Consulting Firms: Big Bucks but Little Value for Governments

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Abstract

Governments all across the world, including those in Australia, utilise the service of consultants. Since the 1990s, commercial companies that provide advice and assistance to government and non-government organisations have played an increasing role in the political scene. The global consulting services industry was estimated to be worth between US$700 billion and US$900 billion (A$1.06 trillion to A$1.37 trillion) in 2021-22.[1]

The benefits of organisations using external consultants is that they may need an independent view for consensus building and decision making. Organisations cannot afford to employ, cultivate, and retain the wide range of skills and expertise they might need for specific projects. Also, they may lack the in-house capacity, or have difficulty recruiting the right skills to deliver key projects. Most importantly, in these times of budget restrictions, organisations can achieve results within defined fixed term and cost parameters.

There is no question that the right consultants, with the right expertise in the right contextual situation can bring value to organisations.

However, critics claim that governments and the larger public sector have, frequently to their harm, become unduly dependent on a few big consulting firms, especially when they are appointed in an opaque process without any perceived expertise in the area. They also carry an expensive price tag and are not accountable when the advice they give is a failure in its implementation.

Introduction

in August 2020, the *Australian Federal Health Department* signed a $660,000 contract with *McKinsey Pacific Rim* for recommendations on vaccine policy. For what some might see as an exorbitant fee, the Department was only given *one document* — an eight-page McKinsey assessment of worldwide vaccine development — that was based on publicly available information.[2]

Notwithstanding this debacle, *McKinsey Pacific Rim* was then awarded a $3.8 million contract in 2021 to provide support services for the distribution of vaccines; and a $2.2 million contract to provide guidance on vaccine manufacturing. There were other consultants hired in addition to them. The *Australian Federal Government* announced collaborations with companies like *DHL, Linfox, PwC,* and *Accenture* to provide services and advice on a range of vaccine and distribution concerns in 2020. These companies were supposedly hired to help with the preparation and delivery of COVID-19 vaccines.[3]

The upshot was that the Australian government's pandemic decision-making — ranging from which vaccines were secured, to the pace of the vaccination program roll out — became a political focal point, with the role of consultants coming under heavy scrutiny.[4]

Fatal Advice from McKinsey: A Case Study

New York Times journalists Walt Bogdanich and Michael Forsythe (2022) recently published a 'tell-all' investigative book titled '*When McKinsey Comes to Town'* (2022) which is essential reading for all governments and corporates thinking of hiring consultants — especially *McKinsey & Company*.[5]

One case outlined in the book is of relevance to *management accountants*, especially in the area of cost management.

In 1996, *Walt Disney Corporation* hired McKinsey to evaluate the park's operation — as in, cut costs and raise profits. In business, it makes perfect sense to cut costs and raise profits for shareholders. However, cost cutting for short-term gain at the expense of quality is usually bad policy that can come back to bite you. Just ask *Boeing* how cost-cutting resulted in the 737 Max disasters.[6]
Until McKinsey came to Disneyland in Los Angeles, the place had a flawless safety record.
In 1997, McKinsey gave Disney a lengthy report titled: *Transforming Maintenance: Defining the Disney Standard.* McKinsey noticed that the lap bars on roller coasters were inspected daily *"when records show they never fail"* and advised Disney to change its ride maintenance policy to less frequent inspections.[7]

Then ride maintenance technician, Bob Klostreich, 20 years old, was shocked at the time. He said, *"We check them every night, which is why they don't fail"*! Klostreich was let go in 1999 after presenting additional safety concerns to management.

A few months later, in September 2000, four-year-old *Brandon Zucker* was killed by the oncoming car after falling from the *Roger Rabbit ride* at Disneyland. Injuries and fatalities on other rides continued even after that fatality — until the Californian government eventually intervened and compelled Disney to clean up its act in 2003 and reinstate its original maintenance policy.
The cost of McKinsey's ill-fated advice was considerable. Disney was forced to pay millions in damages to injured customers and families of the deceased. McKinsey though, still received payment for its dubious safety and efficiency report and walked away with its pocket full and no apparent remorse.

The Disney disaster is just a foretaste. Bogdanich and Forsyth (2022) forensically analyse a number of other McKinsey business misdeeds. This article will discuss later how McKinsey gave *Purdue Pharmaceuticals* advice on how to increase the production of the fatally addictive OxyContin painkillers — whilst simultaneously accepting millions from the US *Food and Drug Administration (FDA), "to improve the agency's ability to identify drugs harmful to consumers"*.[8]

The 'Con' in Consulting

While the Disney case is that of a large corporation getting flawed (and in that case deadly) advice; there are also many examples from the public sector, where consultant firms were hired for large contracts, despite these firms' lacking expertise in the area.

For instance, the Australian government awarded McKinsey a $6 million contract in 2021 to develop an emissions reduction plan for achieving *net-zero*. The published study received harsh criticism for not providing guidance on how to accomplish that aim by 2050.[9]

Such consulting assignments were illogical, especially because there were public sector organisations that already employed experts in the field. When legitimate research institutions such as universities and scientific institutes like the Australian government-funded *Commonwealth Scientific and Industrial Research Organisation (CSIRO)* are bypassed — despite having the kind of expertise required for the specific project — questions are being raised as to why consulting firms with little to no expertise and experience in the subject matter are awarded the contract in the first place.

The *Australian National Audit Office* estimates that the overall committed value of contracts linked to private consulting firms was $888 million in the fiscal year 2022.[10]
In that fiscal year, five major consulting firms: *Accenture, Deloitte, EY, KPMG,* and *PwC* received $2 billion in contracts from the *Australian Federal Government*. Of these, the *Australian Department of Defence* employed consultants from these five firms in the greatest numbers. Around a third of the Commonwealth's $2 billion in 2021–2022 defence spending was spent on contracts with those five companies, totalling nearly $700 million.[11]

Several analyses and investigations have also brought attention to many issues with regards to the Commonwealth's reliance of consultants — including the high cost of external advisers [12]; the regular cost overruns that go along with it[13]; and the resultant deskilling of the public service.[14]
There have been similar reports of dreadful failures across the globe. It was revealed, for instance, that in 2021 the UK government had spent £516 million ($925 million) on outside contracts for its national *COVID-19 Test-and-Trace system*, including £298 million ($539 million) to *Deloitte*. The system has since been considered a failure.[15]

The Great Con (2023)[16], is a book by London-based economist *Professor Mariana Mazzucato* in which she examines how the consulting industry has harmed our businesses, infantilized our politicians, and distorted our economies. In the book, she poses the following question:
"Why are governments getting fooled? And why are governments continually hiring and outsourcing their own knowledge and activities to the consulting firms? Even after, in many cases, dreadful scams, mistakes and so on?"

Accountability and Rewards

Another problem is that of accountability. Despite most governments' increased reliance on consulting firms, it is clear that these organisations are not held accountable for their performance. Professor Mazzucato refers to this as a *"skewed risk-reward"* dynamic; noting that consulting businesses are not held to the same standards as governments for errors, and are not at risk of losing clients or future business because of any serious errors in the advice given.[17]

"The consulting industry has made a variety of mistakes, but interestingly, they are not subject to the same level of scrutiny as the public service. We're all aware of its mistakes when they occur,"
"If things don't work out, consulting firms may settle and not have to take responsibility for their actions, but this won't stop them from bidding on future contracts."

For example, notwithstanding Deloitte's failure in the UK, *Optus* declared in 2022 that it had hired the consulting company for an impartial security examination in response to its data leak.[18]

Playing Both Sides

Another significant and common issue in the consulting sector is *conflicts of interest*.
According to a 2022 interim report by the *US Congress' Committee on Oversight and Reform*, McKinsey failed to disclose to the US government's medicine regulatory body, the *Food and Drug Administration (FDA)* that it also worked for *Purdue Pharma* causing a conflict-of-interest issue that attracted international attention.[19]

Purdue Pharma, the company that manufactures the prescription painkiller OxyContin, admitted to criminal charges in 2020 for its aggressive and frequently deceptive marketing of the drug, which has been blamed for the North American opioid addiction crisis.

For its work with Purdue from 2011 to 2019, McKinsey reached a settlement of $641 million in 2021. Yet, what infuriated Lawmakers was that McKinsey also provided advice to the FDA over this same 11-year span to improve the agency's ability to identify drugs harmful to consumers.

Another example of a conflict of interest was the case where a former *PriceWaterhouseCoopers (PwC)* partner who was briefed on Australian government’s plans to thwart multinational tax avoidance — shared the confidential details with colleagues. Within weeks of the laws taking effect in 2016, PwC was marketing a tax avoidance scheme to overseas-based clients.[20] Only when the *Australian Tax Office (ATO)* became aware of this scheme being marketed to multiple companies and confronted PwC about this was the scheme scrapped. The ATO said that millions of dollars in annual tax revenue could have been lost if PwC had successfully rolled out a tax-avoidance scheme it designed using confidential government briefings.[21]

The PwC tax leaks scandal have given the *Greens* (a political party) and the *Australian Labor Government* an excuse to scrutinise private consultants’ public sector work once more by establishing an enquiry. The official focus of the enquiry is about unethical behaviour by consultants engaged in lucrative federal government work. The committee is accepting submissions until April 21, 2023, and intends to report by September 26.[22]

The inquiry will be heard by the *Finance and Public Administration Committee*.[23] The last major inquiry into the sector was shut down by the former Australian Federal Government in 2019 without issuing a report.[24]

Returning to McKinsey, another example of a conflict of interest at the firm is that whilst it undertook a *net-zero report* for the Australian government in term of climate change mitigation (which, as discussed earlier, was criticised for its lack of detail) — the same firm was also advising 43 of the world's top-100 most-environmentally-damaging companies at the time when the report was prepared.

Citing the need to protects the identities of its clients, McKinsey has largely avoided scrutiny of its dealings with the oil, gas, and coal industries. However, internal documents examined by *The New York Times*, interviews with four former McKinsey employees, and publicly accessible records like lawsuits, have shed new light on the extraordinary scope of that work. They reported that McKinsey has advised at least 43 of the top 100 corporate polluters in the last five decades, including *BP, Exxon Mobil, Gazprom,* and *Saudi Aramco*, bringing in hundreds of millions of dollars in fees for the company.[25]

Unfortunately, these conflicts of interest are the norm rather than the exception worldwide with regards to private consulting firms advising governments. For instance, in South Africa, the *Treasury Department* contracted with and/or hired *Deloitte* to advise on *Eskom* — one of the few remaining vertically integrated utilities connected to the Southern African Power Pool — on its debt and restructuring issues, whilst Eskom was suing Deloitte for contractual fraud at the same time. Accepting such a consultation was in violation of all corporate governance, risk management, control, and independence rules.

Governments must be made aware of these conflicts of interests, and citizens must be able to ask governments for this information. Government consultancy contracts should include terms that require consultancy firms to be transparent where there is a potential conflict of interest.
In this regard, new legislation was introduced in the US in December 2022 to avoid conflicts of interest with consulting firms.[26]

Focus Inwards: Restoring Expertise in Public Sector

Consulting to Australian state and federal governments is big business. The only way to effectively reduce reliance on this industry is by sharpening the capacity and critical thinking of civil servants.[27]

Professor Mazzucato observes that, often, the reason why governments outsource to these firms was due to a lack of investment in the public sector. She said:[28]

"One [issue] is that because we're not investing within our health systems or education systems or transport systems, we're getting a weaker and weaker state, which then requires others to help it do its work,"

"When you no longer invest within your capacity, you actually end up literally requiring them to do some of the most central functions of government."

Governments are aware of this issue, and many around the world are concentrating on investing in the public sector to prevent an over-reliance on consulting firms. In Australia, the Federal Government is currently looking at methods to reduce its $2 billion yearly consulting expenditure as part of a drive to strengthen the capabilities and skills of the public service[29] in the hope that this will assist the public service regain specialist competence.[30]

Summary

What we have seen in the last 50 years is the disintegration of the capacity inside governmental organisations to even be a decent partner to these other organisations, so these actions alone may not be sufficient to address the crisis of its reliance on consulting businesses.

Investment in government capacity, including knowledge of when to work with a consulting firm, would be a major step. It is necessary to develop internal ability within. It is also important to know who to engage with, which private sector companies to deal with, or even which consulting firms that government organisations have successfully worked with in the past. A *National Register* with full transparency must be developed.

This does not imply that governments should not use consultants. They may be sometimes necessary but would require determining if a consultant was merely "going through the motions" or truly carrying out the duties of the government.

Therefore, before hiring a consulting firm, adequate terms of reference or a proper contract must be drafted. A greater grasp of reviewing and determining when a contract can make the government dependent on a contractor is also necessary. Transparency between a company, its government contracts, and its other clients should also exist.

The ideal is to achieve collaboration across public, private, and third sector organisations. Management accountants are well trained to be facilitators in such a collaboration.

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