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The Top 10 Problems With Outsourcing Implementations (And How to Overcome Them)

Using Industry-Leading Change Management and Governance Practices to Achieve Outsourcing Success

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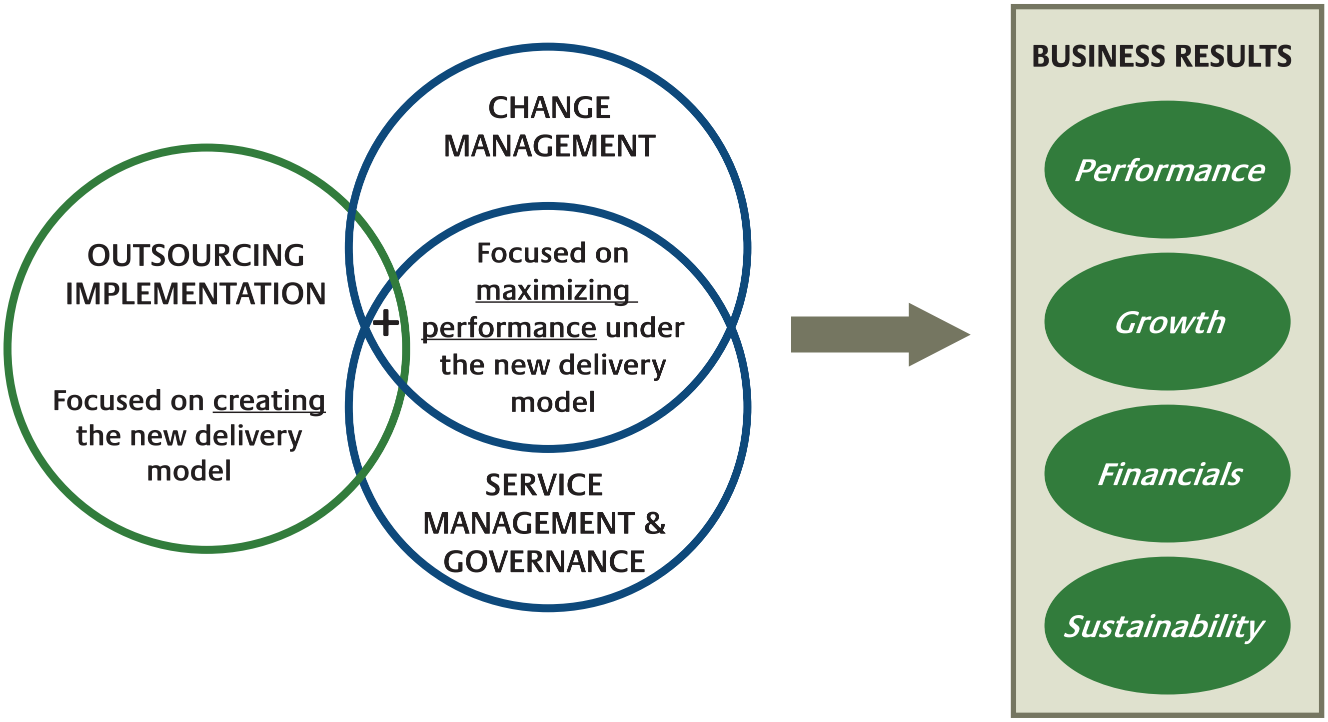
INTRODUCTION

You can choose blue-chip service providers and sign innovative, iron-clad, risk-sharing contracts — but still not achieve successful results if you underestimate the importance of Change Management and governance in outsourcing.

In multiple interviews with outsourcing providers and buyers of outsourced services (clients), we learned that poor Change Management and governance are the most systemic — and far reaching — of all the myriad mistakes that can occur. Experience tells us that some managers and project leaders tend to excel at domain knowledge, vendor and portfolio management, rather than Change Management itself.

Why are Change Management and governance critical business issues? Outsourcing agreements can fail to achieve intended benefits, not because the goals were ill-conceived but because of poor planning and execution, even cultural intransigence. The benefits of outsourcing come through the successful introduction and sustainment of change — a continuous commitment rather than a one-time event.

However, making change happen successfully is one of the more difficult aspects of organizational leadership and corporate management. For this reason, we are highlighting the commonly encountered problems that impede successful outsourcing implementations and, in particular, undermine changes required to achieve expected results.



TOP 10 PROBLEMS WITH OUTSOURCING IMPLEMENTATIONS

As part of our commitment to improve the outsourcing industry through our Innovation Agenda, TPI set out to identify common client problems in outsourcing implementations. Our goal was to identify these problems and then "work backward" to identify actions that could prevent or mitigate these problems.

TPI conducted multiple interviews with outsourcing clients and service providers to identify key problem areas, and also utilized the knowledge base of our 350+ advisors who have extensive outsourcing experience — either as clients, service providers and/or advisors.

We defined "outsourcing implementation" to be the first 6-18 months that a change occurs in an outsourcing relationship. This change could be an initial outsourcing contract, a significant change within an existing outsourcing relationship (involving scope, technology and/or business process change), or a switch from one service provider to another (or potentially multiple service providers).

The outsourcing implementation is when "the rubber meets the road." It is the critical juncture in the outsourcing relationship where:

- Required planning should already be defined in order to initiate the change (including all contract negotiations and implementation preparations by the client and service provider[s]).
- The future groundwork is laid for the enterprise-wide relationship between the client and service provider (i.e, work moves out of the planning stage and begins to impact multiple client leaders, users and other stakeholders).

The final result of our efforts is a "Top 10" list of client problems with outsourcing implementations. There was wide agreement among clients and service providers alike regarding key issues — we ranked the problems based on the prevalence of responses we received and the impact/downstream implications of the problem.

Problem #1: Post-Contract Processes and Decision Rights Not Understood

Based on TPI's interviews and analysis, the #1 problem in outsourcing implementations is a lack of understanding of post-contract processes and decision rights. Simply put, clients and service providers are not operationally prepared to work together after contract signing.

The results are that services simply aren't performed, implementation activities get stalled, client stakeholders and service provider staff are both frustrated, and the entire schedule for achieving expected business benefits is delayed.

Having processes and decision rights rated as the biggest problem may seem surprising given the possibility for high emotion and behavioral change that comes with outsourcing. However, in TPI's view it is this lack of definition and understanding that is a significant root cause of many other issues.

The problem occurs if new processes and decision rights have not been well-designed or socialized. For instance, with the new outsourcing model, who in the client's organization can request services? Does it go directly to the provider, and if so, how? Are new software tools/systems required? What documentation or justification is required for the service request? Are any new approvals required (either within the client organization or by the service provider)? Does approval depend on the nature of the underlying request and/or financial cost? Who decides? What about "emergency" change requests — are these acted on immediately, and what constitutes an "emergency"?

These and a host of other questions about financial, contractual, and service delivery processes and decision rights must be answered and communicated to appropriate stakeholders in the client and service provider organizations. The outsourcing contract is not intended to be (nor should it be) an operations manual; therefore additional work is required to design and communicate changes.

Problem #2: Little or No Support From Client Leaders Receiving Services

Another significant problem that exists in many outsourcing implementations is the lack of buy-in from senior client leaders who will be recipients of the outsourcing services. This can result in active or passive resistance to the entire outsourcing model; create the desire for "special treatment" or opt-out from the outsourcing services, and results in business case deterioration.

Many times leaders who will receive future services do not actively participate in the outsourcing evaluation or receive proactive communications regarding its status. This lack of participation has two detrimental impacts: 1) the leader receiving services is generally unprepared for the changes to come; and 2) the evaluation and negotiation team may not fully represent or understand unique services for a particular unit in the organization.

Problem #3: Poor Mutual Understanding of the Contract

After signing the initial contract, both the client and service provider have multiple team members who are trying to manage the initial implementation activities and ongoing operations. The client has staff who are just learning the details of the agreement, may be emotionally charged regarding the decision to outsource and also have a personal view of what the service provider should (and should not) perform.

The service provider has team members who are also new to the transaction, and sometimes bring a view of "this is what we did in my last deal" without fully understanding nuances of the specific agreement that has been negotiated.

The significant number of new people combined with a high speed of implementation impairs a requisite absorption period, leading to uninformed views on both sides of "what's in the contract."

Problem #4: Client Retained Team Not in Place or Too Small

With many outsourcing implementations, there is an outright lack of a defined retained/governance team or one that is too small. This causes issues in implementation because there is no one "directing traffic" or the team is too small to handle both the volume and complexity.

Clients tend to put off making decisions about the retained/governance team for multiple reasons, including:

- All energies and efforts are focused on "the deal" in terms of contract terms, conditions, and pricing, with no time/resources devoted to post-contract issues.
- Clients may postpone making staffing decisions and communicating changes until they are sure about the final outcome of the outsourcing agreement.
- Clients expect that since they are outsourcing the work, the service provider will take care of everything and the client can "wash its hands" of ongoing management responsibilities, resulting in a lack of governance staff.

Problem #5: Client Retained Team Lacks Required Skills

Even if a client puts a retained team in place to manage the outsourcing implementation and ongoing operations, the team may not have the right skills required for their new roles.

According to data gathered by TPI's Governance Benchmark database, client-retained organizations often look like this:

- 60 percent of staff assigned to the governance organization have no prior outsourcing experience.
- 40 percent of clients in the benchmark did not provide any initial training for the governance team assigned to manage the agreement.
- Only 20 percent of clients feel like they provide enough ongoing training for their governance team.

Also, in TPI's experience, most clients only consider existing staff within their organization and usually want to keep people with the best technical and/or business process experience. However, these people sometimes have a hard time making the switch between performing or managing the day-to-day work and holding the service provider accountable.

Problem #6: Loss of Key Talent and/or Poor Knowledge Transfer

Outsourcing creates uncertainty for existing employees and contractors who provide services to the client organization. The uncertainty can cause this staff to look elsewhere for employment and leave either before or during the outsourcing implementation, causing a need to either backfill the resource or reduce the amount of work performed by the organization.

In addition, some of the client staff is temporarily engaged for knowledge transfer to the service provider during the implementation. If the staff is not properly motivated or if the service provider does not do a good job with knowledge transfer, this can cause decreased efficiency in service delivery and possibly introduce operational risk.

These two issues can be significant problems if not addressed. However, it is in the middle of our rankings because clients and service providers both recognize the importance of these issues and generally make a reasonable attempt at mitigation.

Problem #7: Inability to Meet Pent-Up Demand for Services

Prior to an outsourcing implementation, the client organization may curtail big projects and non-essential spending. This is for two reasons: 1) the client may wait for the expertise of the service provider before initiating activities; and 2) the client may limit its investments in the area designated for outsourcing.

If the client has limited these activities, there is typically a substantial amount of pent-up demand and/or requirements that need to be met shortly after the implementation period begins. However, the ways in which the new initiatives are prioritized, estimated, evaluated, approved, scheduled and performed may all be in the midst of change during transition to the new outsourcing model. This results in "a pig trying to fit through a garden hose"; only a trickle of demand is fulfilled until the new model is in place.

Problem #8: End-User Resistance to Adopting New Methods

Oftentimes, a third-party service provider is brought in to be a "change agent." The outsourcing sponsor wants to achieve business benefits quickly which require changes in process, technology, behavior and (potentially) staffing.

However, for many outsourcing services, the provider is not in complete control of the end-to-end result. The users on the receiving end of new methods can inhibit the achievement of business objectives through lack of compliance, strategy disagreements or delays in executing their required responsibilities.

Problem #9: Culture Clash Between the Client and Service Provider

TPI sees culture clashes between a client and service provider occurring on two levels: corporate culture and (increasingly in today's global economy) national/regional culture.

In terms of corporate culture, the client and service provider may have different norms in terms of speed, style, decision making and organizational structure.

Another aspect of potential corporate culture clash is the fact that outsourcing represents a commercial relationship between two separate entities. Sometimes both organizations can take extreme, inflexible positions that serve to create tension or distrust (e.g, the client taking a position that "I don't care what the contract says, I'm the customer" and the service provider equally digging in its heels and taking a view that "we are delivering to contract specifications").

In terms of national/regional inhibitors, language and the understanding of subtleties in verbal, non-verbal and written communications can be problematic (especially when work is performed offshore with little contact other than by phone or e-mail). Also, expectations regarding the level of open debate, acknowledgement of potential problems, and willingness to veer from the defined process in order to complete work may vary between regions and nationalities.

Problem #10: Changes Don't Last

Old habits die hard. Even for organizations that initially change behaviors and processes to achieve success with outsourcing, there can be a significant tendency to revert to old ways of doing things. TPI sees clients start to cut back on dialogue with their business stakeholders and service providers, reduce governance staff and reduce process rigor over time.

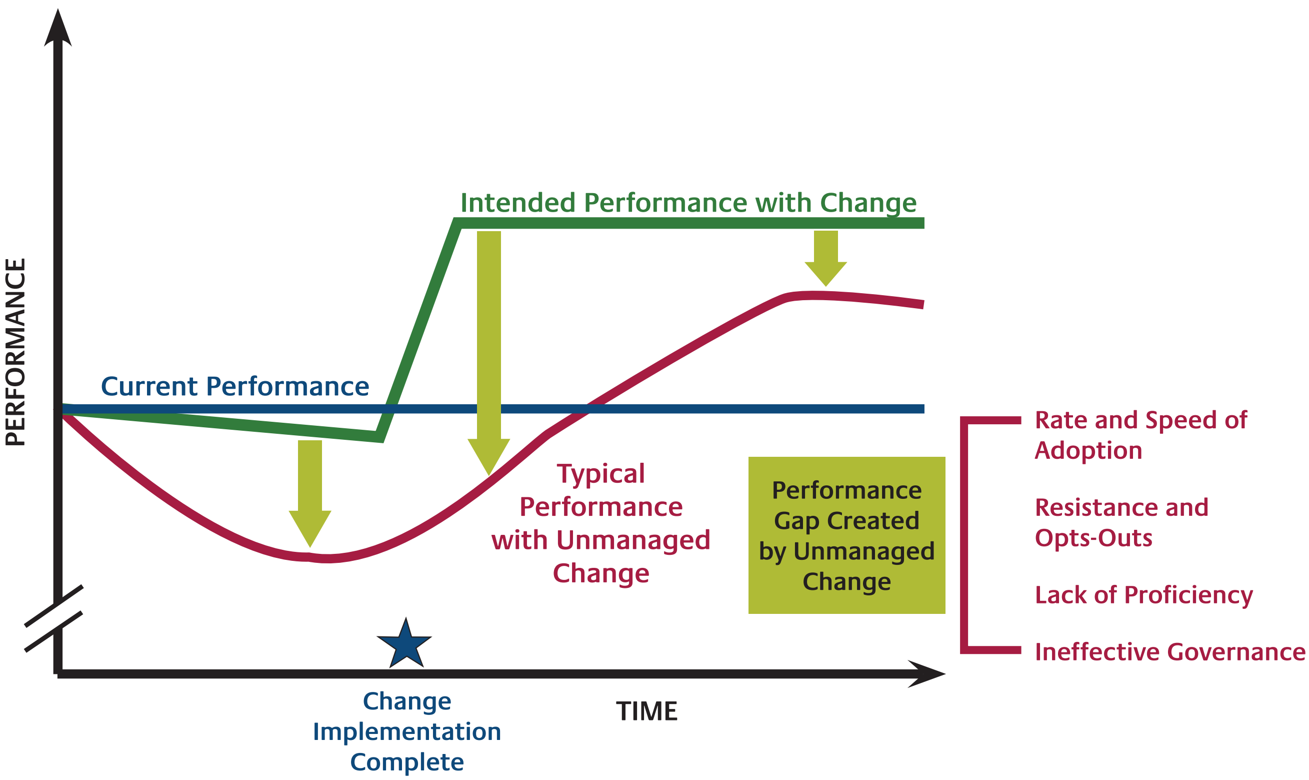
This retrenchment usually occurs because the client believes benefits will continue to occur automatically, and therefore "we can eliminate unnecessary cost." The irony of these decisions is that clients are cutting back on the very things that have made outsourcing successful in the past and are needed to make it successful in the future.

BUSINESS IMPACT FROM THE TOP 10 PROBLEMS

Our findings indicate that unmanaged changes are the biggest problems clients face in outsourcing implementations — not issues related to specific contract terms, pricing or technology. The sum total of these problems causes significant degradation in the expected business case during implementation and beyond. The graphic below illustrates the impact of unmanaged changes in outsourcing implementations.

IMPACT OF UNMANAGED CHANGE

Unmanaged change causes a severe performance gap during the outsourcing implementation and results in expected performance not being reached



OVERCOMING PROBLEMS AND DRIVING SUCCESS: A FRAMEWORK FOR ACTION

While the problems listed above may seem significant at first glance, they can be readily overcome with awareness, attention and focus. In fact, by recognizing these issues in advance, clients and service providers are ahead of the game and can drive early — and lasting — success.

In our work with client organizations and through our liaison activities with service providers, TPI has identified a set of drivers for the entire outsourcing Change Management process. These drivers provide a framework for developing specific actions and techniques, help categorize issues to mitigate problems and enable the realization of intended benefits created by the change implementation.

By themselves, the drivers do not represent groundbreaking innovation — the principles and techniques associated with Change Management are well-known to experienced practitioners.

However, it is the application of the drivers and overall commitment to Change Management by client sponsors that is required to make an actual impact. The lack of sponsorship and commitment is the reason that issues related to Change Management and governance are so prevalent on our Top 10 list.

Change Management may sound like a "nice to have," but — as evidenced by our Top 10 list — it is essential to achieving expected results. To demystify the concept of Change Management, the following drivers provide a framework to lay out a vision, make sure everyone understands their roles and goals, develop a road map to make it happen and then execute.

The drivers include the following thematic elements:

- **Leadership Vision and Commitment**: client and service provider leaders must be clear about the future state and drive the changes required to get there through words, actions and commitment of appropriate resources.
- **Staff Effectiveness**: client and service provider staff responsible for negotiating, implementing, performing and managing outsourcing services must have the necessary skills, knowledge and capacity.
- **Organizational and Procedural Alignment**: client policies, programs and other operating model components are aligned to support and enable the change.
- **Governance Readiness**: the outsourcing governance model is in place with a shared understanding of responsibility, decision-making authority and how services are managed.
- **Change Acceptance and Adoption**: client groups and individual stakeholders who are involved understand, accept and are committed to operate according to the new model.

The following table provides the list of the Top 10 issues and the relative impact each of the five drivers can have to eliminate or mitigate the problems. In addition to the table below, the following section provides specific actions in further detail.

IMPACT OF UNMANAGED CHANGE

Unmanaged change causes a severe performance gap during the outsourcing implementation and results in expected performance not being reached

	DRIVERS AND IMPACT ON MITIGATING PROBLEM				
TOP 10 PROBLEMS	**Leadership Vision & Commitment**	**Staff Effectiveness**	**Organizational & Procedural Alignment**	**Governance Readiness**	**Change Acceptance & Adoption**
1. Post-contract processes and decision rights not understood	●	◕	●	●	●
2. Little or no support from client leaders receiving services	●	◕	◕	◕	●
3. Poor mutual understanding of the contract	●	●	◑	●	◑
4. Client retained team not in place or too small	●	●	◕	●	◑
5. Client retained team lacks required skills	●	●	◕	◕	◑
6. Loss of key talent/poor knowledge transfer	●	●	◕	◑	●
7. Inability to meet pent-up demand for services	●	◕	●	◕	◕
8. End-user resistance to adopting new methods	●	◕	◕	◕	●
9. Culture clash between client and service provider	●	◕	◕	◕	●
10. Changes don't last	●	◕	◕	◕	●

● = High Impact on Mitigating Problem   ○ = Low Impact on Mitigating Problem

SPECIFIC ACTIONS TO MITIGATE THE TOP 10 PROBLEMS AND FACILITATE CHANGE

Actions: Leadership Vision and Commitment

- *Mitigation for Problem #1: Post-Contract Processes and Decision Rights Not Understood*. The client sponsor must be aware of the need to design new processes, and assign necessary resources and importance to these activities.
- *Mitigation for Problem #2: Little or No Support from Client Leaders Receiving Services.* The client sponsor for outsourcing must hold substantial one-on-one discussions with each key leader during the pre-contract stage and during implementation. At the appropriate stage, the service provider executive responsible for delivering the outsourcing services should also meet with the client sponsor and business unit leader. These activities create a dialogue about specific issues and/or concerns for that organizational entity receiving services, and they build mutual understanding.
- *Mitigation for Problem #4: Client Retained Team Not in Place or Too Small.* Even though the client is outsourcing, it does not abdicate responsibility for results. Senior management within the client organization must paint this vision, and commit an appropriate level of management staff to achieve intended results. The contract or service provider — by itself — is not enough.

Actions: Staff Effectiveness

- *Mitigation for Problem #3: Poor Mutual Understanding of the Contract.* To enhance future effectiveness, continuity and mutual understanding, the negotiation team should include executives from both the client and service provider who will be responsible for future delivery.
- *Mitigation for Problem #5: Client Retained Team Lacks Required Skills.* Outsourcing necessitates modification to some roles and creation of new ones in the client organization. Assess internal staff to see if the necessary skills and capabilities exist to fill the roles, and whether they will be able to make the adjustment to a new way of working. Strategic hiring/contracting of external staff that have substantial experience with outsourcing will complement and add depth to the team.
- *Mitigation for Problem #6: Loss of Key Talent/Poor Knowledge Transfer.* All employees and contractors are important in achieving outsourcing success, but in the early pre-implementation stage, the client should identify the top 5–10 percent — essential due to their knowledge and skill base. Specific retention strategies (and sometimes contractual requirements) are created or applied to this group. When appropriate, the client should obtain the service provider's opinion and jointly develop approaches that limit staff turnover both prior to and during the implementation period.

Actions: Organizational and Procedural Alignment

- *Mitigation for Problem #1: Post-Contract Processes and Decision Rights Not Understood.* The client and service provider should jointly design key operational processes and decision rights prior to the implementation period.
- *Mitigation for Problem #4: Client Retained Team Not in Place or Too Small.* Integrated with the design of processes and decision

rights listed above, the client must initiate and complete organizational design for the overall retained organization. This allows inclusion in the business case for outsourcing as well as a full end-state vision of the operating model.

- *Mitigation for Problem #6: Loss of Key Talent/ Poor Knowledge Transfer.* Develop retention policies. These policies vary from reliance on communication and trust to bonuses being paid to all or a subset of staff based on their continued employment and achievement of specific goals and knowledge transfer. Retention policies should address both employees and contractors, and should be developed as part and parcel of the client's early outsourcing strategy — well before any RFP, contract negotiations or implementation takes place.

Actions: Governance Readiness

- *Mitigation for Problem #3: Poor Mutual Understanding of the Contract.* Not every person engaged in the outsourcing implementation should be a "contract expert." The client and service provider should designate single accountability — either in one person or department — for any issues associated with contract interpretation. The client and service provider should have a defined process for individuals to submit requests for contract interpretation, resolve the issue and communicate the correct interpretation.
- *Mitigation for Problem #4: Client Retained Team Not in Place or Too Small.* The client organization should "stand up" the new retained organization by placing qualified staff in defined roles in advance of required activities.
- *Mitigation for Problem #7: Inability to Meet Pent-Up Demand for Services.* Create capability to "fast track" key service requests. During the pre-contract period, the client should continue to engage its customers and end users regarding demand for services. The client should prioritize needs so the most important ones are addressed first after contract signing. The client should engage the service provider during the pre-contract period to provide visibility regarding demand, and determine a joint plan to address this during implementation.
- *Mitigation for Problem #10: Changes Don't Last.* The client governance organization needs to define ways to continuously demonstrate value through objective metrics and data. TPI has worked with organizations that use metrics as a way to achieve funding and buy-in for activities and changes required. Many times the retained organization is able to demonstrate that the value and risk mitigation it delivers far outweighs the cost.

Actions: Change Acceptance and Adoption

- *Mitigation for All Top 10 Problems.* A comprehensive communication program should be designed and delivered to all stakeholders who are affected by changes from outsourcing. All communication strategies and messages need to address one question — "what about me?" The communications not only need to be targeted to different levels of employees and contractors, but should also include individualized, one-on-one communications and forums to personalize the message and feedback loop.

Communications should be continuous and consistent — stakeholders want information and want to be heard.

- *Mitigation for All Top 10 Problems.* In addition to a comprehensive communication program, education and training should be developed and delivered to all stakeholders who are affected by changes from outsourcing. Appropriate training for new processes, new roles, basic contractual scope, and — above all — consistent education about the overall objectives and business benefits expected through outsourcing is required. Where appropriate, joint training/education sessions between the client and service provider is effective to promote mutual understanding and the ability to "walk in the other person's shoes."
- *Mitigation for Problem #9: Culture Clash Between the Client and Service Provider.* For clients using global/offshore delivery models, specific education about multi-cultural awareness helps to improve the team's understanding of the service provider staff's norms and customs. Service providers are often willing to help design and provide content for this type of awareness education. Many service providers have such programs in place for their employees, and are happy to share with their clients how they train their employees about cultural awareness.

CONCLUSION

If a client were able to achieve its cost, capability and capacity goals by itself, then outsourcing would not be required. By definition, outsourcing requires change.

The initial switch from internal to external service delivery is the first and most obvious change. Over time, additional changes are driven by organizational strategy, leadership, available talent/ skills, technology, business processes and regulatory requirements. The changes emanate from multiple sources: the client, the service provider(s), or external stakeholders. Consequently, getting buy-in and governance right is not a one-time event, but a continuous process.

However, implementing and sustaining change is one of the more difficult aspects of organizational leadership. It is challenging enough to align multiple stakeholders within the same company who have different priorities and agendas. Outsourcing introduces additional complexities — stakeholders don't belong to the same company or organization, can include different nationalities and cultures, and may be separa-ted by distance, time zones, languages and commercial interests.

Our findings of Top 10 problems point to the critical need for clients and service providers to cooperate and make Change Management and governance a priority. It needs to be integrated into overall program management and not treated as something "nice to have" but as the only way to achieve lasting, mutual success.

LOOKING FOR A STRATEGIC PARTNER?

TPI's experts can help you achieve your organization-al goals through objective advice, knowledge of your industry and experience with sourcing arrangements from simple to complex.

Looking for a strategic partner? Contact **Shawn McCray**, Partner, TPI, at **+1 941 730 4499** or **shawn.mccray@tpi.net**.

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Shawn McCray is a TPI Partner. He has extensive experience in helping clients with the full sourcing life cycle reviewing strategic alternatives and priorities; evaluating and negotiating contracts; and implementing third-party service provider solutions. Shawn has substantial international experience and particular expertise in assessing existing management organizations and processes and assisting with initial implementation and long-term operational management.

Before joining TPI, Shawn worked for EDS in a number of management positions, including Business Development Manager, Account Manager and Financial Analysis Manager. Shawn was directly involved in creating, implementing and managing sourcing agreements worth more than US$8 billion for clients across a variety of industries.

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ABOUT TPI: TPI, a unit of Information Services Group, Inc. (ISG) (NASDAQ:III) is the founder and innovator of the sourcing advisory industry, and the largest sourcing advisory firm in the world. We are expert at a broad range of business support functions and related research methodologies. Utilizing deep functional domain expertise and extensive practical experience, TPI's accomplished industry experts collaborate with organizations to help them advance their business operations through the best combination of business process improvement, shared services, outsourcing and offshoring. For additional information, visit www.tpi.net.

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