

If We Must Outsource IT Consider These Factors

Create a statement of work so it is clear what — not how — work will be done. Provide incentives, and plan for disincentives with an appropriate deduction schedule.

Demand value-based pricing and benchmarking — the contractor's price must be readjusted on occasion to the market price or renegotiate rates on a regular basis. Build that into the contract language.

The following costs must be transparent to the government IT executive as the outsourcer's customer:

1. Cost of telecommunication line — contractor reports cost per hours, per distances, per line, per switch, per gateway device, etc.
2. Per-person cost measurement — costs incurred by contract employees have to be reported by the contractor for agency comparison purposes.
3. Operational cost measurement — contractor must report costs in terms of cost per unit hours, storage costs, total cost per hour, fixed costs, and variable costs.

In the private sector, the maxim of cutting costs to increase profits is observed in good times or bad. Hence, the CO almost always encourages the employment of a lower cost, more readily hired/fired, less union-organized workforce in exchange for the permanent workforce. Procurement shops have played the part of docent in the museum of outsourcing — however, some of the head honchos of contracting-out have become the exhibits rather than the tour guides!

The paradigm ending indigenous contracting functions is known as business-process outsourcing. IT advances have made outsourcing of procurement and acquisition functions not only financially viable, but managerially trendy. For instance, both IBM and Electronic Data Systems offer contracting services. IBM's Global Services division promotes its Business Process Service using Lotus Notes-based, Internet-accessible procurement software and a vast supply network to offer outsourcing of contracting functions [1]. Global Services, based in Somers, N.Y., had revenues of $26 billion in 1997 [2]. IBM will take over procurement tasks for Hartford, Conn.-based United Technologies Corp. (UTC), a $25 billion manufacturer of aerospace, automotive, and building products. UTC's goal is to cut $750 million in purchasing costs by 2000.

While administrative lead times for government procurements often are measured in months, commercial companies like Boeing and Texas Instruments can measure their lead times in days, hours, and even minutes. The pattern of outsourcing of procurement shops first took shape in industry rather than reinvention-ridden government. Long lead times are the principle contributor to outside sources replaced by in-house contracting functions.

The Financial Rub of Outsourcing

Outsourcing is the divestiture of a core or noncore in-house function to an outside provider.

Privatization, often confused with outsourcing, refers to the transfer of strictly public work, and often the wherewithal to perform that work, to the private sector.

Contracting-out is not necessarily outsourcing or privatization. For example, contracting-out for IT services that have never been performed in-house is not outsourcing.

IT labor costs associated with outsourcing, privatization, and contracting-out can and do vary. Outsourcing-oriented contracts can be written between government or private entities. According to the Outsourcing Institute, the second largest share (30 percent) of the estimated $100 billion worth of U.S. corporate outsourcing ventures in 1996 was in administrative and similar services [3]. It does not take an encyclopedic grasp of things financial to anticipate that the outsourcing of procurement shops — the prime mover of most, and certainly the administrator of all, contracting-out — was predictable.

Why is this kind of outsourcing profitable? Just as outsourcing-type contracts have mainly financial motivations, outsourcing the contracting personnel and their work is based on specialization, which efficaciously lowers costs of employees, and shortens the associated lead times. COs may resent the latest nostrum from corporate cube-farm idea hamsters — outsourcing contracting — but they must be the first to respect the financially sound logic underpinning this strategy. PMs are poised to ask whether they can get existing procurement services for a reduced price at a break-even quality level. Replying in the affirmative, companies such as IBM offer to immediately tighten overhead costs as they rip into the expense of fringe benefits for in-housers. The procurement process resembles to busy executives the chaotic, annual ritual of the running of the bulls in Pamplona, Spain. PMs are tired of being gored by the expense and lost time associated with the current method of contracting-out.

The systematic and aggressive use of IT outsourcers who tap into reduced-cost labor pools in low-cost geographic areas quickly undermines the economic viability of in-house procurement shops [4]. It is a return to Adam Smith's pin factory with a vengeance: specialization ruthlessly reduces IT costs. Many more in-house procurement shops will soon find themselves the victims of service shedding. Outsourcing has attached itself lamprey-like to the soul of every cutback-stricken organization — and the contracting shop is increasingly coming under the penetrating gaze of fiscal watchdogs. It is ironic — and to those last, least, and left-out during outsourcing's heyday — pleasurable to witness the champions of expropriation themselves expropriated. ◆

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