

Rising to the New Challenges of Transactional Services in the Public Sector





A Fresh Perspective

Introduction: A Fresh Perspective

The following is an abridged version of Capgemini's recently updated paper on the financial transactional services in the public sector. This is designed to provide you with a summary of the findings and thought leadership, which is included in a full-length paper that you can download from www.capgemini.com.

Our latest paper updates the findings of our 2008 paper¹, in which we have explored and compared the general trends of transactions in the public and private sectors to see what lessons might be learnt.

The updated version brings in a fresh point

of view on the most recent trends and what can be learned from the comparable challenges that exist between the financial services industry and the public sector. For example, the financial services industry has the challenge of multi-channel customer interaction and shareholders seeking efficiency. In the public sector there is pressure from the public and the politicians to cut on the budgets and spending while improving the customer interaction and experience. Both sectors have industrialized processes with transactions that are replicated for billions of events, with a similar need to reduce the cost of these processes.

So why the need to refresh our thinking? Much has changed since we published our paper in 2008. Due to the financial crisis, governments in the developed countries now need to balance the cost cutting with maintaining or even improving service levels. Developing countries face the growing challenge of having to deploy new, complex and scalable transactional service capacity for their citizens.

Companies and government agencies alike have continued to move their activities online. The rising curve of the online service delivery adoption has raised the expectations of the service levels. Yet many transactions in

¹Rising to the challenge of Financial Transactional Services in the Public Sector, Capgemini, 2008

the public sector are often still provided by systems that were not intended, designed and built to support the exponential user and data growth. Subsequently, the rise of online service delivery not only requires new investment but also adds new risks in making these legacy systems secure for an online world with its increasing levels of cyber crime.

Both the private and the public sectors are still under pressure to reduce the costs associated with the delivery of the transactional services. But since 2008 three other significant trends have emerged, these include:

- The increased urgency to reduce fraud and non-compliance;
- The changing nature of Business Process Outsourcing (BPO) and Shared

Services strategies moving away from pure cost reduction to transformational outsourcing; and

- The rapid rise of Cloud technology, with dramatic changes to delivery models.



Setting the Context

Setting the Context: twice as good, in half the time, for half as much

Public sector organizations today are faced with changing customer expectations and new technologies at a time of political and economic strain. The rapid growth in the internet usage and social media proves that the customer requirements, which includes the exchange of information, accessibility of the government services, data re-usage and so forth are fundamentally different than what was a decade ago. Public sector agencies are transforming themselves in an attempt to keep up with the expectations of the modern citizens around rapid, customized and secure online transactions with the government.

Yet this transformation needs to take place at

a time when revenue streams that are open to governments have become tighter. The fiscal situation of almost all the advanced economies has deteriorated and economic downturns are now limiting on how much the tax burden can be increased. So, the taxpaying public is shrinking as populations are aging worldwide. This has resulted in the multiple challenge of delivering services better, faster and cheaper.

Efficiency & Effectiveness

The public sector has to look at how it can take out cost and drive in efficiencies. For example, staffing typically takes up a high percentage of the costs for running

government services and there is an opportunity to take advantage of this by:

- Re-examining the current business processes that support transactions, for instance the back office functions;
- Looking at how embracing new technologies, can reduce the costs per transaction and improve the customer experience;
- Looking at how standardizing and sharing of the business processes and IT can create economies of scale with other government agencies; and

- Looking at the option of outsourcing certain routine tasks so that efforts can be redirected to more specialized, effective tasks.

Higher value through specialization

Given the pressures that governments are faced with, it is possible to foresee a fundamental change to the way government services are structured. In essence it will be a move from government agencies 'doing everything' to a new role consisting of 'being focused, efficient and better'. Specialization allows for a level of investment in creating high quality services for users that is difficult to achieve when governments need to operate multiple smaller services.

A similar role change can be observed within the private sector. Many banks have found that the efficiency of the traditional

integrated 'produce-to-deliver' or 'doing everything' payments model is no longer optimal. Traditionally, banks handle everything, from developing propositions to producing payments, managing client relationships, and offering a whole series of other services to their clients. Through a number of procedures (regulation, liberalization, commoditization and technological development) banks now adapt their business models by specializing, outsourcing or sharing certain services.²

Global sourcing has also allowed insurers to lower administration cost-per-policy compared to insurers with in-house operations. By outsourcing back office functions such as policy administration, insurers are able to focus more on their core competencies of sales and marketing, underwriting and asset management.³



² World Payments Report 2011, Capgemini, 2011

³ Global Trends in Life Insurance: Policy Administration, Capgemini, 2011



Public Sector Transactions

Public Sector Transactions

Pooling and Sourcing of Services

In the UK, the Netherlands and soon the US the tax agency is now the provider of social security benefits, tax credits and other payments. In Denmark the tax agency is responsible for the vehicle registration and related road taxes, while France is currently preparing a vehicle tax to be collected by the Ministry of Ecology. The UK has recently announced the merger of around 50 separate social benefits into one Universal Credit system, while also merging the operation of income tax and National Insurance Contributions.

All these examples show that traditional transactional services, administered and processed by separate government entities, are increasingly being pooled and blended together. Importantly, technological developments (such as Cloud) now allow a fundamental acceleration in the delivery of joined-up transactional services.

Types of Transactional Services

Looking across the public sector we have found that there are significant overlaps in the back office functions responsible for transactional processes. There is commonality among the transactional

services operated in some of the key delivery units of the government and it is clear that there is a great potential for sharing and aggregation of services. This would naturally result in cost efficiencies and economies of scale.

Those financial transactions that make the best targets for improvement are areas such as invoicing and, tax and benefit payment, both of which are highly repetitive and occur frequently. The transactional services that qualify for industrialized pan-government solutions (when looking at cost efficiencies) are those that are repetitive and undertaken by multiple agencies.

The scale of the transactional processes operated by advanced industrialized nations is enormous and growing rapidly in developing countries. At this level, any imperfections in individual processes are amplified by numerous factors. When multiple agencies replicate financial transactional departments, there are vast opportunities to be more cost efficient and effective. And when government agencies do not effectively share information, it will be inevitable that citizens will have to submit their personal information over and over again when transitioning with their government.

Moving towards Standardization

Government transactional services have more in common across countries than is thought. In many countries governmental

agencies involved with transactions have already taken the business approach of standardizing and merging their underlying processes. And it is not only financial transaction processes that are merging in the public sector. For example, France has successfully created core business data for its citizens and businesses, leading to a single and universal data view of the taxpayer. The single view has allowed the tax agency to be a data hub for the citizens, businesses and other government agencies.

Standardization and merging of transactional processes can also be observed in the financial sector, the reasons include improving efficiency, reducing costs and streamlining the more automated elements of the payments value chain. Standardization is fueled by banks that are (sometimes jointly) seeking to boost transaction volumes and scale to expand

existing businesses, generate additional revenues, and/or facilitate new business models.⁴

Breaking down transactional services into their basic building blocks shows that they are standardized and common in organizational and process terms and that their lowest common denominator is information and its processing. An information-centric approach to optimizing an organization's people, processes and technology is the only way to guarantee that structures and processes will be able to drive the performance and efficiency improvements in both the financial industry and the public sector.

⁴World Payments Report 2011, Capgemini, 2011



Leveraging Private Sector Experience

Leveraging Private Sector Experience

Apart from generic observations, we can see that both the private and public sectors are reacting to the three trends we have described in our introduction. These include, the BPO/Shared Services, the Fraud and Yield Management and Cloud Computing, which are rapidly affecting the way transactional services are delivered.

BPO and Shared Services

The pooling of business functions into silos for greater standardization, automation and control is an ongoing trend in the private transactional service sector. The rule of thumb has been that, if tasks can be documented to an 80/20 level

or higher, if they are repetitive, and if they can be learned in no more than six weeks given a certain skill level, then they can be outsourced. Private sector experiences have shown that sourcing can be applied to transactional activities, but far less to high value-adding activities such as decision making, strategy or policy. Private sector experience has also shown that transactional activities account for 80% of the headcount.

It is not a surprise that banks have particularly looked at how they can take out cost in their operations. The focus has been on the repetitive, highly manual processes that can be automated to lower overheads

and protect profits. Banks are also looking at other aspects of their financial transactional processes, including risk management, asset management and securities. In this environment, going forward it is imperative for the payment providers to distinguish their propositions and demonstrate their value through increased specialization.

So the response to the changes in the payment landscape has been to reassess how services-back, middle and front office-are structured. But the underlying trend has been towards BPO, Shared Services and specialization.

If government transactional agencies apply

a similar approach of BPO, Shared Services and subsequent specialization this would imply that:

- Core policy, regulation, assessment and fraud management functions will remain the core responsibility of government agencies that provide transactional services,

but

- Citizen-based functions - registry, transaction and all accompanying citizen contacts and interactions, can be commissioned 'as-a-service.' This could mean sharing services with other parts of the government (registry services) and/or joining forces with the third-party providers to handle (bulk) transactions. This will free up civil servants to focus and specialize on core functions where they can add the highest value.

Fraud and Yield Management

Transactions in the private financial sector closely resemble paying benefits and credits in the public sector. For example, as is the case in the insurance sector, the processes of registry, assessment and transaction are beset with a growing challenge of fraudulent claims. The public sector is under political pressure to protect or even increase the tax yield and to cut (benefit) on spending. So for the public sector, it is worth taking a close look at how the banks and insurers tackle the similar issues of Fraud and Yield Management.

As the adoption of non-cash payment instruments grows, so does the potential for fraud in the financial sector. The payments industry is pursuing various technological innovations to tackle fraud and ensure more secure non-cash transactions-and thereby

bolster consumer confidence. The adoption of new chip technology on payment cards (EMV chips) has already proven to be effective with a massive drop in fraud cases. Attention is focused most, however, on e-commerce transactions, especially as electronic thefts are increasingly hitting the headlines.⁵

The current challenges related to fraud detection have driven increased implementation of advanced technologies in the life insurance industry. New investigation solutions based on risk scoring and predictive analytics allow more granular analysis of data to identify fraud patterns and thus allow for early fraud detection. The scoring models use a combination of rules-based engines, data mining, database searches, predictive modeling, and network link analysis (including social media) to identify the possibility of fraud in an insurance claim.

⁵World Payments Report 2011, Capgemini, 2011

Enterprise-wide data warehouse systems that capture historical information from the fraud cases and integrate information from the third-party sources have made the fraud detection processes more powerful.⁶ Better fraud detection processes (Early Fraud Detection) leads not only to lower claims expenses, it also increases customer satisfaction.

Public sector agencies involved with large transactional volumes also need (near) real-time insight into the possible fraudulent or non-compliant transactions. Like insurers and banks, tax and welfare organizations handle millions of transactions on a daily basis. Fraudulent transactions account for millions of Euros of uncollected tax and unjustly paid out benefits. As an example, the HMRC states the UK tax gap to be around € 40 billion⁷ while social benefit fraud is estimated to be around € 1.4 billion.⁸

In general, the private sector's main focus is on fraud prevention by identifying high risk activities and by refusing the provision of a service or product, or by flagging high risk cases for investigation before a transaction is completed - so called upstream activities. This is in stark contrast to the public sector approach which is mainly focused on detection, investigation and prosecution of fraud that has already been committed - so called downstream activities. In downstream processes, once repayment is made, recovery of payment requires time and cost, mostly for people concerned, and may not result in success, especially in identifying fraud cases. Keeping this in mind, it may be tempting to take the radical approach of 'prevention being better than cure' and limit investments downstream. However, in the public sector this is unlikely to be a successful strategy as many tax frauds (in contrast to many banking,

credit card or insurance frauds) require a combination of upstream and downstream techniques in order to be successful.

Drawing from the experiences in the financial sector, public sector organizations should implement new technological solutions in order to execute their tasks around:

- Monitoring inbound citizen communication to identify fraudulent transactions through rules, heuristic measures and forensics.
- Applying data in conjunction with agile business policies and business rules across:
 - Advanced data validation
 - Predictive models and segmentation

⁶Global Trends in Life Insurance: Claims, Capgemini, 2011

⁷UK tax gap narrows to £35bn, says HMRC, BBC, September 2011

⁸DWP Website, December 2011

- Networks linking data items and customers
- Risk and propensity models.
- Using input from data and advanced analytics to design and execute outbound public campaigns aiming at driving desired customer behaviors.

The likelihood of fraud in those developed countries that are affected by the economic downturn is growing and all the governments desperately need the uncollected tax yields. Sourcing and specialization can free up staff to focus on assessment and fraud management. Private sector experiences show that technological solutions can help staff to compile customer 'black' or 'watch' lists and profile risks 'upstream.' Combining technology

with skilled and focused staff will significantly enhance fraud detection capabilities. It also demonstrates that better fraud detection capability lowers the cost of service delivery and enhances customer satisfaction.

Cloud Computing

Financial institutions are moving cautiously towards the Cloud, with IT spending on Cloud technologies expected to be € 17 billion in 2012. Capgemini's analysis has shown that banks tend to adopt a gradual evolutionary approach to Cloud computing services, evaluating each project based on the type of applications and nature of the data. Lower risk projects that are likely to move first to a Cloud model include customer relationship management and enterprise content management. Higher risk projects will involve

core business functional systems, such as wealth management or core banking.

In the longer term, Capgemini expects the banks to have an application portfolio mix of on-premise and Cloud-based services delivered across a combination of private, hybrid, and public Cloud-based deployment models. Cloud solutions are also becoming enablers for public sector agencies seeking to introduce standardization, cost efficiency and increased service levels.

Typically, payments processing and underlying systems have been designed and implemented in isolation, all with their own separate applications and maintenance. Cloud technology has the potential to reduce the cost of these business processes and the IT that supports them by

disaggregation, consolidation and sharing. Public sector agencies can enhance the transactional and citizen-facing services of the banks by adopting Cloud. Using (private) Cloud technology to transform separate transactional processes into a pan-government function is about:

- Streamlining the current application and process landscape;
- Smooth migration, maintaining reliability and consistency;
- Maintaining service levels within the same underlying process;
- Moving towards virtualization, consolidation and potential outsourcing; and

- Increasing the flexibility of legacy systems and reducing the cost of introducing (legislative) changes.

Cloud technology also has the potential to make transactional services better and more customized by improving communications with the citizens and other public sector agencies. Earlier we discussed how the BPO and Shared Services allowed the public sector agencies to source and handle routine tasks jointly or 'as a Service.' The 'as a Service' concept of Cloud computing means that services, platforms and storage/infrastructure solutions are ordered, accessed and used over the internet, eliminating the need for local implementations, software management and infrastructure.

Significant business benefits include reduced costs as a result of the virtualization of the

services and a reduction in license costs for software because most Cloud software and platform solutions are sourced on a pay-per-use basis. The concept also reduces the amount of infrastructure required because this too can be sourced from the Cloud, which means saving potential on IT maintenance capacity.

Cloud solutions ensure flexibility toward changes in legislation, product portfolio and political demands. The improved reuse of data, harmonization of processes through standardization, and the easier sharing of existing data ensure that fewer mistakes are made. Massive cost reductions are also anticipated on data entry, whilst improving quality.

Summary

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In conclusion, the trend to source and/or share business processes has been ongoing since 2008, although the focus has shifted from pure cost savings to more holistic business outcomes. Connected to this trend is the role shift by financial service providers, moving away from doing everything to more specialist roles. We foresee a similar evolution for the public sector delivery organizations, commissioning common processes and bulk transactions ‘as a Service’ while policy setting and fraud detection remain at the heart of the agency.

The topic of Fraud and Yield Management has become more important than ever, both

in the developed and emerging countries. Since the public sector is facing fraud challenges similar to the private sector, leveraging new technologies to enhance employee fraud detection and yield enhancement capabilities on urgent basis. Finally, the promise of Cloud in terms of enhancing transactional service delivery is enormous. Private sector experience shows that customer relationship management and enterprise content management has the most propensity for Cloud delivery. Public sector organizations have a huge potential to move their citizen interaction and transactional service to the Cloud, using ‘as a Service’ models for facilitating of cost efficiency and specialization.

Although we do not believe that the sectors are fully interchangeable, we do feel that experiences can be transferred for mutual benefit. As a direct consequence of the difficult fiscal situation, now and in the foreseeable future, we believe that many public sector transactional service providers can benefit from private sector experiences. Capgemini has the experience and capabilities to help the public sector agencies in their journey to enhance vital transactional service delivery, and make their services better, faster and cheaper.

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