

# Outsourcing White Paper Series: **Guidelines for Outsourcing Governance**

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Provided by

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# The Context of Outsourcing

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Organizations engage in outsourcing agreements for a variety of reasons such as cost cutting, economy of scale, enhanced capability, improved flexibility or simplified management of a functional area. Whatever the reason for outsourcing, it is critical that the appropriate governance model be established to ensure not only initial success, but also long-term viability.

No matter what governance model that is adopted for your organization's outsourcing needs, NET(net), Inc.'s experience has shown that in order to be successful, the model has to focus on the business goals of the organization and provide an overall framework for ensuring appropriate levels of communication and customer satisfaction are met. Too many organizations focus on service level agreements (SLAs) to manage the outsourcing relationship, and while SLAs are very important, they are not the only factor in achieving success in outsourcing.

Having an appropriate governance model does not have to be a complicated effort, but it often is glossed over or not considered quantitative enough to put into an outsourcing agreement. However, those organizations that focus on governance and relationship management find their path to outsourcing success much easier.

This White Paper is the latest installment in NET(net)'s Outsourcing Series, in which we provide guidance and recommendations for helping organizations cope with the complexity and changing nature of outsourcing agreements. Many clients we work with underplay or overplay their ability to persuade their suppliers to bring them to their way of thinking. In this whitepaper series, we will discuss the four most effective strategies we have seen clients use to optimize their persuasiveness with their suppliers.

This White Paper focuses on the importance of having an effective governance model in place to manage the outsourcing agreement and also make sure it continues to align with business needs for relationship sustainability.

# Guidelines for IT Outsourcing Governance

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Many organizations already have a governance model in place for their internal IT organizations. The value of a good governance model comes from the communications process put in place as much as it does from the model itself. There are many models which can be used for various types of services delivered by the internal IT function. These models provide a range of ways in which IT decisions are made including Business Monarchy, in which the business provides direction and ultimate decision making, and Business/IT Duopolies where the IT function and the individual strategic business units (SBU's) jointly determine how IT capital and resources are spent.

If your organization already has an effective governance model in place, that is a very good basis for your outsourcing governance model. The model will need to be adjusted to take into account the fact that an external group is providing IT services, but it is a great starting point for the critical discussions to ensure success in outsourcing.

The discussions on outsourcing models need to focus initially on making sure all parties know the answers to two key questions:

- 1** Why are you outsourcing?
- 2** What are you outsourcing?

These seem like simple questions, but the answers are often difficult to determine.

In the early days of outsourcing, many organizations tried to start with the “What” rather than the “Why”. They had a problem area and decided that someone else had more experience handling the problem than they did. This led, as we all know, to some very unsuccessful outsourcing agreements. Today’s problems are a little more complicated because there are few organizations that have not outsourced at least some part of their IT function. Having an outsourcing agreement in place leads organizations to expand the current agreement or conclude that because it worked well in one area it will work well in another area.

Even though you may have experience (either positive or not so positive) in outsourcing one or more areas, it is always critical to start the outsourcing discussion with agreement on the goals of outsourcing.

- Why are you Outsourcing?

For many years, the most common reason companies list for outsourcing is cost reduction. While cost cutting is an important reason to consider outsourcing, it is by no means the only reason and often an exclusive focus on cost cutting or unit pricing does not lead to a deal that is optimized or effective.

The following are some of the most commonly listed reasons for considering outsourcing:

- Cost Cutting
- Enhanced Capability
- Shedding Non-Core Functions
- Speed of Execution
- Staff Augmentation
- Geographic Expansion
- Improved Customer Service
- Flexibility in Staffing

It is often the case that an organization has multiple reasons or goals for outsourcing, and often these goals are in conflict. For example, improved cost cutting and improved customer service can each be achievable goals of outsourcing, but if both goals need to be achieved, it can be more of a challenge to construct an outsourcing deal that meets both objectives. This is precisely why a good governance model provides value to the organization by helping all parties understand the goals and constraints of the agreement.

- What are you Outsourcing?

The next step in creating an effective outsourcing governance model is to understand what is being outsourced. There are a lot of options from outsourcing the entire IT function to outsourcing specific components. Overall, these can be placed into three broad categories: Infrastructure, Applications and Support.

Within each of these categories, an organization can choose to outsource a variety of functions or capabilities and the organization also has options on the scale of the outsourcing arrangement. Many organizations are moving to outsourcing of their data center operations and this can range from using Software as a Service (SaaS) (infrastructure is part of the monthly charge) to co-location (the physical facilities are outsourced, but management of the infrastructure remains with the company) to managed services (the entire infrastructure operations (data center, network management, telecommunications and in some cases even disaster recovery) is managed by the outsourcer).

There are valid business reasons for choosing the functions and scale of outsourcing, and part of that decision process should be the governance model. Many times, companies view the governance model as an afterthought or something that is assumed to be handled by the service provider; however, NET(net) has found that outsourcing agreements which have a solid governance model have a much higher rate of success.

## IT Outsourcing Governance Tools

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In order to facilitate the development of an IT outsourcing governance model, we need to keep in mind that multiple models may be required by the outsourcing situation. For example, if you are outsourcing a project, you will need to decide how that project is managed and also how it is integrated into your existing IT environment. This brings us back to the goal your organization has for the outsourcing engagement. If a goal is to complete the project in the minimum amount of time and you do not intend to support the resulting application internally, then the outsourcer can manage the project and your organization can provide oversight. If a goal is to improve the technical capability of your IT staff, then you will need to extend the time frame for project completion and include some of your internal staff in the project team. In that case, will the outsourcer manage your staff or will there be dual management of the staff? Either model will work, but success depends on making sure both organizations understand the goals and impact those goals will have on other factors that are often measured (time, cost, and scope).

In the case where your company is outsourcing an entire effort (such as managed data center services), the governance model will focus more on business outcomes and less on how the service is provided and managed. We often see a tremendous amount of effort directed toward service levels and penalties, which are critical metrics for an outsourcing agreement; however, they should not be the only metrics and they should not be the focus of governance.

Organizations can get caught up in the details and lose sight of the overall goals or outcomes and a well designed and agreed upon governance model can be an effective tool for ensuring success in an outsourcing arrangement.

In addition to service levels, we always recommend supplier scorecards as a means of providing a simple and effective governance approach. The classic stoplight indicators (Red – Yellow – Green) for key metrics can provide an overview of the entire agreement and can highlight the goals and outcomes in priority order. One

item often missed in a supplier scorecard is customer satisfaction and the ability to communicate well. To be sure, these factors are more difficult to measure quantitatively, but they are always well known by the people who interact with the outsourcer and are always a good indicator of overall success.

One additional tool that helps ensure outsourcing agreements remain effective is a formal communications plan. This is separate from the governance model and provides a framework for how communications is handled between the two organizations. Most outsourcing agreements have some type of communications plan such as regular review meetings. These meetings usually provide updates on status, but can also be used to address changing goals and needs. The daily, weekly and monthly meetings are often focused on operational issues, which is appropriate. The quarterly and annual meetings need to focus on looking forward and improving the relationship. If not well managed, these meetings can become sales tools for the outsourcer rather than a venue for serious discussion about the current and future health and scope of the agreement.

## Putting it into Practice

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NET(net) has offered some guidelines and tools that we have found effective in helping organizations make sure their outsourcing agreements are well managed and retain their value throughout the life of the agreement. Keep in mind that while each outsourcing situation and agreement is unique there are some common factors that help ensure success. These factors, such as determining why you are outsourcing before deciding what to outsource, can be used to create an effective framework for your outsourcing agreement. Once you have decided the “why” and the “what”, make sure to engage in the critical discussions with your suppliers on the most appropriate governance model for long term success. The one thing common to all outsourcing agreements is that the business environment and even the goals of the agreement will change over time and by using these tools and techniques your organization has a much better chance of making outsourcing a success.

If you would like more information on how NET(net) can help you assess or create an effective and sustainable governance model for a new or existing IT outsourcing relationship(s), please contact us at [info@netnetweb.com](mailto:info@netnetweb.com).