

## After the ink is dry: How to Ensure Best Practice in an Outsourcing Relationship

Liz Campbell, Cathy Hyatt – EquaTerra

This paper looks at what is required after the contract has been signed to make sure a sourcing relationship works well and meets business objectives. It highlights three management processes and eight principles of good governance which, if followed, will keep any company on the right track with their outsourcing provider.

A Conference Board study found that 97 percent of respondents that had experienced outsourcing would outsource their operations again - but would pay less attention to service levels and more attention to the contract and contract governance. This shows businesses must be aware of the need to focus on developing professional and highly detailed management capabilities that will help them achieve successful, effective long-term sourcing relationships.

Seeing the ink dry on any just-completed outsourcing deal is a cause for celebration. But now the hard work starts. Now is the time for launching and administering a new service provider relationship on a scale more complex and riskier than anything most companies have ever done before. To ensure the business case and long-term value are realized, the relationship with the provider must be managed well. But how is this done best? How much will it cost? And how many, and what types of resources, are needed to manage the relationship?

It takes money, people, process, and technology to govern and manage an outsourcing relationship. A company should expect to spend from 3 to 10 percent of its annual sourcing spend to manage a given contract. Although that may seem high, it is not. Look at it as a required investment to protect

the outsourcing business case expected to yield from 15 to 40 percent in savings.

Managing an outsourcing portfolio of service providers, or even one relationship, is tough. EquaTerra has grouped all of this work into three segments or processes, which should be implemented in an effective governance operating model:

**Relationship Management** should be focused on driving current and future value by implementing and maintaining high-quality business planning and satisfaction processes. It requires hands-on interpersonal and negotiating skills, supported by well-defined and mutually agreed governance protocols, decision rights, issues management and dispute resolution procedures.

Relationships with suppliers who work with multiple business units should be managed in a coordinated fashion. A formal mechanism should be established to enable joint strategic planning, and a relationship manager should be dedicated to each strategic service provider.

**Service Delivery Management** breaks down into three groupings of sub-processes aimed at ensuring the quality of: provider performance, program management and retained internal services. The quality of service provider performance is focused on monitoring and reporting, breach notification, problem escalation and resolution. Today's technology and operating models enable and require that the company has timely control and access to information regarding performance across the business units, operating locations and suppliers – on a day-to-day and week-by-week basis. It makes little sense to have three or four service providers each delivering performance reports that have to be rolled up into something useful by management, a month after the fact.

With a lot of money at stake with discretionary and non-discretionary projects, a well-run program management office is critical to delivering successful projects and reducing value leakage.

The last area of service delivery management is internal services. This includes everything retained from the outsourced function – those components you want to keep for purposes of strategy, process design, architecture, security, compliance and so forth.

**Contract Management** encompasses two key areas: financial management and contract administration. This work includes billing and payment, consumption forecasting and tracking, financial compliance to the contract, charge-back, benchmarking, internal controls and third-party contract management. These processes are critical yet often overlooked. When they aren't given due attention, the result can be highly damaging value leakage.

With the right management processes in place to govern the outsourcing contract, a company should be on the right track to maintaining a successful relationship with its provider. Most successful outsourcing relationships have good management at their heart. Companies that use the following eight principles of good governance will ensure their management processes work effectively.

## Principles of good governance

### 1. Balanced stakeholder needs

Companies that successfully outsource continuously 'take the pulse' of all stakeholder groups to balance their needs over time. Stakeholder groups include senior executives, IT personnel in both retained and outsourced groups, the service provider, and the 'users' of the services (employees, customers, suppliers and others).

While it may be impossible to please all of these stakeholder groups at the same time because service availability or variety have been deliberately restricted to cut costs, the company's governance group can strive to balance each group's needs over the term of the agreement. When stakeholder groups see that the governance group doesn't place one group or one set of requirements above others all the time, their participation and satisfaction increase.

### 2. Pursue stakeholder involvement

Formal governance boards and steering committees are essential, but informal stakeholder involvement is the way successful relationships are built and maintained over time. Stakeholder involvement results from an effective combination of information exchange and action. For example, a governance group can set up ad-hoc advisory teams, actively pursue the opinions and participation of key business leaders, and offer informal educational presentations such as 'lunch and learn' seminars that stimulate the exchange of information. Superior governance requires regular interaction, information exchange and meaningful action.

### 3. Seek cultural synergy

One criterion often used when selecting an outsourcer is cultural synergy. Governance groups can achieve improved results by identifying and building on strengths both cultures share. For example, if both cultures are process-oriented, shared process development can be an effective way to work together. Interestingly, improved results can also be obtained by avoiding shared cultural weaknesses; once identified, the governance group and service provider can work together to find ways to steer clear of these traps.

### 4. Drive out false agreement

False agreement occurs when someone agrees to do something without any intention of actually doing it. Although not unique to outsourcing relationships, this can be particularly damaging to them. Since the governance group operates predominantly through influence rather than authority, its members must be able to rely on commitments made by others, whether internal employees or service provider staff.

Driving out false agreement requires diligence – documenting agreements, consistently following up on commitments and holding others accountable. By asking others only for what they really need and following up diligently on all commitments, the governance group will build the trust and credibility needed to deliver results.

### 5. Remember, the 'customer' is not always right

Governance group members must keep their minds open and reach across organizational boundaries to understand the motivations of all stakeholders. Communication is an imprecise science, and misinterpretation increases when people attempt to bridge the language and experience gaps across functions and cultures. By taking special care to develop a deep understanding of stakeholders' motivations and expectations, governance group members can negotiate more creative and mutually beneficial solutions.

### 6. Experience matters

When governance group members are drawn exclusively from the client company, they begin with an experience deficit that puts them at a real disadvantage. Moving from management to governance with little or no training on the critical differences between the two can lead to costly mistakes that can contribute to the failure of the outsourcing relationship. However, it is possible for governance groups to rapidly fill their experience deficit through the use of coaching and other outside support.

Although service providers can and do help in this area, their perspective isn't fully aligned with the client company's perspective. The best source for this support is an independent third party with real hands-on experience in company-side governance. By making this investment, governance groups can shorten the learning curve, avoid costly mistakes and more quickly become effective partners.

### 7. Avoid the paradox of alignment

Alignment between the company's goals and the service provider's actions has long been considered the Holy Grail of outsourcing. Yet alignment remains elusive – companies want to cut costs and increase service quality, while service providers want to increase revenue and decrease service delivery costs.

While these objectives are not necessarily opposed, they tend to prevent effective alignment unless both parties actively seek out those areas where both sets of objectives can be met. Companies that expect the service provider to adopt and align with their objectives at the expense of their own will be disappointed; and continued disappointment leads to distrust, which can seriously damage the relationship. Better to seek true alignment around mutually beneficial outcomes than to gain false agreement to one-sided goals.

### 8. Service level agreements are not enough

Service level agreements (SLAs) are extremely important and should be continuously refined and improved over the life of the agreement. However, they must be augmented by other methods to ensure customer satisfaction. For example, the principles of balancing stakeholder needs and pursuing stakeholder involvement can be used to monitor and improve customer satisfaction and relationships among stakeholders.

Ultimately, customer satisfaction depends on the relationship between the governance group and the service provider – when trust is high and commitment to achieving the agreement's goals is shared, customer satisfaction becomes a key success ingredient that's jointly nurtured by both sides.

In the end, excellent outsourcing governance requires many components: leadership, tools, processes, personnel, skills and principles. Operating from shared principles can create the basis for the high-trust relationship required to deliver the complex results expected from today's outsourcing agreements, and therefore, avoid value leakage throughout the supply process.

### About EquaTerra

EquaTerra sourcing advisors help clients achieve sustainable value in their business processes. With an average of more than 20 years of industry experience in over 600 global transformation and outsourcing projects, our advisors offer unmatched industry expertise. EquaTerra has deep functional knowledge in Finance and Accounting, HR, IT, Procurement and other critical business processes with advisors throughout North America, Europe and Asia Pacific. Our people are passionate about providing objective, conflict-free advice to our clients, which has fueled our exponential growth over the past three years. We help clients achieve significant cost savings and process improvement with outsourcing, internal transformation and shared services solutions. It is all we do.

For more information, please contact us at  
1 713 669 9292 (US) or 44 207 100 7766 (Europe)