HARINGEY COUNCIL

Agenda item:

Executive **On 13 June 2006**

Report Title: **IT insourcing: budget issues**
Forward Plan reference number (if applicable): **N/A**
Report of: **Chief Executive**

Wards(s) affected: **All**	Report for: **Information**

1. Purpose

1.1 To set out the progress in the insourcing of the support for the Council's IT infrastructure.

1.2 To report the emergent financial challenges caused by the reopening of negotiations in December 2005, the agreement reached with the former supplier and the approach adopted by the former supplier as the settlement was reached and subsequently.

1.3 To highlight the risks and challenges as the insourcing project moves forward.

2. Introduction by the Leader

2.1 The previous administration made a difficult decision to insource its IT infrastructure support arrangements. As set out in the report the costs of doing this have increased for a variety of reasons.

2.2 Modern organisations that are heavily dependent on IT need robust support arrangements, and we have decided these are best delivered in-house rather than relying on third party contractors. The move gives us important in-house capacity and a structure to ensure not only the maintenance and security of vital IT systems now but a strong cost-effective basis for developing our IT systems in the future.

2.3 The cost increases have been contained within existing resources and there will be no impact on the council tax.

2.4 The insourcing project will be tightly managed by the Chief Executive and her team and tightly overseen by me and my colleagues on the Executive.

3. Recommendations

3.1 To note the completion of the Tech. Refresh project and the reasons for the Insourcing project.

3.2 To note the emergent financial challenges facing the insourcing project and the

Council's IT budgets and, in particular, their direct causes namely: the reopening of negotiations in December 2005, the settlement agreement reached with the former supplier and the approach adopted by the former supplier as the settlement was reached and subsequently.

3.3 To note that the proposed approach to the funding of these budget challenges as set out.

3.4 To note the risks and challenges facing the insourcing project and the arrangements that have been put in place to manage those risks.

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4. Executive Summary

4.1 The report sets out the progress in the insourcing of the support for the Council's IT infrastructure and the emergent financial challenges caused by the reopening of negotiations in December 2005, the agreement reached with the former supplier and the approach adopted by the former supplier as the settlement was reached and subsequently. It concludes by highlighting the risks and challenges as the insourcing project moves forward

5. Reasons for any change in policy or for new policy development (if applicable)

5.1 The report does not in itself represent proposed or actual changes in policy.

6. Local Government (Access to Information) Act 1985

6.1 No background papers were used in the writing of this report which are not exempt.

7. Background

7.1 In June 2003, the Executive agreed a project to refresh the Council's infrastructure. This was a planned replacement of the Council's entire IT infrastructure and was planned and commissioned as a joint exercise with Deloittes (as architects), Northgate Information solutions (NIS) (as builder and deployment agent) and the Council.

7.2 The infrastructure contract was let in 2002 to NIS, as part of the desegregation of our outsourcing arrangements from the previous bundled contract with ICL/Fijitsu. The terms of this contract included provisions to cover the refresh of the Council's infrastructure, but precise terms could not be established as the nature and timing of any refresh were, by their very nature, uncertain. The contract was due to run to 2009, with a potential extension to 2012.

7.3 It was envisaged that NIS would play the substantial role in managing the deployment and, therefore, the transition of support from the old infrastructure to the new one. In parallel with the project, revised contractual terms would be agreed with NIS to cover their support of the new infrastructure.

7.4 Members will recall that the refresh project faced substantial difficulties. In the Spring of 2005 it was recognised that the project would overspend by approximately £10 million and the decision was made to bring the project in house. The project management arrangements were reviewed by the Audit Commission, who reported to the Executive in January 2006. The project is now completed and the Council's infrastructure has been refreshed.

7.5 As reported to the Executive in December 2005, it proved difficult to reach acceptable terms with NIS for them to provide the support to the new infrastructure. The Council was presented with a stark choice: to continue with NIS or to potentially breach its contract with NIS and deliver the service in house. The two options were considered by the Executive in December and appraised against three headings: cost/price, risk and contractual/commercial issues.

7.6 The in house option, which actually included the outsourced provision of certain key and high risk elements, was assessed to be substantially cheaper than the NIS offer but members were advised not to take account of this saving in coming to a decision due to (a) the inherent uncertainty in our cost projections as the Council has not run this service in house before and (b) the need to review our overall approach to IT support, in particular the recognition under either option that we were short of technical/architectural expertise. This later point will need to be picked up in due course. The appraisal against the other criteria was finely balanced and centred on the risk to good service delivery from the option. Members decided, based on officer advice, to insource the service and seek a negotiated exit from the contractual arrangement with NIS.

7.7 Following the decision by the Executive in December, the then Interim Chief Executive was approached by NIS and negotiations were reopened. This culminated in a revised offer which was presented to the Executive on 18 January 2006 for decision. Members endorsed the previous decision and officers sought to negotiate with NIS.

7.8 Settlement has now been reached but a combination of:

- the reopening of the negotiations;
- the consequences of the settlement;
- the approach of NIS in the run up to and after the settlement; and
- other changes (detailed below)

have led to a projected cost in excess of funding of £2.9 million. This report explores:

- each element of the cost increase; and
- highlights the on-going risks and the management action being taken to manage and contain them.

8. Cost increase

8.1 The costs have increased over those projected in December for four reasons. These are explored in this section and summarised in the table at the end.

8.2 Reopening negotiations

The decision to insource was taken formally on 20 December, following extensive discussion. It was assumed that the insourcing project would start in February, following preparatory work in late December and January. As set out above, negotiations were reopened on 23 December by the Interim Chief Executive and the final decision was made by the Executive on 18 January. Officer time in the intervening period was taken with servicing the on-going negotiations and, as there was not a firm decision, commitments towards the insourcing project could not be made. The insourcing project formally started on 6 March, five weeks after the planned start date.

In the December report, it was estimated that each week of delay would cost approximately £200,000. This is because the support for the new infrastructure was being provided from within the Refresh project, which was only funded to the end of January, and because this resource was, by its nature, short term and expensive project resource rather than base, salaried staff. The projection was broadly accurate and the cost of this delay is £810,000.

8.3 Consequences of the settlement

The financial model which supported the December decision contained a provision for a "divorce" settlement with NIS and assumed that the full service received from NIS would be moved away from NIS during the first half of calendar 2006. NIS agreed to a full mediation with the Council. The negotiating stance of the Council was agreed with leading members and the settlement was agreed with the then Leader. The NIS stance was influenced by the wake of the Buncefield fire, and, potentially, by a perception that the Council's position was not water tight as it had already publicly wavered once in its decision.

The Council was seeking a full exit from the current arrangement and was prepared to make a payment (in lieu of damages and in recognition of the benefit to the Council in actual and opportunity costs of not submitting to formal litigation) to facilitate this. The details of the settlement are subject to a confidentiality agreement and are therefore exempt under Schedule 12A paragraph 3. The report detailing the settlement will be made available to members on request. The package is, however, £440,000 in excess of the provision.

Members will also note that the settlement has fully utilised the contingency built into the December forecast. Projects of this nature require a contingency to assist in the management and containment of the risks associated with the projections. It is recommended that a new contingency is created at a value of £500k in relation to the further ongoing risks and issues set out later in the report.

8.4 Incumbent supplier

The December projections were made on the basis of certain assumptions about timescales and approaches of both parties, some of which proved to be wrong. These are set out in the following table:

	£'000
25% charge on staff costs to 13 May	60
Further delay	230
More staff to be transferred in than anticipated	110
Legal fees understated	70
Legacy hardware requiring replacement	200
Non availability of transferred staff to backfill	300
Total	**970**

8.5 Other changes

Finally there are two other changes, totalling £170,000, which have been taken into account in the revised projections. These are additional administrative costs in complying with the new arrangements agreed for major projects by the Executive (£70k) and additional provision for replacement helpdesk software (£100k).

8.6 Summary

The additional costs described in this section are summarised in the following table:

	£'000
(a) Reopening negotiations	810
(b) Consequences of settlement	
Direct net cost	440
Reinstate contingency	500
(c) Incumbent supplier	970
(d) Other	170
Total	**2,890**

This shortfall is over a number of financial years, as set out in the following table:

	£'000
Incurred in 2005/06	452
Less underspend on Refresh project	(193)
	259
Costs to be incurred in 2006/07	2,331
Costs to be incurred in later years	287
Total	**2,890**

Members will wish to note that the projections have been heavily scrutinised. The only realistic way to reduce the cost projections would be to accelerate the recruitment of permanent staff, hence reducing the additional cost burden of using contractors. This would require us to balance the financial benefit of early recruitment against the risk that there will be avoidable payouts to employees as a result of the restructuring. The current plan is already aggressive and it would be imprudent to make it more so.

In the meantime, the budget will be actively managed to try and reduce the exposure. There are two substantial areas:

- Actively managing the staffing levels in response to the demand from the business. We currently have backlogs of activity for fault resolution and change requests (both small and large). The ultimate staffing levels are predicated on improving our servicing and processes and, therefore, having fewer staff in the permanent structure than our current interim establishment. We will seek to accelerate these improvements to allow an earlier release of staff; and

- We have taken a prudent view on what level of activity can legitimately be charged to the business. We will seek recharging possibilities, where this makes sense.

9. On-going risks and issues

9.1 As members are aware, the Council has never run all of its IT operations in house. The December report attempted to not underestimate the challenges that the insourcing exercise would present but there are good opportunities for us to grasp, in terms of improved service delivery and developing a fit for purpose team, set up to deliver best practice services. The project has six objectives:

- To grasp the opportunity of the expansion of in-house services and to use the lessons learnt from the previous outsource arrangements to improve the business focus, service delivery and culture within IT Services. This will include adoption of recognised best practice, honest and open inspection of current issues and behaviours and implementation of a revised and revitalised organisation.
- To transition support of the infrastructure delivered by the Tech Refresh from the project team to permanent staff
- To outsource the Networks and Security element to a new managed service provider and to purchase 3rd party software tools as required by the service management design via a competitive tender in accordance with public sector procurement rules and best practice.
- To design an organisational structure and processes based where applicable on ITIL (Information Technology Infrastructure Library – the leading IT service delivery standard) recommendations to deliver the service.
- To recruit skilled resources to enabled the support and maintenance of the infrastructure.
- To deliver this programme of work in accordance with Haringey's Project Management Framework(PMF) and with adherence to the recommendations of the 2005 Audit commission report and subsequent Haringey PMF enhancements agreed by the Executive on the 21st Feb 2006.

9.2 The project is scheduled to complete by December 2006.

9.3 At a high level, there are four risks:

- the speed with which the service is restructured and the new structure populated:

  One of the primary reasons for the transition cost is that our infrastructure is being supported by temporary staff. One of the aims of the project is to establish a permanent staffing structure and to populate it. Delays in either agreeing the new structure or in recruiting into will require the use of temporary staff for a longer period, which will increase cost;

- sustaining service quality in a period of rapid change:

  The insourcing project is managing the new infrastructure and establishing new processes, procedures and practices at the same time. There is a risk that the developmental work will detract from the quality of the on-going service delivery. This will require careful management and balancing of priorities;

- managing and migrating away from a (largely) undocumented legacy environment:

  A number of the Council's applications are still to be migrated to the new infrastructure. This migration was not part of the scope of Refresh and is being delivered, as planned, as part of the transition. These legacy applications were managed by our previous infrastructure provider and are now managed direct. It is increasingly clear that the condition of and documentation about these applications is less good than we had anticipated and managing the transition, whilst maintaining service, will be challenging; and

- demand management:

  There is a constant demand for changes to and improvements to the Council's infrastructure. This activity requires input from IT staff and the level of change to the infrastructure needs to be carefully managed so that stability is maintained and It resourcing is rationally deployed.

9.3 The project is being treated as a major project within the Council's project management framework. Risks are managed by the project team and reported, on an exception basis, to the board. We have established robust challenge arrangements, both internal and external. The project is sponsored by the Head of Legal Services and is part of the Customer Focus stream.

10. Comments of Head of Legal Services

10.1 The agreement with NIS to rescope the contract clearly states that the terms are to remain confidential between the parties and the reasonable endeavours will be used to ensure it remains confidential and is treated as such by Council officials.

10.2 The Head of Legal Services confirms that the revised project management framework is being followed for this project and that arrangements are being out in place for there to be external challenge and review.

11. Comments of Director of Finance

11.1 In the reports to Executive on 20 December 2005 and 18 January 2006 my comments noted the possible financial risks and the inherent uncertainty in cost estimates of this nature. This report provides an update of the position following the decision to bring the service in-house and the financial impact of the consequent negotiations and issues that arose in dealing with Northgate over that period. The costs outlined above amount to £2.39 million and it is recommended that a further contingency is set aside of £0.5 million. I recommend that the contingency sum is held centrally and allocation to the project will be subject to approval of the project stream board chaired by the Head of Legal Services.

11.2 I propose that the funding of this one-off cost is met as follows:

- £1.4 million from the net revenue underspend as set out in the report on the financial outturn for 2005/06 (a concurrent item on this agenda) – this underspend has not been allowed for in our forward financial planning
- £1.5 million from the general reserve – in my budget setting report to the Council in February 2006 target balances are set at £10 million and it is projected that over the financial planning period this will be exceeded by £3 million, therefore there is sufficient flexibility to deal with this without impacting on services.