Managing Performance

5

5.1 Introduction

Now comes the challenge of making outsourcing deliver value to your organization – can you make a success of it? After the excitement of choosing a service provider and celebrating the award of the contract, how do you ensure that outsourcing produces the benefits that were promised? At first you may have a sense of anticlimax – or calm before the storm – depending on your perspective! The consultants and other expert advisors that helped guide your organization through the selection of the supplier and the negotiation of the contract have probably packed their bags and left.

The supplier that worked so hard to win your business, anxious to meet the service requirements, keen to meet with your organization, enthusiastic about what could be achieved and the improvements that could be made, now has the contract to provide the outsourced services. What difference will this make to the supplier's attitude? How will it approach the task? If your organization has followed the guidelines in Chapters 2 and 3, the risk of serious problems will have been minimized but it is not possible to guarantee success.

Much has been written about the decision to outsource, and many management consultancies offer expert advice on sourcing decisions and the evaluation of suppliers' proposals. Considerable analysis is available on the rational and contractual aspects of reaching an outsourcing agreement. Relatively little attention, however, has been given to the task of actually making outsourcing work once the contract is signed, which is a vital component of the work of many IT professionals. In the following chapters we will be looking at the challenges and opportunities presented by IT outsourcing in practice, how to manage the inherent risks and ways of tackling failure in the outsourcing relationship. This

chapter covers the management of the outsourced services and the maintenance of the outsourcing contract.

If an outsourcing initiative is to be successful it needs to be managed with care, attention to detail, vision about what might be achieved, close monitoring of financial issues and sensitivity to the needs of different stakeholders such as your senior executive and the service users. Both your organization and the service provider need to invest time in gaining deeper understanding of each other's working culture, establishing lines of communication between your two organizations and making sure that all those working on the outsourcing initiative are well informed, confident and motivated.

It is important that senior management continues to be involved in the management of information services. Few information systems operate in isolation. IT is integral to many business processes and cannot be divorced from business targets or outcomes. Try to devise systems that allow senior managers to participate in the co-ordination, monitoring and management of the outsourcing relationship, bearing in mind the other demands on their time. After all, we know that technology is ineffective unless it is aligned with business objectives.

As we first saw in Chapter 3, clear objectives should underpin the entire outsourcing initiative. Without agreed objectives, you will not know what you are trying to achieve through outsourcing and you will not be able to monitor your success.

5.2 Building Outsourcing Relationships

The key to successful outsourcing is building a relationship with your service provider that works in the longer term, not a quick fix economy drive. Put time and energy into deciding in advance how you are going to manage this relationship. An organization (whether customer or supplier) that is satisfied with its outsourcing relationship is likely to see it as successful and to take steps to reinforce and develop the relationship. From experience and research in this field we can draw lessons that will help your organization develop an effective outsourcing relationship:

1. *Build trust*. Work towards an open and honest relationship that is built on mutual trust. Trust needs to be earned. Where trust exists,

each party believes that the other organization will behave in a way that is mutually beneficial and will not act opportunistically. Express the wish to develop trust during negotiations and give the supplier opportunities to earn it. Acknowledge good performance and be open about concerns.

Your organization will have made a number of contractual commitments – payment procedures, the standard of assets transferred, assistance to be given during implementation and so on. Monitor these activities and alert the supplier to any difficulties. Deliver on time and demonstrate that your organization can be trusted.

The supplier needs to develop a track record for delivering services that meet contractual standards. Once this is established, your organization may invite the supplier to take part in strategy and planning discussions. The relationship can then evolve into a more strategic and closer alliance.

2. *Look for win-win solutions*. Recognize that both parties must benefit financially from the contract. Trying to create a "win–lose" position leads to resentment and a loss of commitment. It may also lead to a confrontational rather than collaborative style of relationship. Within some organizations there is a culture that encourages adversarial relationships with suppliers. There is an emphasis on "beating the supplier down" to the lowest price, fighting to win on every detail of contract interpretation. Those who are seen as "soft" on suppliers are criticized and probably feel that they have damaged their promotion prospects. Such an approach is unlikely to be successful in the longer term in IT outsourcing deals. It is a question of balance – there is no point conceding so much that your organization tips over into a "lose–win" position.

Both organizations should be able to understand and respect each other's goals and requirements. Work together to show the business community the benefits that can be delivered by IT services.

3. *Aim for co-operation not domination*. Outsourcing should not be based on a relationship of domination and dependence but on a spirit of co-operation and collaboration driven by shared benefits. During the negotiation stage, your organization and the supplier may have felt like adversaries, both sides defending the interests of their own organization. The relationship shifts when the contract is signed to become one in which co-operation is increasingly important if the IT services are to be successfully delivered. There will, of course,

continue to be discussions about contract changes that will require tough negotiation. But in the operation of services and in liaison with users, the style of relationship needs to become more co-operative and this change takes conscious effort.

4. *Good communications*. Effective relationships depend on good communication. Consider various ways in which your organization can communicate with the service provider at all levels within your two organizations. Map out a communications programme. You will be alerting your supplier to service failures, but remember too to congratulate them for good work. Share with the supplier as much as you can about your organization's processes and IT costs. The aim is to create a long-term relationship and one of the first steps towards this is to create an environment in which information is readily shared between your two organizations.

   A programme of liaison visits or secondments between your two organizations also encourages good working relationships.

5. *Aim for mutual understanding*. Take time to talk to your supplier about your organization – its plans, targets, organizational structure and core business. Don't limit discussions to the outsourced services or contractual issues, and don't let any personal prejudices get in the way. Try to give your service provider a better understanding of what makes your organization tick and what it hopes for in the future.

   Similarly, take an active interest in your supplier's affairs. Learn more about the organization, its culture and the services it offers. Celebrate with them when they succeed in winning new business; commiserate when they lose a potentially lucrative contract. Read their annual report and keep a look out for any relevant articles in the press.

   We are all inclined to make assumptions about organizations from the few individuals we meet: aim for a deeper understanding and you will be able to get more out of the outsourcing relationship.

6. *Criticize if you must, openly*. There is no room in an open and honest relationship for either organization to criticize the other behind their back. Problems or concerns should be tackled straightaway, before they fester and grow. Recognize that there may be a different perspective or point of view that is not apparent to your organization. Find out what this might be before you jump to any conclusions or take precipitous action.

This applies to service providers too. Work hard to co-operate with other suppliers and do not run down your customers in front of other organizations.

7. *Learn when to compromise.* Establish an open relationship and be prepared to compromise. Encourage a shared determination to make the contract work. Accept that your organization and your supplier will have different perspectives on the outsourcing arrangement. Expect value for money but accept the supplier's need to make a profit. Outsourcing contracts last for a long period and success depends on both parties being able to achieve business benefits from the deal.

8. *Resolve personality conflicts.* It can happen, unfortunately, that there is a personality clash between individuals appointed by your organization and the supplier to work on the outsourcing contract. These things happen and need to be resolved. Personality conflicts can be very damaging to the relationship between organizations. Try to avoid confrontations developing and avoid a blame culture. Be alert to the potential for problems developing and ensure that none of your own dealings with the supplier's representatives are soured.

9. *Foster realistic expectations.* Some users may expect miracles from your outsourcing supplier: minimal costs, improved quality and new services introduced immediately with no effort on their part. The reality of outsourcing throws into sharp relief facts about IT services and costs that relate to in-house provision too but may have been less visible in the past. Examples include:

   ● IT services cost money and appropriate budget allocations must be made to cover costs.

   ● New services take time to implement and users need to be closely involved not only in specifying but also in testing the services prior to formal acceptance.

   ● Customized services with minor modifications to meet each section's preferences are more expensive than standardized services and difficult to justify.

   Everyone in your organization who is concerned with the outsourced services needs to have an accurate understanding of the contract and a realistic expectation of the services to be delivered by the supplier. Otherwise the relationship between your organization and the service provider will be dominated by disappointment and dissatisfaction.

5.3 Understanding Stakeholder Perspectives

In Chapter 3 we looked at different perspectives within your organization on the outsourcing initiative. Once the contract is signed and implementation is underway, different viewpoints begin to emerge. Stakeholders in the outsourcing initiative include not only members of your organization but also staff in the supplier's company. They can behave co-operatively, enthusiastically, antagonistically, collaboratively or destructively depending on the issue at hand. Rather than look for a superficial harmony or agreement, it helps to face up to the realities of shared, complementary or conflicting goals. By understanding that stakeholders' goals sometimes conflict, we can recognize other positions while still protecting our own interests.

Table 5.1 illustrates some typical perspectives on outsourced services.

Table 5.1 *Perspectives on outsourcing.*

Stakeholder	Viewpoint
Customer's senior managers	Concerned that outsourcing should deliver business benefits. Looking for added value.
Customer's senior IT managers	Anxious that supplier meets contractual commitments. Will want to curtail excessive demands for service improvements so that expenditure on outsourced services stays within budget.
Customer's IT staff	Want to ensure that outsourcing is well managed and that the outsourcing service provider works well with other suppliers. Will watch for any negative impact on other in-house IT activities and will be concerned about possible extensions to the outsourcing contract to incorporate additional IT services and staff transfers.
Service users	Expect service excellence, however may have little knowledge of the costs incurred.
Supplier's senior management	Proud of winning outsourcing deal. Subject to keeping the customer satisfied will look to maximize profits.
Supplier's contract manager	Will carefully balance customer service and profitability to meet set targets. Concerned to ensure that problems are not escalated and referred to senior management.
Supplier's IT staff	The technical experts who will take professional pride in providing a good service but will also be aware of the budget and time constraints.

5.4 Outsourcing "Partnerships"

In all that has been written about outsourcing, the word "partnership" is the most commonly used description of the relationship between customer organization and supplier.

The dictionary describes a partner as "one who shares or takes part with another or others, especially in business firm with shared risks and profits; companion in dancing; player on same side in game; husband or wife" (*Pocket Oxford Dictionary*, 1984). Unless a joint venture company has been set up, the outsourcing customer and supplier are not true business partners. Although payments for outsourced services may be based on shared risks and rewards, the customer and supplier remain independent organizations, each ultimately concerned with protecting their own interests. The two companies might "play on the same side" in the "game" of promoting the possibilities of exploiting technology to deliver business benefit, but they will not be entirely on the same side when costs and timescales are discussed. The supplier is responsible for ensuring an adequate profit margin that maintains the viability of its business and meets shareholders' requirements. The customer needs to acquire IT services as economically as possible, compatible with the quality standard required.

Suppliers especially like to talk about their outsourcing partners and the term certainly does convey a warm feeling of collaboration and mutually beneficial activities.

This book promotes co-operation, collaboration, open, supportive and honest relationships between customer organization and supplier. But the word "partnership" does not frequently appear because it has been over-used and it is not entirely accurate.

Here are two extremes of the outsourcing relationship:

1. An arm's length relationship in which the customer organization fosters competition between multiple suppliers and awards contracts for each new piece of work on the basis of quality, time to delivery and price.

2. A very close, long-term strategic relationship in which the outsourcing parties do repeated business with each other and endeavour to share risks and rewards. This style of relationship takes time to evolve.

Your organization will need to determine the style of outsourcing relationship best suited to its needs and approach to business. Whichever style is chosen, outsourcing remains a commercial transaction in which the supplier has to keep earning business every day.

5.5 Communicate, Communicate, Communicate

Outsourcing introduces a whole new set of roles and responsibilities into your organization. This can produce uncertainty, doubt and fear. It can also lead to confusion and disorganization. Communication, not only between yourself and the supplier, but also with senior executives, business managers and users, will be a key element in delivering outsourced services successfully.

Communication takes place at various levels between your organization and the service provider:

- Senior managers, who review the overall outsourcing relationship, consider whether strategic objectives are being met and identify future direction, will discuss strategic matters.

- At the contract management level, discussions will focus on whether both parties are meeting their contractual obligations; they will agree contract charges, monitor performance, respond to contract change requests and provide an escalation route for service problems.

- With business managers and users, the supplier will discuss developing or changing service requirements.

- At the day-to-day operational level, discussions between your organization and the supplier will monitor performance against agreed service levels and review project progress.

You will need to devise a new organization structure to manage these communications effectively and this will be discussed in later sections.

It is important that regular communication is maintained at these various levels even when things are going well. Liaison should not simply be

about problem resolution but should also include planning, identifying opportunities and celebrating success. Communicate early and often and allow time for the outsourcing relationship to mature: don't expect liaison to work well from day one.

Remember to continue communicating with business managers and users in your organization. Their awareness, understanding and commitment are important factors in the overall success of outsourcing. Initially their expectations may be unreasonable and they may find it hard to come to terms with the more structured and formal approach that may be necessary now that some IT services are purchased from an external provider. This happens in part because the concept of outsourcing will have been sold enthusiastically before the contract is signed. People throughout your organization need to be aware of the reasons behind the decision to outsource and the objectives, and they need to understand the impact on their work. Consider preparing newsletters, posters, leaflets and presentations jointly with your supplier to communicate these key messages to others in your organization.

Communications with staff who are transferring to the supplier are particularly significant. As their new employer, the supplier should take the lead but it is helpful if senior management from both your organization and the supplier are involved. It is only natural that this group of staff will be wary of what the future holds. They may fear a loss of control, increased workloads without compensation and working in a new culture. Communications will be needed at group and individual level, briefings, road shows, Intranet sites, personalized letters and enquiry points.

5.6 Transition

The implementation of the outsourcing contract, or transition from in-house to outsourced IT services, should be well managed just as any other IT project. The overall transition plan is initially put together by the supplier and submitted as part of the response to the statement of service requirements. The plan is refined during negotiations and put into effect once the contract is signed.

Transition commonly takes place in phases and may take up to a year to complete. Any longer and there is a danger that the state of transition becomes the norm and the incentive to complete the task is lost.

The first few weeks are significant in that they create an initial perception of outsourcing that, like all first impressions, can be difficult to change at a later date. The supplier will want to make a good start and you will want to demonstrate that you have chosen the best supplier. So it helps to choose some activities that can be completed readily and do not carry too many risks. Effective communications with service users will be important because there may be an unrealistic expectation that services will improve from day one and the supplier will be fully responsible for all aspects of service performance immediately the contract is signed.

The transition phases can best be managed as a series of projects, with the completion of each project a checkpoint in the transition to outsourced services. There should be a timetable for these checkpoints and this can form a useful measure of the supplier's performance during transition. Although the supplier will lead the overall transition programme and will be responsible for many of the activities, your organization will also have a number of responsibilities, particularly tasks that involve internal communications.

The transition plan should cover:

- transfer of responsibility for IT services;

- all activities relating to the transfer of staff to the supplier;

- transfer of assets, reassignment of software licences and so on (this is discussed further in Chapter 7);

- set up and introduction of contract management structures;

- implementation of contract management processes including invoicing and payment procedures;

- post-contract verification of service costs, performance levels and assets if this was agreed during negotiations;

- compilation and distribution of guides to the contract and to the outsourced services to users;

- communications programme;

- introduction of change request processes (there will probably be a backlog of requests if system changes were frozen during the selection of supplier and negotiations);

- implementation of problem management and escalation procedures.

5.7 Incentives and Disincentives

Think through carefully what incentives you are able to give to encourage your new supplier to innovate or propose service improvements and what discourages poor performance.

Contracts often include penalty clauses for serious breaches. These are necessary to protect the interests of your organization but represent a significant failure. Fines are not generally imposed lightly on suppliers and must be backed up by detailed, accurate service performance records. Although some allowance may be made for isolated reductions in service levels, any failure to meet contractual standards should be resolved quickly before it becomes accepted as normal practice. If hefty fines are imposed, the supplier's account managers will spend a lot of time verifying data in order to protect their organization's interests. As a consequence, there is a risk that insufficient attention will be paid to correcting service faults and raising standards, which is of course the objective of imposing the fines in the first place.

Day-to-day management of minor service lapses are therefore probably best dealt with by a system of service credits, which can be paid as fixed sums or treated as a rebate to charges. Alternatively, a sliding scale of charges can be used, so that lower charges (or no charges at all) are paid if service levels fall.

Although compensation, penalties or service credits are frequently incorporated into outsourcing contracts to discourage poor performance, they do little actively to encourage service excellence. It is not easy to formulate incentives that encourage innovation and service improvements but here are a few suggestions to consider:

- Encourage suppliers to propose service improvements based on their expertise, perhaps by setting up quarterly meetings dedicated to considering proposals put forward by your service provider.

- Set aside a modest research fund to be used in whichever way the supplier chooses in the development of innovative proposals. This fund can be topped up at your discretion if and when these proposals are accepted by your organization.

- Devise formulae that allow you to share the benefits of service improvements with your supplier.

- Act as a prime reference site for your service provider.

- Publish articles about the success of the outsourced services provided by your supplier.

- Award bonus payments to the supplier's team related to the findings of independent user satisfaction surveys in your organization.

- Pay a proportion of the operational savings made through technology upgrades to your service provider.

Think through the consequences of any incentives planned; they can sometimes produce unanticipated results. For example, if payments are linked to system availability, your organization will pay more for 98 per cent availability than 95 per cent even though the lower performance level may be quite sufficient for your organization and you gain no benefit from the higher availability level. If your service provider is under contract to make IT purchases on behalf of your organization and is paid commission on each acquisition, more equipment may be purchased than you need because this increases your supplier's income.

In all cases your organization should stay in control and have the final say on the adoption of innovative proposals for service development. But you can take steps to encourage your service provider to come forward with ideas and guide them on the type of proposal that would be welcomed by your organization.

5.8 Adding Value

It is one thing to get your supplier to provide the outsourced IT services to contractual levels; it is quite another to derive added value from the outsourcing relationship.

What do we mean by "added value"?

- More services for the same cost?

- Access to new technological skills?

- Ready access to additional IT skills?

- Innovation and fresh thinking?

- Reduced operating costs?

Different stakeholders have different perspectives. Users will probably expect more services without increased charges. Business managers may think about exploiting technology more effectively. Suppliers may consider the delivery of operational savings, as specified in the contract, to be "added value".

Initially when the outsourcing contract is signed, the focus needs to be on critical transition tasks. Get the basics right first and ensure that outsourcing processes are functioning correctly. Once this has been accomplished, work with your supplier to consider ways in which the outsourcing relationship can add value to your organization. Draw on ideas from both organizations and put together a package of initiatives to take forward. Here are a few ideas to get you going:

- Aim for a culture of continuous improvement in the management of the contract. Set targets each year for service enhancements (those that deliver business benefit) and cost reduction.

- Empower staff in the supplier's organization to make service improvements subject only to reasonable constraints.

- Maintain a record of the technical skills available from the supplier and make sure that all new project managers within your organization are aware of this potential resource.

- With the service provider, carry out annual reviews of key performance indicators. Remove those that no longer serve a useful purpose and divert the supplier's resources away from priority areas. Introduce new measures that reflect current business needs.

- Set up an Added Value Forum that meets to discuss ways in which technology can be exploited to deliver greater business benefits within your organization.

- Explore potential commercial possibilities through, for example, joint ventures with your service provider.

An environment in which innovation is welcomed and service excellence valued is challenging and motivating for everyone.

5.9 Contract Management

The contract management process ensures that both customer and supplier fully meet their respective obligations as efficiently as possible to meet the overall business objectives of the outsourcing initiative. The customer organization will want to buy IT services economically and the supplier must make a profit to stay in business and there is a natural tension between these objectives. The contract managers from both customer and supplier will aim to get the best possible deal for their respective organizations while maintaining a good working relationship. Effective contract management is based on:

- a shared understanding of outsourced service boundaries and costs;

- an unambiguous and comprehensive contract with supporting schedules including service level agreements;

- mechanisms for proposing, negotiating and incorporating contract changes;

- clear contract management structures and reporting procedures;

- effective channels of communication;

- regular and frequent meetings.

Contract management plans need to be developed at an early stage in the outsourcing programme so that you can hit the ground running when the contract is signed. It is not helpful to discover shortly after the deal is agreed that all suitably skilled staff have either transferred to the supplier or have been assigned to new projects within your organization! Initially, the emphasis in contract management will be on disseminating information about the contracted services and discussing interpretation of the contract in detail with the supplier's representatives. It is vital that your organization has people with the right blend of skills and knowledge to tackle these tasks.

The responsibilities of the contract management function include:

- disseminating information about the outsourcing contract and clarifying details;

- agreeing contract interpretations with the supplier;

- monitoring compliance with the contract, ensuring an appropriate balance between the cost of monitoring and the risk of problems occurring;

- managing the contract change process;

- managing disputes;

- regular liaison with the supplier's contract manager;

- negotiating financial arrangements for new services;

- monitoring the total value of the outsourcing deal, business benefits delivered and expenditure;

- reviewing delivery against overall outsourcing objectives.

Contract management is a distinct role within the IT function and it would be a mistake to assume that any IT manager could readily succeed as a contract manager. Here are some of the qualities, skills and expertise needed by the customer's contract manager:

- Credibility and authority within both customer and supplier organizations

- Determination and self motivation

- Excellent communication and negotiation skills

- Good understanding of business requirements

- Broad technical understanding and awareness of technology developments

- Knowledge of financial matters

- Political skill to retain the support and confidence of business managers and service users

- Sound understanding of the contract

- A firm but fair approach when dealing with the supplier

- Courage to stand up to tough negotiation by the supplier and to resist unreasonable demands from service users

- Ability to manage conflicts

- Awareness of computer services industry issues.

Having an appropriate person to manage the outsourcing contract is key to its success. The right blend of knowledge, attitudes and skills earns the confidence and trust of business managers and service users. The supplier will regard such a contract manager highly, as someone who enjoys wide support within your organization and a high degree of credibility.

The contract manager treads a fine line between your organization and the supplier. It is important that your organization feels that the contract manager is close to hand and not unduly influenced by the service provider's point of view. It therefore makes sense for the contract manager to be based in an office where he/she is readily accessible to the service users. If the supplier's contract manager is offered an office nearby, this can enhance communication between the two managers and to help them resolve disputes. If your organization's contract manager is offered accommodation at the supplier's site, he/she should use this only occasionally.

5.10 Service Management

In outsourcing relationships the focus of service management shifts to service performance monitoring and review. The service management function covers:

- monitoring services to assess whether performance targets are met;

- carrying out periodic reviews of service level agreements, performance measures and service requirements;

- maintaining service quality and technology interface standards, which help create a predictable and measurable environment – these standards make it easier to integrate services from different suppliers and will facilitate the transfer to a new service provider when the current outsourcing contract comes to an end;

- discussing business plans that could affect the outsourced services as early as possible with your supplier;

- involving your service provider in your organization's planning process – they may be able to offer valuable input to the review of the viability, costs and timescales of different options.

Measure services at the point of delivery. Your service provider should have the option of changing the method of service delivery over time, as long as performance standards are met. Monitor features such as capacity, availability, business continuity, security services, desktop facilities, problem management and user satisfaction.

To carry out this function you will need to set up a service control team, based in your organization's offices. The team needs a good understanding of the applications and technical environment used by your service provider and will, therefore, need to include in-house technical staff. Monitoring tasks rather than hands-on IT work is not to everyone's liking, so the service control team should have clear career development opportunities to help it remain well motivated for the critical outsourcing role it performs.

The responsibilities of the service control team include:

- carrying out formal service acceptance procedures when the outsourced services are first introduced;

- analyzing performance data from the reports produced by your supplier;

- assessing service management standards through the supplier's adherence to best technical management practices such as the Information Technology Infrastructure Library (ITIL) standards;

- monitoring the completeness and correctness of operations and system procedures such as contingency plans, back-up procedures and test procedures;

- resolving service issues and problems;

- reviewing invoicing procedures;

- analyzing new service requirements or changes requested and following them through the change control process.

The team can collect data from performance reports produced by your supplier, regular meetings with the supplier's service management team, visits to the supplier's premises and direct access to some of the supplier's systems. This data should be consolidated and analyzed for the contract manager and other senior managers in your organization. It may also be helpful to present a summary of the findings to liaison meetings with representatives from the service user community.

5.11 Service Users

To get the best out of your outsourcing arrangement, you will need to encourage the service users to develop a good understanding of the new, formal arrangement between your two organizations, how to request service changes, how to tackle problems and how costs are incurred. One of the advantages of outsourcing is that users should become more aware of the balance between quality and price, and should more critically examine the business benefits of system modifications and developments.

Promote understanding by sharing information with users as the outsourcing programme progresses. If there are a large number of service users you may find it helpful to ask for user representatives who have a good knowledge not only of business operations but also of business strategy and longer-term goals. These representatives can help you identify future service requirements and set appropriate performance standards. These representatives are sometimes known as "informed customers" or "intelligent customers". Their role is to:

- act as a point of contact between your service provider and a group of users, co-ordinating views and disseminating information;

- encourage constructive working relationships between your supplier's staff and the end users;

- interpret the users' requirements and concerns as necessary for the supplier;

- promote understanding of the outsourcing contract, the costs incurred for various IT services and the balance between quality and cost;

- help users understand and follow problem escalation and change request procedures;

- liaise with the contract manager and service control team to co-ordinate activities across your organization.

This role is especially important if there are a large number of service users, perhaps widely dispersed throughout your organization. In these circumstances it is not possible for all communications and other dealings with your outsourcing supplier to pass through a small team in the IT department. User representatives can then play a very helpful role in

the success of the outsourcing initiative. You will need to be clear about whether their role is to control, co-ordinate or facilitate communication between business areas and your service provider and to what extent they are authorized to instruct the supplier. Do make sure that the role is fully developed, understood by all those working on the outsourced services and communicated to all users.

Contact with the service users helps your supplier to get a better understanding of user requirements and problems.

5.12 Contract Administration

You will need to implement a number of administrative procedures and clerical functions to support the outsourcing contract. Contract administration procedures include:

- contract maintenance;
- charges and cost monitoring;
- ordering procedures;
- payment procedures;
- budget management;
- performance reporting;
- asset management.

The procedures should be designed to reflect the scope and complexity of the outsourcing contract and your organization's policies and business processes. Clear administrative procedures ensure that everyone understands who does what, when and how.

5.12.1 Contract Maintenance

IT service requirements will evolve over the life of the outsourcing contract and must respond to changes in the business environment. The contract documents should be modified through formal change control procedures and by mutual agreement with your supplier. It is best to update contract documentation as changes occur rather than relying on

informal arrangements. Even in the best outsourcing relationships, differences of opinion do occur and it helps to have up-to-date contract documentation.

Apply sound document management principles:

- Identify all relevant contractual documentation, for example contract clauses and schedules, service level agreements, procedures and manuals.
- Control all changes to documentation using version control and change control procedures, ensuring that no changes are made without proper authorization.
- Record the status of documents – current or historic, draft or final.
- Ensure consistency across all contract documents.

There are three types of contract change:

1. Changes to contract conditions, which should be processed as numbered contract amendments and formally accepted by both your organization and the supplier. Maintain a register to track the status of each amendment, recording the date the change was first proposed and when it is accepted. Remember that the amendment legally only comes into effect when it is formally accepted by both parties. The contract administrator should monitor the progress of all proposed amendments and chase outstanding responses from your supplier.

2. Contract changes made under an enabling condition. For example, service level agreements are usually included as contract schedules while the main contract clauses include a condition defining how changes to these agreements will be processed or a new agreement added. Records of such changes should be maintained. It can be helpful to add a record of the changes formally to the contract from time to time.

3. Changes to the interpretation or understanding of the contract, which are documented and agreed through separate letters, reports or minutes of meetings. These can be difficult to track but do need to be recorded. One solution is to make a note in the contract amendment register and annotate the working copy of the contract with a cross-reference to the relevant material.

Keep the master copy of the contract (the original, signed contract documents and amendment papers) separate from the latest working copy that incorporates agreed amendments. A back-up copy should be held in a separate secure location.

5.12.2 Charges and Cost Monitoring

The contract should specify cost formulae and charging mechanisms. Different approaches may be needed for the different services covered by the outsourcing contract. Types of service charge include unit costs, a flat service charge irrespective of usage, fixed price quotations and benefit sharing mechanisms.

In many cases the costs incurred by the supplier will not be visible to the customer organization and payment will be based on agreed service charges. But in some instances, contracts may operate on the basis that the supplier shares some cost information with the customer organization. This open book accounting approach gives the customer access to information about costs incurred and profit margins achieved. This degree of openness is important in benefit sharing arrangements.

Charges and costs incurred under the outsourcing contract should be monitored to help determine if the arrangement is delivering value for money. This information will feed into discussions with your supplier about possible changes to services or charging mechanisms.

If the contract provides for inflation by allowing price variation relative to an agreed index, the contract administrator will need to monitor price changes to ensure that they fall within agreed limits. Similarly, where contracts commit the supplier to reduce operating costs over a set period, this will also need to be monitored.

The contract manager will need to keep under review the overall cost of the outsourcing contract to ensure that the service costs remain within budget. Internal costs, including the costs of managing the contract, need to be taken into account.

5.12.3 Ordering Procedures

The outsourcing contract will specify requirements and costs for a core set of IT services. During the life of the contract new services or modifications to current services will be required. Processes for raising these

requests and reaching agreement on charges should be incorporated in the outsourcing contract. Procedures should be introduced and clear guidance issued to determine:

- who in your organization may request and authorize service changes;
- whether and when there should be an internal technical or business review of service requests within your organization;
- responsibility for financial approvals;
- who in the supplier's organization may accept service orders and allocate resources to deliver them.

The contract administrator should record details of all service orders submitted to the supplier to ensure co-ordination and accountability. This helps identify any discrepancies, check orders and spot any opportunities to reduce costs through economies of scale.

5.12.4 Payment Procedures

The outsourcing contract should cover payment processes including:

- structure and content of invoices;
- submission of invoices;
- invoice approval process;
- payment terms.

Your organization probably has existing procedures for paying invoices. You will need to ensure that there is adequate co-ordination and liaison between service users, the contract manager and the finance department so that invoices are correctly authorized for payment.

If invoices are submitted centrally you may need to allocate or recharge costs to individual departments to meet your organization's internal accounting requirements. In this instance you will need to make sure that the supplier provides sufficient detail and presents charging data in a suitable format on the invoices.

Do not forget to monitor your organization's compliance with the agreed payment terms. In large organizations especially, there can be quite a

delay between invoice authorization and actual payment to your supplier. The larger outsourcing suppliers understand this and some delay should not cause too many difficulties. But smaller suppliers may be more sensitive to any delay and their business will suffer as a result. Look into this before it becomes an issue. It helps to understand how your organization works and how many days will elapse between invoice authorization and payment to your supplier.

Service credits may be incorporated in the outsourcing contract to compensate your organization should the supplier's performance be poor. The credits should be clearly linked to specific services and agreed service levels. The contract administrator should monitor the calculation and payment of service credits.

5.12.5 Budget Management

Practice varies from one organization to another, some organizations retain budgets for outsourced IT services centrally while others delegate budget provision to the departments that use the services. In both instances, however, there is generally a need to monitor committed and proposed expenditure under the outsourcing contract to ensure that it does not exceed the allocated budget.

The contract manager will also participate in forward planning for the service, budget allocation and in defining forward commitments for future use of the outsourced services.

5.12.6 Performance Reporting

Requirements for performance reports and management information are defined in the contract. Information may be required about all performance measures or only about "exceptions" or instances where performance varies from agreed standards. Exception reporting helps focus on potential problem areas and reduces the volume of reports and hence time needed to review the data. But it can also hide trends and uninspiring (but not contractually inadequate) performance. Information about service performance may be disseminated to the contract manager and key user representatives, with summaries submitted to senior IT and business managers. There is further discussion about performance measurement and reporting in Chapter 6.

5.12.7 Asset Management

If ownership of any of the assets used in the delivery of the outsourced services, such as hardware, office equipment and premises, is retained by your organization, then you will have responsibility for these assets. If your supplier carries out the day-to-day management of these assets you will need to ensure that:

- your organization's asset register is kept up-to-date;

- any third party use of the assets is recorded (for example, if your supplier delivers services to other customers using your equipment);

- upgrades and replacements are planned and budgets identified;

- your supplier provides an audit trail of technical changes made to any systems.

If assets have been transferred to your supplier as part of the outsourcing deal but will transfer back at the end of the contract term, you will need to ensure that your supplier is maintaining an up-to-date asset register and recording upgrades and changes.

In some cases, charges will be based on the assets used, for example help desk service charges may be based on the number of PCs. Clearly in this instance it is essential to keep the asset inventory up to date as charges will be based on the information in this system.

5.13 Outsourcing Management Organization

In earlier sections we examined a number of new functions that need to be introduced to manage and monitor the outsourcing initiative once the contract is signed. These are summarized below:

- Contract management
  - Disseminating contract information
  - Negotiating interpretations and contract changes
  - Monitoring contract expenditure against budget, value and benefits

- Service management
  - Service performance monitoring
  - Service level agreement reviews
  - Maintenance of service quality and technology standards
  - Service planning
- Service control
  - Analysis of performance reports
  - Monitoring contingency plans, test procedures etc.
  - Resolving service issues
  - Analysing service change requests
- Informed customer
  - Co-ordinating user feedback and disseminating information to users
  - Promoting understanding of contract and procedures such as problem escalation
- Contract administration
  - Contract maintenance including document updates
  - Introduction and maintenance of various procedures such as charging, invoicing and payment procedures
  - Detailed budget monitoring
  - Collection and distribution of performance reports.

All outsourcing contracts need to be managed effectively if they are to be successful, but the size of the team required will vary depending on the scale and complexity of the IT services that have been outsourced. Small-scale outsourcing initiatives may require a small team of perhaps three or four members of staff who share responsibility for the various functions. Large complex outsourcing deals, on the other hand, may require very large teams of 50 or more staff with separate sections concerned with service control, contract administration and so on.

Your organization needs to plan at the outset how and when the outsourcing management team will be identified and trained. This needs to be done before staff transfers are discussed in detail with potential

suppliers to ensure that your organization does not find that it has agreed to transfer all those with relevant expertise and business knowledge to the supplier.

The outsourcing management team needs to develop influencing and relationship management skills, the ability to co-ordinate and represent business requirements and negotiating skills that will be used informally in daily dealings with your supplier. Some technical skills need to be retained too so that proposals put forward by the supplier can be properly assessed and technical plans evaluated.

From the experiences of various organizations we can draw a number of lessons about outsourcing management:

● Establish unambiguous roles and responsibilities for the outsourcing management team, service users and the supplier. Develop a responsibility matrix that shows which party is responsible for each specific activity and whether that activity is within the scope of the core contract or subject to excess fees.

● Build a formal contract management structure into the contract and monitor your supplier's compliance with this structure.

● Define the supplier's point of contact in your organization for specific issues and ensure adherence. This will stop the supplier making unwanted advances to business managers and shifting the focus of the contract away from the main services to more lucrative opportunities.

● Regularly review the outsourcing management team numbers and skills – requirements will probably change during the life of the contract. Try to anticipate changes in requirements before any skills gaps have an impact on contract performance.

● Retain the right to veto the supplier's choice of key contract management staff so that the quality of outsourced services can be maintained and ensure that, whenever possible, your organization is given early warning of any such changes.

● Use secondments between your organization and your supplier to help build effective working relationships and greater understanding between your two organizations.

● Be aware that job titles can give a false impression and use descriptions that are meaningful in your organization. The function may be

described as contract management, relationship management or alliance management. The team roles may be described as manager, liaison officer, advisor, administrator or support staff. There are many other possibilities. Everyone needs to know exactly what is expected of them and what they can expect from others.

- Maintaining adequate technical expertise in the outsourcing management team can be difficult. With the daily technology work on the IT services transferred to the supplier, the technically skilled staff that remain in your organization may not have the opportunity to update and practise their skills on a regular basis. It will also be difficult to develop this expertise in-house. Your organization will need to address this issue before problems occur. Some companies have found it useful to second these staff to the service provider from time to time for short periods; others have found it necessary to buy in technical specialists as and when required.

- It is useful to build into the contract management process a review of the process itself. This might be combined with an annual performance review.

5.14 Meetings

There will be plenty of informal contact and liaison between your service provider, the users and the outsourcing management team but a well-structured and planned series of more formal meetings will help you get the most out of the outsourcing deal and avoid unnecessary problems. The overall objectives of the organized meetings are to:

- ensure that the outsourcing arrangement is properly controlled and managed;

- promote the development of excellent relationships between the supplier and your organization;

- tackle issues before they become major concerns;

- derive maximum added value from outsourcing;

- provide a formal record of problems aired, which will be necessary should formal action be taken against the supplier or the contract prematurely terminated.

The number and frequency of meetings will vary according to the nature of the outsourcing initiative. Some examples are given below:

- Weekly operations meetings to discuss detailed service issues and problems.

- Monthly status meetings to review performance and monitor costs.

- Quarterly strategic meetings to discuss new directions or services.

- Quarterly service improvement meetings to review proposals from the supplier to enhance the efficiency or effectiveness of current outsourced services.

- Twice yearly innovation forums in which ideas are brainstormed and the emphasis is on adding value to the outsourcing relationship.

- Annual meetings to review service performance criteria, overall contract value and other major issues.

Each meeting should have its own distinct set of objectives. Aim to avoid overlap: it is not uncommon for the same set of people to find themselves at several different meetings discussing similar topics, which can waste a lot of time.

It is a good idea to set down proposals for a structure of meetings, giving suggested membership, frequency and terms of reference for each meeting and explaining how the meetings interrelate. Preferably do this before the contract is signed and invite comments from colleagues in your organization and from potential suppliers. The aim is to have in place an agreed set of meetings when the contract is signed. Representatives should be nominated and dates fixed in diaries for the coming year as soon as possible – remember that you want to maintain the commitment and involvement of senior managers in the outsourcing initiative.

5.15 Change Control

If outsourcing is to succeed it is important that your organization recognizes that IT service requirements will change and is willing to accept appropriate costs. Enhanced or new services will attract higher charges, but IT should be an enabler not a constraint to business so encourage

co-operative contract evolution to take advantage of developing technologies and other opportunities for service improvements.

The outsourcing contract should include change control mechanisms. A formal change request process ensures that your organization understands the value it will gain from the modified or additional services and the full costs that will be incurred. The change control process should prevent an enquiry about a possible change generating a considerable amount of investigation and analysis without proper review and authorization.

In the early days of a new outsourcing contract a large number of change requests may be raised:

- There may be a deluge of user demand for service improvements if these have been put on hold during the supplier selection process.

- In many outsourcing contracts, although the core set of IT services outsourced have been well defined, various IT activities are inadvertently overlooked or service use volumes have to be adjusted.

You will need to determine who can authorize various change requests and how this is done. This will probably vary according to the cost of the change and the impact on the overall outsourcing programme. If there are a very large number of change requests to be dealt with, it may be worth setting up a separate change authority group.

The change control process encompasses a set of procedures, which enable either your organization or the supplier to propose a change and define where the change will be costed, how other impacts will be identified and where the decision will be made to accept or reject the proposed change. The process is illustrated in Figure 5.1. A fast-track process should also be designed to handle urgent requests. In this instance the contract manager could be authorized to submit the proposal to the supplier for impact assessment. The IT Director or other senior manager could review the costed proposal.

The author of the change request allocates a priority rating on the following lines:

1. A necessity: the outsourced IT services will not function correctly without this change.

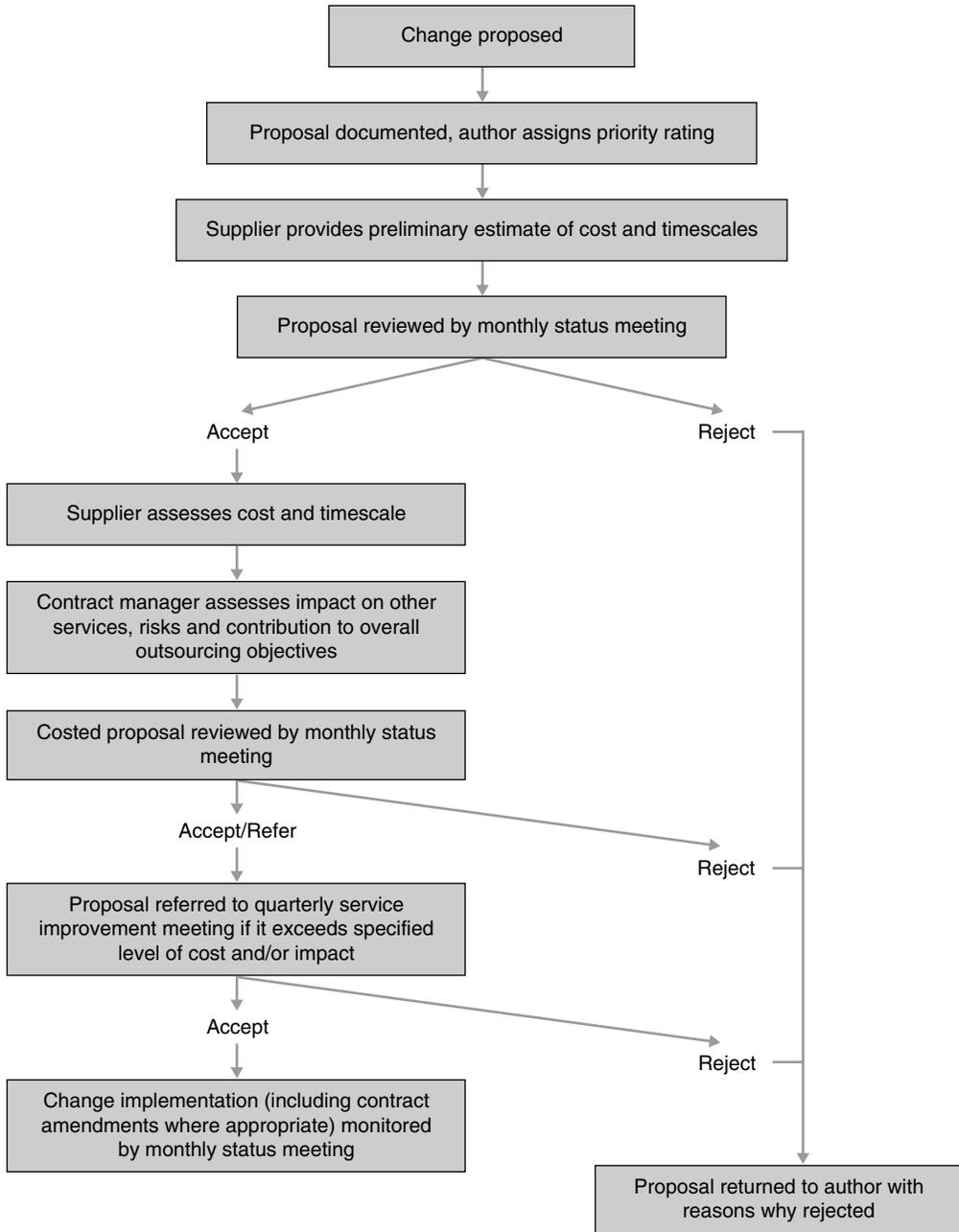2. An important change: this is needed to meet business objectives.

Figure 5.1 *Change control process.*

3. A nice to have, but not vital.

4. A cosmetic change, which would be welcome but does not deliver a quantifiable business benefit.

The last two categories of change are unlikely to be accepted unless costs are minimal.

To avoid unproductive but lengthy impact assessment work, the supplier is asked to give a preliminary estimate of cost and timescales. If these are significant the change will only be taken forward if it has a high priority rating.

A suitably authorized group such as the monthly status meeting will review the fully costed proposal. This group may have a limit set on the changes it can authorize. More expensive changes or those with a greater impact on your organization may need to be referred to a more senior management group.

The final step in the change control process is to monitor progress in the implementation of the change, including contract amendments where appropriate.

At any of the review points, the change proposal may be rejected for a variety of reasons such as being too costly or delivering insufficient business benefits. When this happens the author of the request should be notified and given the reasons for the rejection.

A register should be maintained to record details of all change proposals received, impact assessments, decisions and progress. A sample form that can be used to collect this information for each change request is given in Figure 5.2.

5.16 Issue Management and Problem Escalation

Inevitably every outsourcing programme raises some unexpected issues and problems occur. Rather than let disputes fester it pays to introduce procedures for bringing problems and potential difficulties to your supplier's attention. Your organization should not expect always to get its own way. Try to find a resolution that costs your organization little but

Reference No. (Assigned by contract administration office)
Change Proposal
Priority Rating (Assigned by author)
Preliminary Estimate (Prepared by supplier)
Initial Review Outcome (Authorization to proceed to full impact analysis where necessary)
Supplier Impact Assessment
Contract Manager Impact Assessment
Outcome of Review of Impact Assessment
Planned Implementation Dates
Date Author Notified of Rejection (where appropriate)
Implementation Completion Date

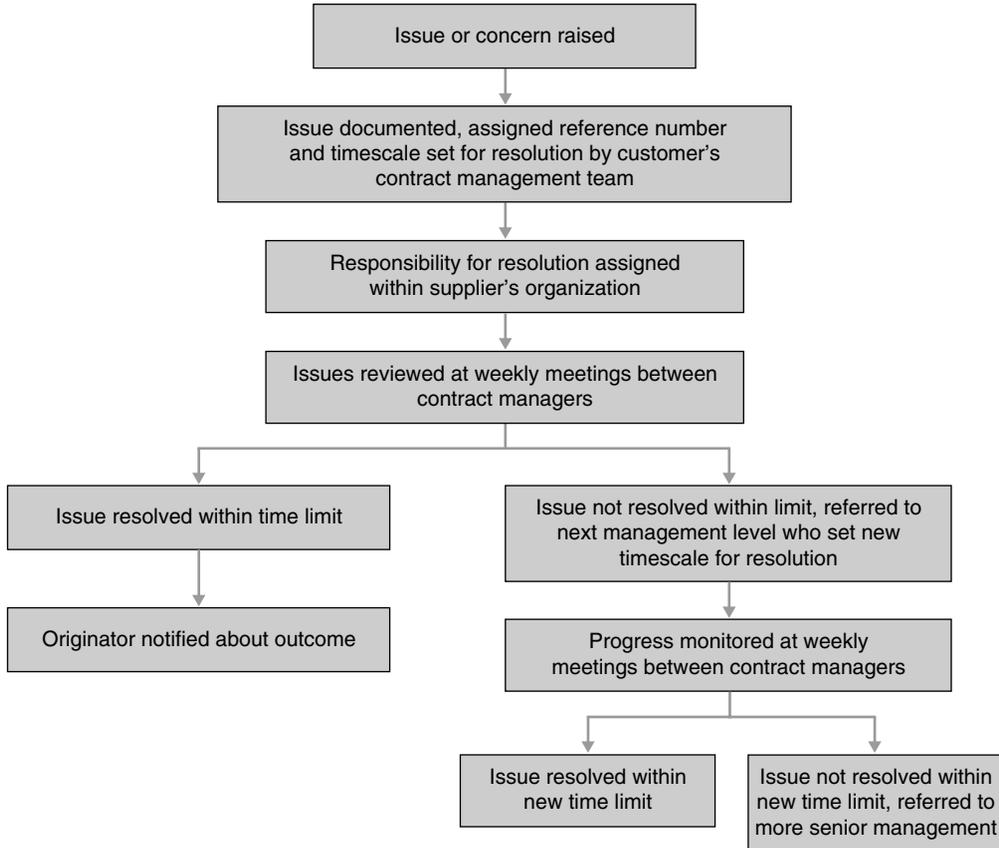**Figure 5.2** *Sample change request form.*

Figure 5.3 *Issue management process.*

gives your supplier a face saving way to agree with you. One solution is to aim for a written commitment to a timetable for resolving the problems. While your supplier has to make a sufficient profit margin to stay in business, it will want a satisfied customer as well. Generally suppliers price contracts in such a way that they make most profit towards the end of the contract term so they want the contract to last long enough to reach this stage.

Potential problems are best raised initially as issues, which may be questions or statements about concerns or difficulties with the outsourced services. Issues should be assigned to named individuals for resolution and reviewed regularly. Until the supplier has reviewed the issues, the severity of the problem is not always clear. Indeed it may be a misunderstanding rather than a service problem.

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Introduce a well-defined, timed escalation process that includes a way to prioritize issues and allocates time limits for the resolution of problems. Define equivalent pairs of people at each level in your organization and the supplier; problem resolution can then be referred up through the various seniority levels in each organization. Make sure that you maintain order during the escalation process without either side going straight to the top and bypassing agreed procedures.

The issue management process is illustrated in Figure 5.3.

The goal of all those involved in issue management should be to resolve problems without the need to refer them to senior management levels. When major difficulties do occur, the time you have spent in escalating the problem through agreed procedures and the time spent by your IT managers trying to resolve the problem will illustrates the depth of concern to your supplier's top management.

Chapter 8 looks further at resolving difficulties when outsourcing fails to deliver.

5.17 Critical Success Factors

We conclude this chapter by summarizing the critical success factors that underpin effective management of outsourced services:

● Plan together with your supplier from the beginning. Focus on the underlying objectives of the outsourcing initiative to develop a shared vision of the way forward.

● Invest in building and sustaining excellent working relationships between the supplier, the outsourcing management team and service users. Aim to develop understanding and mutual trust through honest and open dealings with your supplier. Look for win–win solutions and know when to compromise.

● Nurture teamwork; put together teams from your organization and your supplier to tackle issues and use secondments to increase understanding between your two organizations.

● Try to understand the perspectives of different stakeholders in the outsourcing initiative and ensure that users and senior managers in particular have realistic expectations about the outsourced services.

- Recognize the importance of communication and introduce systems that ensure information is disseminated to all those involved in the outsourcing initiative.

- Introduce incentives and processes that encourage improved service performance and increased business benefits derived from outsourcing. Look for opportunities to add value to your organization from the outsourcing relationship.

- Retain in-house control over the strategic direction of the outsourced IT services by setting up a skilled contract management team.

- Define outsourcing management roles and responsibilities both for your organization and for the supplier's representatives. You also need a clear definition of the boundaries of the outsourced IT services.

- Monitor the performance of outsourced services against objective criteria and resolve problems as they occur.

- Schedule regular operational and strategic review meetings.