THOUGHT LEADERSHIP

RELATIONSHIPS AT THE CORE OF SUCCESSFUL OUTSOURCING CONTRACTS

The past decade has seen an overwhelming number of outsourcing deals resulting in unsatisfied customers. A recent survey comprising customer organizations as respondents has shown that over seventy-eight percent believe that their providers were delivering successfully on their contractual obligations, however well over seventy-four percent of these very customers expressed dissatisfaction with their outsourcing deals. This overwhelming sense of disappointment is reflecting on the inevitability of outsourcing contracts translating into scope reductions or diminished expectations at best, and mid-tenor contract terminations at the worst. The most common complaints customers have is around reduced focus of providers, repetitive breach of service levels, reduced focus on process improvements [as opposed to contractual commitments] et al. It is pertinent to delve into the root causes as to why an engagement based on a “win-win” strategic approach has over time diluted enough for customer organizations to take a rigid and sometimes judgmental stance against provider organizations. Is the root cause in the very nature of services that were contracted for, the price points agreed upon, or something else more integral to sustenance of such complex engagements?

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July 2007
Volume II, Issue 7

Introduction

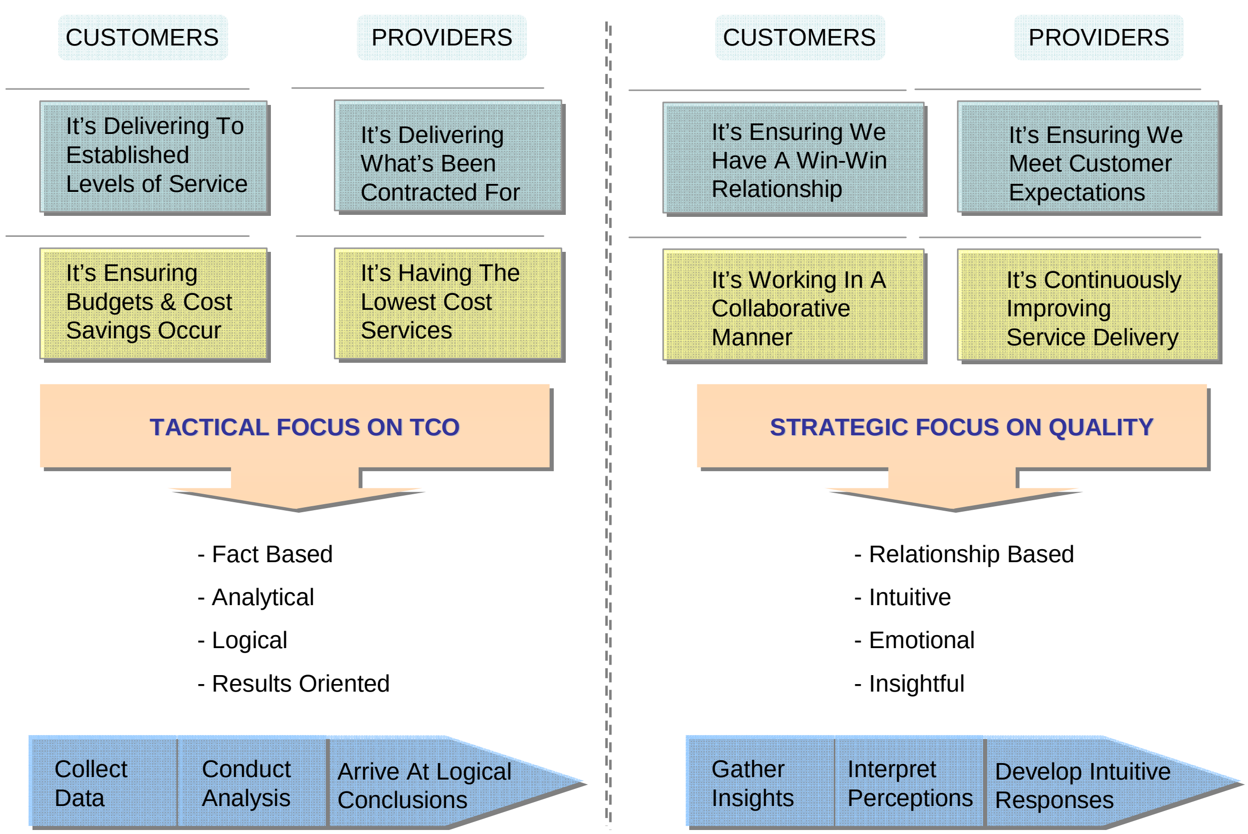
Outsourcing engagements - more often than not driven by competitive bidding processes - are the result of very comprehensive and complex evaluation criteria, wherein customer organizations contract with chosen service providers. This evaluation criteria entails a thorough assessment of provider competencies around business qualifications that are an indicator of relevant experience and reference-ability within the context of services in-scope; evaluation of the solution that has been proposed, both from a perspective of its relevance, and its effectiveness [in helping achieve strategic objectives identified]; IT and physical infrastructure that is being proposed as the core pedestal upon which the services are being positioned; the relevant people competencies [including domain and process expertise] that are available for immediate deployment; corporate and process quality capabilities that can assure adherence to customer expectations; and last but not the least, risk evaluation and management capabilities.

It is quite a common knowledge that such a thorough evaluation leads only to a decision-point wherein customer organizations are able to sit down and commence negotiations with one or two identified service providers. These negotiations (the harbingers of the eventual contract agreement) are as complex and long-drawn out owing to the very nature of expectations, and matching capabilities [especially within the context of a competitive assessment].

One of the natural corollary expectations to such a comprehensive and complex evaluation is that the terms and conditions governing the contract will always be adhered to, and will be sustained throughout the longevity of the contract term. However, most such engagements have failed to create the value propositions expected of the providers. In turn, the providers themselves have expressed concerns surrounding the inability of their customers to keep up the senior management support and related continuity with governance that is necessary to keep the deal's expectations alive. The most common explanation for reduced focus has been attributed to the fact that the services in scope are themselves a commodity, and therefore do not deserve more attention than is barely necessary to keep the service delivery happening.

In essence, the services have been restricted to the definition that they are "a fixed unit of utility delivered at a fixed unit price for a fixed time period". While this statement is in itself not as damaging, the resultant proposition surrounding quality and value takes a significant plunge as the decisions [or lack of them] by management on both sides of the equation results in reducing quality and value to the lowest common denominator.

The most pertinent aspect required to be understood is how customer organizations and service providers approach a deal, how the essence of the deal needs to be agreed and implemented, how the relationship [behavioral] patterns need to be understood, and how to identify proactively root causes of issues before they begin to fester and cause larger issues that may result in pre-tenor contract terminations. Foremost is to evaluate reasons for failure.



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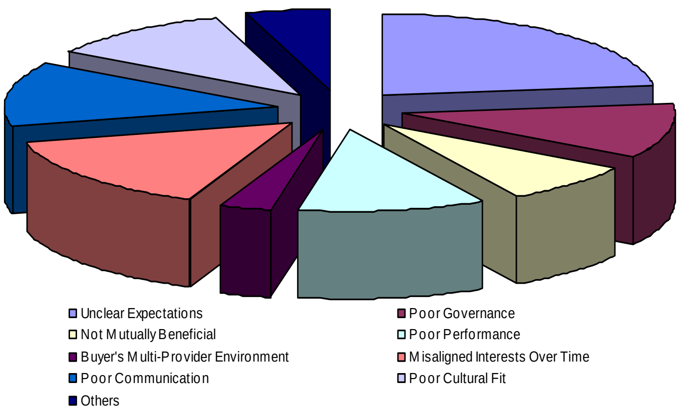
LEVERAGING KNOWLEDGE, CREATING VALUE

Failure Reasons

The relationships fail as a result of non-value generating engagements, driven by a rigid approach towards thinking that lies at the crux of the engagement itself. This failure manifests itself into a number of issues.



Constituents of Quality & Value

This evaluation begins with a thorough understanding of the specific constituents of quality and value propositions that customers expect, and which service providers are expected to commit to. The most important facet is in the ability of both customers and providers to realize that relationships are the cost drivers to sustenance of quality and value. The manner in which such relationships are established lies in the thinking of organizations.

There are two distinct thinking approaches that customers and providers engage in - **Tactical Thinking**, driven by a perspective on reducing the Total Cost of Ownership (TCO) or Strategic Thinking, driven by an approach to ensure end-customer satisfaction.

Tactical Thinking

- This approach often has its roots dug deep into addressing one principal factor - total cost of outsourcing (TCO). Most customers approach their outsourcing engagements with the prime objective of reducing their operational budgets and commence funneling back the savings they achieve over time back into their businesses.

- From this perspective, providers are expected to deliver to established levels of services (and not necessarily required to suggest improvements, or even reduce or remove current constricting factors associated with those services).

- This approach is seemingly logical, but tends to impart a fair amount of rigidity into both contractual and performance evaluations. Quality consciousness is at best measured by the current level of service performance achieved [prior to commencement of the outsourcing engagement]. In turn value propositions [even if they were offered in the first place by the provider] cease to become main-stay evaluation points, as value is not perceived with a rigid set of service level expectations governed by an equally rigid contract.

Strategic Thinking

- On the other hand, customer organizations driven principally by a "win-win" strategy approach their provider relationships quite differently. The mainstay driving factor with this approach is about end-customer satisfaction, and continuous improvement. These are the type of relationships that are often complex, time-consuming to establish in the first place, and equally difficult to manage.

- While the benefits of this approach are fairly measurable, the primary constraint lies in the inability of both customers and providers to quantify the value created over time during the course of the engagement itself. Moreover, expected improvements contracted for are either enhanced, or diluted as a direct result of scope changes.

- The most vital information gathering exercise then is to understand the nature of such scope changes, before embarking on including them into the scope of an existing arrangement.

- It is no gainsaying that each new scope inclusion has to necessarily follow a complete evaluation of provider competencies through deployment of the same evaluation model that was deployed to identify and contract with the provider in the first place.

- However, without necessary risk and return evaluations conducted by both customer and provider organizations, such scope inclusions are at best viewed by the providers as another opportunity to either increase their base price, or enhance current economies of scale, or both.

- On the other hand, customers could [and more often than not do] view such inclusions as business-as-usual, and therefore not worthy of particular attention [resulting in becoming another task for the Program Manager].

Therefore it is a foregone conclusion that either of these two approaches individually is not effective enough to create value. What is necessary is for customer organizations and providers to approach the entire structuring effort of a deal holistically. It necessarily follows that both the tactical and strategic have to be enmeshed into the entire thinking itself, if any value is to be created and sustained.

Guidelines To Effective Relationships

The most important guideline is for customer organizations and providers to approach the entire process of working together holistically, but adopting a proven, flexible and comprehensive sourcing strategy that incorporates both the strategic and tactical objectives clearly and measurably. The other most important guidelines to follow are furnished under.

Mutually Agreed Governance Model & Change Management: Instead of just adopting a model recommended by the provider (which more often than not is a replicable model that is deployed with most customers), it would be wise to develop one together, where accountabilities and responsibilities are clearly defined. Penalties and reward systems (beyond contractual) are agreed with so as to ensure there is enough breath left in the system once the engagement goes into a "business-as-usual" state.

Change management Is Key: Change Management becomes a key component of the governance model and plays well to ensure flexibility and adaptability remains at the core of the relationship. Both organizations have much to learn from each other, which often require incorporating a change into the existing nature of management. From a customer organization's perspective, an additional compounding factor is to ensure that the "retained organization" is aligned appropriately with the provider and expectations are mapped into the relationship.

Written Documents & Maps Aren't Enough: Most providers do bring to the table significant experience with process mapping, models and frameworks that are backed up by gigabits of data. The essence of such documents if not incorporated into the roles and the contractual obligations is a sure sign of failure, as individuals then assume that operational aspects of such detail.

Changes In Business Circumstances Need To Be Understood: This is a reality check for management across both sides, as changes in leadership or business circumstances do have an impact on decision structures and review mechanisms, including scope inclusions/ decreases that can have a significant impact on performance and existence of the deal itself (in some cases). It is important therefore for managements to proactively take into account such changes and the nature of impacts they can have with existing arrangements.

Flexible Value Propositions Are The Norm: Value expectations change over time, and usually are the principal issue providers have with their customers, resulting in relationship deterioration. Providers usually manifest such deteriorations with reduced management focus, categorization of the customer as non-strategic etc, leading to further corrosive festering of the relationship. It is important for both organizations to realize value requirements and assessments do change, and when this does happen, it is not always necessary to engage in complex re-negotiations that take a long time to bring to fruition. Flexibility with such value demand when imbibed as a part of the deal-making culture saves time, money and the relationship itself.

Remove the "Dust Factor": More often than not, less than 20% of the resources on both sides of a deal are tasked with the role [including other responsibilities] of maintaining relationships with counterparts (which is often driven by the governance structure). This approach leads to teams working in silos and blame-fixing becomes the norm.

Implementing Principles of the Contract: While a Master Services Agreement clearly outlines responsibilities and expectations from a legal and performance standpoint, it is more important to ensure that the daily operational aspects of service delivery and performance are appropriately understood, recorded and agreed upon. Proactive resolution of issues and accountability apportioning represent "honesty keys" to sustaining the relationship. Unresolved issues and renegotiation requests at each stage can only compound the deterioration of a relationship rather than assuage it.

Matryzel Consulting is an independent strategic consulting, services sourcing and advisory firm specializing in practices that have a direct influence on the services globalization industry.

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