1. **About Vanguard:** Vanguard helps service organisations change from a 'command-and-control' design to a 'systems' design. The Vanguard Method enables managers to study their organisation as a system and, on the basis of the knowledge gained, re-design their services to improve performance and drive out costs. John Seddon has received numerous academic awards for his innovative contribution to management science.

2. The remit of this inquiry is:

   To examine progress in relation to: the development of shared services and other innovative ways of achieving economies of scale and: harnessing the strengths and skills of key public sector partners to deliver the best possible quality services in local areas.

3. The Scottish Improvement Service tells us that shared services have been cited as a potential route to cost savings and performance improvements for councils, and as such are being explored by many across the UK\(^1\). As an example, the 2009 Arbuthnott review recommended that eight councils in the Clyde Valley area collaborate on a shared services programme.

4. People have been seduced by the concept of economies of scale, they have been led astray by a common bias: as the financial journalist John Kay has noted: ‘Our intuitions about the merits of centralisation and scale are generally wrong\(^2\).

   **Shared Services: a no brainer?**

5. It may seem obvious: if, say, there are six organisations in the same field and each has an HR function, they should share the HR service and cut their costs. The amount of work would of course stay the same, but passing it through one organisation rather than six would require fewer buildings, managers, IT systems, suppliers, and so on.

6. The broader argument amongst the advocates of scale designs is that many services are simply ‘transactions’. The protagonists argue that centralising services will not only lead to lower overheads but also cheaper transactions through lower-cost channels (telephone transactions being ‘cheaper’ than face-to-face, and internet transactions ‘cheaper’ than telephone).

7. These arguments would lead one to believe that sharing services provides ‘no brainer’ opportunities for cutting costs.

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\(^2\) John Kay 18/1/12 ‘A real market economy ensures that greed is good’, Financial Times
8. The culminating piece in the logic is a requirement for an IT system to link the front- and back-offices, enable the channels and allow managers to control the activity of the workforce and manage the processing of work.

Three basic arguments

9. These ideas constitute the three basic arguments for conventional shared services. The first two – which we might sum up respectively as ‘less of a common resource’ and ‘efficiency through lower transaction costs’ – originated in the economics literature. The third – IT as the enabler – is, of course, promoted by IT providers and scale consultancies.

10. The first is palpably obvious: achieving the same output for less of a given resource reduces cost. Many shared services projects are based on these kinds of savings alone. But such savings are not always easy to achieve in practice and, where achieved, are relatively modest.

11. As an example, take IT. It is often claimed that buying one IT system for a shared venture rather than, say six – one for each of the participants – represents a ‘saving’, yet money was spent. You often learn that IT systems are not, actually, needed. Moreover, the features of IT systems typically procured by local authorities and housing services actually serve to increase the costs and worsen the quality of service; in spite of being regarded by regulators as ‘best practice’ (see, as an example, housing repairs, later).

12. Even shared service protagonists concede that less-of-a-common-resource savings are marginal. The business cases for large-scale IT-dominated shared services ventures make much higher claims for the second strand – improved efficiency through lower transaction costs. As well as lowered overheads (higher volumes of work achieved by the same infrastructure) and cheaper channels, they promise efficiency gains through staff specialisation and work standardisation – ‘front offices’ to handle telephone calls and ‘back offices’ to actually process the work. The rallying cry is ‘simplify, standardise and then centralise’, using an IT ‘solution’ as the means.

The evidence suggests otherwise

13. On paper, this all seems to make sense. But how does it square with the evidence? The fact is that we are witnessing a mounting series of embarrassing and costly shared service failures.

14. Some, as in Western Australia, are a write-off from the start; they never get off the ground. Many, like the UK Research Councils, have enormous teething problems, causing headaches for service users, who can’t get the service they want.

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3 Western Australia’s Department of Treasury and Finance Shared Service Centre promised savings of $56 million, but incurred costs of $401 million. See http://www.erawa.com.au/croot/9709/2/20110707%20Inquiry%20into%20the%20Benefits%20and%20CA%20with%20the%20Provision%20of%20SCS%20in%20the%20PS%20-%20Final%20Report.PDF for more details (accessed 13/12/12)
and suppliers, who can't get paid, alike. Most, as with the Department for Transport, run massively over budget. And when managers try to undo the deal, like the Somerset councillors attempting to get out of their South West One shared service centre, they discover that disengagement is prohibitively expensive. Western Australia, just one of many failures down under, had to take the full cost of disengaging, an eye-watering $90m, on top of its failed investment of $401m.

15. Leaders in the public sector are unaware that similar expensive failures have been racked up in the private sector. The reason, of course, is that private sector leaders take care not to parade their dirty washing in public. The private sector was initially sold shared services by the same economists and ‘scale’ consultants who now pepper official propaganda with projected savings from other ventures as grist to the mill – as when Western Australia's projected savings were published in a Scottish Executive report extolling the virtues of sharing services!

**Economy comes from flow, not scale.**

16. Counter-intuitively, economy comes from flow, not scale; it is achieved through managing value, not cost.

17. To take just one example from the private sector: Aviva UK has achieved astonishing results. While one might think Aviva (financial services) is not similar to public sector services, the parallels are many: Aviva was an example of ‘industrialised’ design: call centres, back offices, standardised and specialised work, activity management and IT-dominated work-flow systems – all features being promulgated by successive governments as best practice for public sector organisations.

18. In Aviva, improved and sustained customer service has also resulted in improved efficiency; Aviva’s claims organisations – similar to public sector organisations in that customer demand is of high variety and requires high-quality problem-solving – have not only shown improvements in service and efficiency, but are also now settling claims with less indemnity spend, making the operational efficiencies look minor by comparison.

19. For a review of Vanguard’s work with Aviva see:

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4 A National Audit Office report said that the UK Research Councils project was due to be completed by December 2009 at a cost of £79 million. But, in reality, it was not completed until March 2011, at a cost of £130 million. See [http://www.nao.org.uk/idoc.ashx?docId=23db711b-66fa-47be-9773-686ce60c0218&version=1](http://www.nao.org.uk/idoc.ashx?docId=23db711b-66fa-47be-9773-686ce60c0218&version=1) (accessed 13/12/12)

5 The Department for Transport’s Shared Services, initially forecast to save £57m, is now estimated to cost the taxpayer £170m, a failure in management that the House of Commons Public Accounts Committee described as a display of ‘stupendous incompetence’. The most recent evidence of the higher cost was documented in a House of Commons Transport Select Committee report ([http://www.publications.parliament.uk/pa/cm201011/cmselect/cmtran/549/549.pdf](http://www.publications.parliament.uk/pa/cm201011/cmselect/cmtran/549/549.pdf)) (accessed 13/12/12)


8 See [http://www.scotland.gov.uk/Publications/2006/05/11102023/5](http://www.scotland.gov.uk/Publications/2006/05/11102023/5)
21. The change in Aviva began with the leaders studying their organisation as a system. Studying industrialised designs in any service reveals the design itself is the primary cause of poor-quality and high-cost service. Studying reveals that high-volumes of demand are what we describe as ‘failure demand’ (demand caused by a failure to do something or so something right for the customer, [Seddon 2003])9. The causes are systemic and are associated with the features of industrial designs: the separation of front and back offices, the focus on activity management, the specialisation and standardisation of work—all notions based in a philosophy of managing cost. So while it may be true that transaction costs go down, studying reveals that the total volume of transactions goes up—citizens have to engage in more transactions to get a service—and thus the true costs of service rise.

22. In public sector services it is common to discover that failure demand accounts for as much as 60 to 80% of all demand. The growing number of outsourced shared services deals in the public-sector should be a source of alarm, harbingers of the nightmare coming. These deals are based on transaction volumes. Birmingham City Council, for example, has woken up to the fact that they are paying their private-sector provider hundreds of millions every year to service failure demand10. That’s the good news. But the bad news is Birmingham’s leaders remain unaware of the causes.

23. Studying teaches managers a counterintuitive truth: 95% or more of their organisation’s performance is governed by the system, not its people.

**Demand is the lever**

24. By focusing on a thorough understanding of demand, services can be designed to optimise the response to customers' needs and this leads to dramatic reductions in failure demand, thus releasing capacity.

25. The key is to do the exact opposite of that advocated by the shared service protagonists. Those, in both private and public sectors, that have taken this route, have abandoned 'scale' designs in favour of 'flow' designs: a thorough knowledge of customer demand is used to design a service that meets the variety of demand at the point of transaction. Measures-in-use relate to the purpose of the service from the customers’ point of view and are used by the people who deliver the service to control and improve service provision. It is to manage value, not cost.

**Evidence-base from the public sector**

26. Many examples of public sector success in designing against demand have been published11. These show dramatic improvements in service with equally

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dramatic reductions in cost. To cite just some examples: Improving service has halved the cost of stroke care in Plymouth, released police officers to deal with serious offences in Wolverhampton, saved Rugby Borough Council’s planning service 168k, significantly increased the number of businesses in Great Yarmouth producing safe food, reduced an enormous administrative burden on Staffordshire Fire and Rescue, halved the cost of advice cases in Nottingham, prevented unnecessary, unhelpful and expensive hospital treatment for vulnerable adults in Somerset and reduced the number of missing persons reports, currently costing Cheshire Police £3.8million, by an incredible 75%.

27. The savings to the wider public and the social benefits of these interventions are far greater. These are just highlights, taken from a recently published book of case studies. This is real evidence, but the concern is that it is so much against the grain of opinion and current political narrative that it seems impossible for many minds to comprehend.

28. Managers and employees at these public sector organisations – and others like them – have worked their way to a profound realisation: economy is to be found in the flow of the work rather than through its scale. By learning how to design their services to meet citizen demands they have improved the services while driving out costs. Cost reduction is the consequence of their focus on managing value, in direct contrast to the political narrative which has managing cost as its raison d’être. It is counterintuitive: managing cost drives up costs, while managing value drives costs out of a system.

29. In these designs, where services are local, people-centred and responsive, morale rises and the symptoms of poor morale – sickness and absence – fall. There’s another important and unexpected consequence. When citizens experience good service their behaviour changes. They not only have good things to say about their council (and send employees flowers or cakes instead of brickbats), they begin to behave more responsibly in their own communities. The economic value extends beyond cost-savings. Better services create better communities; the moral economics outweigh even substantial financial benefits.

Opportunities in health and social care

30. Our studies show that there are substantial opportunities to improve health and social care, provided leaders have the freedom to unpick the industrialised designs which have been built into the system by successive governments. The evidence shows that regulation (including targets and obligatory computer systems) and the corollaries of functional design and functional budgets lead to huge sub-optimisation of these services.

31. Our current work in health and social care in England shows that care services for the elderly – accounting for the largest slice of demand into the NHS – can be massively improved by creating one service for users while saving

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12 Pell (2012)
(conservatively) 25% of costs. Furthermore, this and other similar studies have shown that demand for care services is stable. But this is against the grain of the conventional wisdom that demand for care is constantly growing, an opinion based not in fact but epidemiological-based projections. Yet the opinion is grist to the political mill: politicians can talk about ‘rising’ demand forcing us into ‘hard’ choices about services and make hay with spurious ‘consultation’ exercises, where we, the people, get to vote on who we don’t help any more or which services get cut.

**Commissioning: a current fad**

32. All across the UK, government and audit bodies are pushing ‘commissioning’. The ideological view is that competition will deliver efficiency; providers must compete on price and, it follows, a price requires a specification.

33. A citizen has a health or social care need. The need is assessed and, we have to say, eventually, for it can take a very long time, a service is commissioned, then provided. Boxes ticked. What happens next in a shockingly large proportion of cases is the person represents (failure demand). We then go through the same loop: assess, commission, provide ... and the person re-presents, amplifying assessment activity and service provision as much as 9 times, 12 times, even more than 20 times. It can extend an episode; it can become a whole life.

34. Investigation reveals how service provision goes over and under needs: people receive things they don’t need, are given more than they need, or provided with things that are insufficient to meet the need.

35. In services such as drug treatment, social, and health care we see contracts being awarded to providers who are obliged to deliver services as specified. The result is a failure to meet the nominal value of service users. In care services you learn that people who need help with bathing get their thirty minutes, no less, no more; and it may mean a different person on each visit. What ought to be a thermostat in the care system is removed; there is no incentive to re-enable people.

36. Similarly with drug treatment, we see treatment professionals being obliged to follow the ‘treatment’ as specified in their contracts, spending as much as 50% of their time in bureaucratic reporting of compliance while the ‘treatments’ fail to meet the variety of drug users’ needs. With meals-on-wheels contracts we have seen specific instructions not to report on a change in the condition of the meal recipient (‘just do what the contract says’).

37. Behind this lies the cost-management notion that efficiency is gained by reducing unit costs. Once again, while we may see a reduction in the unit costs of services commissioned, we fail to understand how the true costs of service rise. Some of these costs are knowable, the greater unknowable.

38. When managers study care services they realise that their preoccupation with driving down unit costs actually served to drive costs up. It takes time to digest. But

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14 See Seddon 2008 p69. If an organisation does not recognise and respond to what matters to the customer (their ‘nominal value’), then the customer’s experience of the service is poorer and the organisation is forced to consume extra resources to resolve the situation of disaffected customers.
digestion is speeded by unequivocal evidence, hard data illustrating predictable patterns of resources expended while generating human misery. Poor quality service is costly.

How managing value drives costs out

39. Armed as they are with knowledge, managers devote their energy to designing a service that works. Crucial to their endeavour is thorough knowledge of demand – what people need, in their terms – as it becomes the crucible for everything that follows. They build a design that is super-sensitive to people, their needs and their context. The design places the individuals’ wishes at the centre of service provision. People who need help are met by people who have the expertise to help them and the services provided are truly tailored. It is fast, friendly and purposeful.

40. Everyone – citizens, service professionals, providers – is happier, more motivated and more engaged; ingenuity and innovation emerge naturally. And then the big prize is revealed: costs fall out, dramatically. Costs of administration fall by tens of thousands, costs of services provided fall by hundreds of thousands and the costs of failing to meet needs falls by millions. Managers now understand that managing value drives costs out of a system while managing cost only served to drive costs up.

41. Once this Rubicon has been crossed, managers eschew the ideology of cost management – like transaction channels, activity management, service levels, ‘back-offices’ and economy of scale – in favour of acting on the system, ensuring that all the things needed to maintain the new design remain in place: continued knowledge of demand, providing expertise to absorb variety, the speedy pulling of expertise to need, the determination of need in context, fast provision of tailored services, and so on; all aided by measures that relate to purpose from the customers’ point of view.

42. Vanguard’s current work across care/vulnerable/disadvantaged/benefit/housing services shows a profoundly dysfunctional and predictable pattern. The extreme end of the story is: if your life goes off the rails and you pull for help from the state, you will become worse off. It is rational, if not moral, to argue that we (taxpayers) and the people whose life goes off the rails would be better off if we simply discontinued all such services.

43. The alternative, of course, is to design services that work, that help people get back to normal. Leaders that have seen, through studying, how the current system delivers lots of things that fail to meet needs, and so creates enormous unnecessary costs, ignore the missives coming out of government and get on with the opportunity. Our work has shown that the labels (care/vulnerable/disadvantaged/benefit/housing) do not reflect people’s needs and we are helping local authorities and their partners understand how to design services against demand. It energises the people who provide the services, they work in a system designed to help them achieve its purpose and costs drop out as services improve.

Threats and opportunities arising from the Universal Credit reforms
44. The Westminster government plans to reform the social security benefits system through the introduction of the new 'Universal Credit' in order to 'make work pay'. However, ministers have also stipulated policy which dictates how the Universal Credit must be delivered. The government wishes to use the welfare changes to further its intention to make all public services 'digital by default'. Claimants will be pushed towards an online delivery channel and, if that fails to meet their needs, a centralised call centre. As a corollary, the government intends to close down locally-based housing benefits offices.

45. Examination of what actually happens in IT-dominated industrial designs such as the one proposed for Universal Credit reveals massive disruptions to the service flow, for the customer service is anything but smooth. There is huge waste in the shape of handoffs, rework, duplication of effort, and a focus on meeting activity targets and service levels. All of these 'system conditions' lengthen service delivery times and, consequently, create failure demand. In other words, the service gets worse and costs go up. On all counts such industrial 'scale' designs fail miserably.

46. Under government proposals, full implementation of Universal Credit will take seven years and a massive investment in IT (already at an eye-watering £700m). By contrast, if what constitutes the Universal Credit could be defined today, housing benefits offices redesigned along systems principles could provide it quickly and efficiently in a matter of weeks. In fact, to ensure that the Credit is fit for purpose, these offices should be used to develop the rules, taking risk out of the solution. But, as we noted earlier, the DWP's plan is for housing benefits offices to be run down as the UC goes live.

47. However, the opportunity exists to approach the design in a different fashion. The essence of the better design is i) to provide the necessary expertise at the first point of contact to satisfy all of the predictable 'value' demand (a claim or a change of circumstances); ii) to allow agents to 'pull' expertise for the less predictable demand, using measures that relate to the purpose (right money to right people as quickly as possible); and iii) to switch management's focus from managing activity to managing the whole system's achievement of purpose. Using these joined-up principles, benefit offices have subsequently learned another lesson. People's needs and problems come in a variety of interlocking forms and guises; solving them all at first point of contact offers huge potential (if usually invisible) cost savings since it reduces knock-on demand onto other services.

A misplaced faith in IT

48. The architects of the Universal Credit are by no means alone in putting their faith in IT as a way to industrialise service in the hope that this will drive down costs. Alas, computers are not good at handling variety. People are. As managers develop the systems approach, they learn to use computers for the things they are good at and a contrario avoid using computers for things that people are good at. The consequences are fewer computer systems and more control. The value of IT lies in supporting those who deliver service; in scale designs, IT systems dominate and hinder the delivery of good service. Computers have become the cement for command and control management, reflecting the unquestioned assumption that managers should set targets and then create control systems – incentives,
performance appraisals, budget reporting and computers – to keep track of them. On the contrary, to make service organisations work better, it is necessary to take these things out.

49. In their aptly-titled book, ‘Dangerous Enthusiasms’, Gauld and Goldfinch show that up to 30 per cent of major IT projects fail completely, while a further 60 per cent go far over budget and/or fail to meet specifications. The House of Commons Public Accounts Committee (PAC) noted:

50. ‘The lack of IT skills in government and over-reliance on contracting out is a fundamental problem which has been described as a “recipe for rip-offs”. IT procurement has too often resulted in late, over-budget IT systems that are not fit for purpose ... The UK has been described as “a world leader in ineffective IT schemes for government”. There have been a number of high cost IT initiatives which have run late, under-performed or failed over the last 20 years including: the Child Support Agency’s IT system, the IT system that would have underpinned the National ID Card scheme, the Defence Information Infrastructure Programme, the implementation of the Single Payments Scheme by the Rural Payments Agency, and the National Offender Management System (C-Nomis).’ (House of Commons PAC 2011).

51. The Scottish public sector has not been immune from these IT problems. Audit Scotland’s report ‘Managing ICT contracts: An audit of three public sector programmes’ reported on the management of important IT programmes that were delayed, cancelled or overran on costs. The three IT programmes had already cost more than £130m in total at this stage: Registers of Scotland had instigated a programme originally budgeted at £66m, which ballooned to £112m before the contract was terminated; at Disclosure Scotland, a new ICT system intended to protect vulnerable groups of people was expected to be delivered 18 months late; and Crown Office and Procurator Fiscal Service, in which £2.3m was spent before the project was terminated due to increased costs.

52. Ministers assume that these failures can be ascribed to poor project management and specifications. They always say ‘this time it’s going to be better because we are going to employ better project management’ and when the next big failure comes along, they just repeat the mantra. Consider this: What we now know as ‘Prince 2’ was originally developed in the 1970s to solve the problem of large-scale IT programmes. The evidence from the last 30 years suggests Prince 2 doesn’t achieve that.

The Vanguard Method and IT: Understand, improve, pull

53. The Vanguard Method leads organisations to approach IT in a different way: First of all study the ‘what and why’ of current work performance – and in doing so

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17 See http://www.audit-scotland.gov.uk/docs/central/2012/nr_120830_ict_contracts.pdf accessed 10/01/13
use the ideas of ‘value’ – what matters to customers and ‘flow’ – what the organisation does for any particular customer demand. Secondly, using knowledge of customer demand, improve the service design using measures that relate to its purpose; then, when the better design is proven and stable, ask if IT can further improve the flow of work.

54. What happens is that IT applications get ‘pulled’ into the work flow by people who know what they want from them, and only in places where the people can predict how it will lead to improvement. The result is always less spend on IT – something IT companies are not so keen on – and more value from it.

55. One example is in Portsmouth, where one of the City Council’s housing suppliers spurned the usual choice of off-the-shelf IT packages designed for housing repairs (typical cost £250,000) and instead only introduced IT once the whole system had been redesigned. Their new bespoke IT package cost them only £3000 and works by matching the demands of customers (which ones want what jobs at what times) with the supply of tradesmen by highlighting when each is likely to come free from his current job. Large screens at headquarters provide transparency, and the system works as a single piece flow, with each tradesman getting one job at a time to avoid bottlenecks and delays. The contractors have designed their system such that they arrive within 15 minutes of the resident’s specified time for an appointment 94% of the time. The service has recorded a 99% satisfaction rating from residents, with over 90% of jobs being completed right first time.

Regulators and inspectors should cease specifying the measures and methods by which services operate

56. There has been a fundamental error in regulation: the regulator specifying matters of measures and method. This leads to a culture of compliance, exacerbated by the fact that the regulators ideas are, frequently, flawed.

57. To stay with housing repairs and IT for an example, ‘PDAs’ (personal digital assistants – hand-held computers) are considered ‘best practice’ in repairs services. Yet studying reveals how PDAs create massive sub-optimisation and thus PDAs are rejected by all who – like Portsmouth – have studied and redesigned their service to meet tenants’ needs.

58. This problem – top-down specifications driving costs into public-sector services – is ubiquitous and systemic; we published many examples of it in 2008.¹⁸

59. Two further examples: the Food Standards Agency’s requirements were impairing the ability of the system to achieve its purpose of ‘going out and ensuring businesses are producing safe food’¹⁹. In the aforementioned example of prize-winning innovation in Portsmouth, Audit Commission inspectors could not tick their boxes for ‘best practice’ and thus reduced the council’s star rating – in spite of the evidence showing that the service was palpably outstanding, repairs being provided on the day and at the time tenants’ wanted, and costs halved.

60. In short, where regulators specify measures and methods, these become the very things which prevent innovation.

61. While ministers and regulators should have the scope to specify purpose, the practice of mandating method and measures should be removed from all agencies and, instead, made the responsibility of the managers who deliver the service. This change to the locus of control is an essential prerequisite for innovation.

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