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TOPIC:

## Outsourcing in the Public Sector

Examining the role of the  
Chief Procurement Officer in the  
outsourcing decision and process.



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Published by NIGP:  
The Institute for Public  
Procurement.

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# OUTSOURCING IN THE PUBLIC SECTOR

*Examining the role of the Chief Procurement Officer in the outsourcing decision and process.*

## **INTRODUCTION**

In the public sector, outsourcing is the “contracting out” of functions that historically have been provided by public employees. The belief that there are functions which are best performed by the private sector is not new. Moving these functions from the public to the private sector requires a fair and open process in the public’s best interest.

*NIGP: The Institute for Public Procurement* recognizes that the outsourcing of particular governmental functions can be a fiscally sound tool of responsible public administration. However, identifying and assessing the elements of public performance most appropriate for outsourcing -- and ensuring a successfully executed outsourcing decision – is a substantial challenge for all entities.

Public procurement offers a uniquely qualified and professional resource for government decision makers considering outsourcing alternatives. The Chief Procurement Officer (CPO), or Procurement Director or Purchasing Manager, serves a strategic role in a public entity’s decision to outsource. The CPO is central to a fair, transparent and effective outsourcing process. While the decision is ultimately reserved for the elected body, or senior executive, the CPO is prepared to provide informed insight on market structure, cost, risk, competitive methods and contract form as these factors impact the quality and cost of services. The CPO is uniquely positioned to help design, and to manage, a process for achieving a successful public outsourcing effort. As such, it is important to engage the CPO early as a strategic partner in the outsourcing assessment and as the administrator of any ensuing selection and contract formation process.

## **WHAT IS PUBLIC OUTSOURCING?**

Outsourcing is the “contracting out” of a service traditionally delivered by public employees. While examples exist from over a century ago, outsourcing gained momentum in the United States and Great Britain in the early 1980’s. Both governments established criteria for contracting out a process or function. OMB Circular A-76 is the current guide used for outsourcing at the federal level in the United States. Many states and local jurisdictions have adopted similar guidance. OMB Circular A-76 provides insight on “how” to outsource while describing the characteristics of “inherently governmental activities” versus “commercial activities.” It does not, however, offer a definitive list of which functions are “inherently governmental” (and, therefore, should not be outsourced) and which functions are potentially “commercial.”

Two questions, each with their own considerations and processes, confront a governmental entity: (1) Whether to outsource; and if so, (2) How to do it.

## **WHETHER TO OUTSOURCE**

### **“Inherently Governmental Activity”**

OMB Circular A-76 defines “inherently governmental activity as “an activity so intimately related to the public interest as to mandate performance by government personnel.”<sup>1</sup> These activities require the exercise of substantial discretion in applying government authority or in making decisions for the government. Inherently governmental activities normally fall into two categories: the exercise of sovereign government authority or the establishment of procedures and processes related to the oversight of monetary transactions or entitlements.

An inherently governmental activity involves:

- Binding the United States to take or not to take some action by contract, policy, regulation, authorization, order or otherwise;
- Determining, protecting and advancing economic, political, territorial property, or other interests by military or diplomatic action, civil or criminal judicial proceedings, contract management or otherwise;
- Significantly affecting the life, liberty or property of private persons; or
- Exerting ultimate control over the acquisition, use or disposition of United States property (real or personal; tangible or intangible, including establishing policies or procedures for the collection, control or disbursement of appropriate and other federal funds.

### **Key Considerations in the Outsourcing Determination**

Though examples of outsourcing are present in nearly every facet of government, the threshold decision, whether to outsource a particular function, is a difficult one requiring a thorough, thoughtful assessment. In his book, “Outsourcing State and Local Government Service,” John O’Looney describes the decision to outsource governmental service as similar to a corporation choosing to divest itself of peripheral businesses to better focus on core competency. O’Looney adds that, “while the comparison is apt in many respects, the decision to outsource a government service is typically more complex than is the case in the private sector. Political and cultural considerations, ideology, and concern for values other than the bottom line will, for good or ill, affect the decision making in the public sector differently than in the private sector” (1998).<sup>2</sup>

A key consideration in the decision to outsource is an organization’s sensitivity to risk.

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<sup>1</sup> Office of Management and Budget. (1999). *Performance of commercial activities* (OMB Circulation No. A-76). Washington, DC: U.S. Government Printing Office. Retrieved from [http://www.whitehouse.gov/sites/default/files/omb/assets/agencyinformation\\_circulars\\_procurement\\_pdf/a076supp.pdf](http://www.whitehouse.gov/sites/default/files/omb/assets/agencyinformation_circulars_procurement_pdf/a076supp.pdf)

<sup>2</sup> O’Looney, J. (1998). *Outsourcing state and local government services: Decision-making strategies and management methods*. Westport, CT: Quorum Books.

According to O’Looney, a strategic manager must consider the following points:

- How outsourcing may increase the susceptibility of local government to systemic corruption of its mission.
- The degree to which the service can be described and monitored in terms of clear performance measures.
- The degree to which the service that is being outsourced is, itself, critical or necessary to ensure that the function is effectively carried out (e.g. professional services).
- The number of potential providers of the service.
- The economic costs and benefits of transitioning to an outside provider of service.
- The political and social costs/benefits when making the change.

Consideration of these factors leads the strategic manager to a comprehensive view that considers not only front end savings, but the long term effect of possible failure by the “outsourced” service provider.

When a governmental service is outsourced, the institutional knowledge and expertise held by the public employees may be lost. The risk of failure is present, whether for poor performance or un-sustained public support. The public entity will bear the cost of restoring the service, including the restoration of “in-house” expertise and knowledge. This too must be measured by a strategic manager when considering outsourcing.

### **Valuable Role of the Public Procurement Professional in the Outsourcing Determination**

What role should the public procurement professional have when determining whether or not to outsource a particular governmental function? In an interview with the Global Delivery Report, Dawn Evans, President and CEO of the Sourcing Interest Group, observed that, “[p]rocurement brings robust data to the table.”<sup>3</sup>

Procurement professionals use market intelligence in their sourcing decisions and can bring compelling data to outsourcing decisions. This not only includes cost factors, but also market research and the identification of innovative suppliers, solutions and process improvements.

Ideally, strategic outsourcing involves all areas that have a stake in the outcome – the internal business units, legal and procurement. Procurement’s experience running complex supply chains, price negotiations and supplier relationships, while adjusting to a changing global environment, makes it a valuable asset in determining the optimal public outsourcing process.

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<sup>3</sup> Evans, D. (2011). Counterpoint: Why procurement does belong at the outsourcing table. *Global Delivery Report*. Retrieved from <http://globaldeliveryreport.com/counterpoint-why-procurement-does-belong-at-the-outsourcing-table/>

## **HOW TO OUTSOURCE**

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### **Essential Features of a Public Outsourcing Process**

The process must be competitive, fair and transparent, and capable of delivering the best value for the public. These public policy mandates create an environment where the procurement professional plays an integral role in the outsourcing decision and its execution. When a potential outsourcing opportunity is identified, the outsourcing process should embrace the following work flow with the understanding that it may be ended short of completion at any time:<sup>4</sup>

1. **Comprehensive risk assessment** (including an examination of public interest, safety, health and security.)
2. **Requirements determination** (An evaluation and statement of what is needed, when it is needed and how much is needed, which may include considerations of historical usage, future need, program objectives, trends, demand analysis, market analysis and the use of software or other forecasting tools.)
3. **Sourcing** (A fair and transparent process leading to the selection of a supplier/contractor whose costs, qualities, technologies, timeliness, dependability and service best meet the established requirements.)
4. **Vendor performance and accountability** (Specific, measurable performance criteria including service level agreements and reporting requirements included in the contract.)
5. **Post-award contract administration** (Management supervision and oversight to assure full compliance by the supplier/contractor with the contract terms and conditions including price and vendor performance and accountability criteria; as well as contract administration that includes payment, monitoring of progress and performance, inspection and acceptance, quality assurance, modifications, negotiations, contract closeout and other activities.)
6. **Communication** (A continuous flow of information throughout the outsourcing process from the public entity to all stakeholders including employees, contractors and the public, before and after contract award.)

### **Central Role of the Chief Procurement Officer in the Strategic Outsourcing Process**

Procurement professionals go beyond negotiation to drive deals that encourage suppliers to innovate and continuously improve their processes.<sup>5</sup> Managing the elements of an outsourcing process, formal or informal, calls upon the skills and experience that a Chief Procurement Officer utilizes every day in the normal course of public purchasing. The Chief Procurement Officer, Procurement Director or Purchasing Manager also acts as a professional resource for decision makers by assisting in the outsourcing process in, but not limited to, the following areas:

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<sup>4</sup> National Institute of Governmental Purchasing, Public Procurement Practice, Outsourcing

<sup>5</sup> Ibid, Evans, D (2011)

- Market and vendor research;
- Cost and pricing analysis;
- Assistance with risk assessments;
- Development of statements of work and service level agreements;
- Management of competitive source selections and evaluation teams;
- Contract negotiation, formulation and award;
- Post-award vendor and contract management; and
- Ability to communicate effectively with all stakeholders throughout the process.

## **RECOMMENDATIONS AND CONCLUSION**

Outsourcing has a direct impact on a government entity's ability to function successfully and deliver necessary services to the public. The decision to outsource must be well-informed and thoughtful and should be supported by skilled professionals with the strategic vision and expertise to improve operations while protecting the public good.

As a matter of course, the Chief Procurement Officer promotes competition, ensures transparency, understands the place of the government organization within the marketplace, and manages the risks associated with the purchasing process. These competencies, together with the inherently governmental nature of the public procurement function, establish the definitive and integral contribution professional procurement staff can bring to the outsourcing decision and its successful execution.

While the final decision to outsource may reside with the elected body or senior executive, the effectiveness of the outsourcing process and the likelihood of a successful outcome are greatly enhanced by the early engagement and contributions of the Chief Procurement Officer.