Briefing 2:

From the coal face

THE REALITY OF OUTSOURCING – A PERSONAL VIEW

A leading global automotive supplier

Briefing two of EquaTerra's 8-part Guide to Sustainable Sourcing, looks in detail at one client's outsourcing experience. The narrative is reprinted with kind permission of a leading global automotive supplier and provides insight into the key issues that face any company wanting to outsource.

The Company described in this article employs nearly 45,000 people in 30 countries. The Company's principal customers include many of the world's foremost original equipment manufacturers of vehicles and industrial products, and aftermarket retailers and wholesalers.

DECISION TO OUTSOURCE

"After a few relatively unsatisfactory years of running a shared services operation that had been stretched by acquisitions, the Company took a long hard look at shared services as a part of an overall corporate cost cutting strategy. As a result, and with support from senior management, the Company embarked on what would become a multi-year outsourcing arrangement utilising service delivery centres in four different countries.

It was not the largest outsourcing deal, but it was unique in a few ways. At the time the Company contracted for its outsourcing deal it was operating under Chapter 11 bankruptcy protection. In addition, it was a U.S. presidential election year (2004) when every other political television commercial talked about jobs leaving the country and sending work offshore.

PLANNING FOR OUTSOURCING

Between 2000 and 2004 the Company set out to improve its internal shared services environment, and this was key to being able to execute a "lift and shift" of its chosen operations to an outsource provider. The "lift and shift" model contemplates taking existing processes and transitioning them to a provider, initially, prior to any major process re-engineering. Outsource service providers work in a very strict rules-based environment, so anything a company can do to drive consistency in practices, to whatever level possible, will help the transition and keep transition costs down.

The initial draw of outsourcing is a significant downward step-change in cost. Most companies do not come to the table on an outsourcing deal unless there are cost savings to be had. Had the Company not spent the time working on process improvements, customer service, stabilisation of the control environment and creating a set of metrics on which to manage the operations, the cost involved in outsourcing would have been dramatically higher in the initial years, and the business case for outsourcing would have been far less favourable.

HR PLANNING: A DELICATE BALANCE

Outsourcing by its very nature means the loss of jobs. In many cases, an outsource provider will offer positions to some members of an existing staff in order to leverage the knowledge at the company and help to mitigate the loss of "tribal knowledge", but in other cases an entire staff is displaced. Either scenario requires some focus on managing the human resource element throughout transition. The strategy starts even before contract negotiations begin by engaging human resources, legal counsel with a speciality in employment law, and some level of corporate communications staff.

The human resource element unfolds in three phases: planning, post-announcement and exit. In the planning stage decisions are made as to the make-up of the HR plan in an outsourcing scenario. Will some staff be offered positions with the outsource company or not – this is generally a mutual decision between the client company and the outsourcer.

If no offers are to be made, a legal arrangement called secondment is often considered. In this case, key employees are retained and kept on the client company's payroll, but are effectively managed by the outsourcer. Finally, as in most outsourcing cases, a good severance plan must be crafted to strike a balance between keeping employees motivated during the necessary transition period, and the cost/risk profile their departure could create.

Most companies find a strong severance/retention package is necessary to keep employees motivated while they "teach someone else their job." The transition process, by its nature, has staff dealing with the impending loss of a job which puts them all at different places in the cycle of dealing with grief and loss. During this time, however, a company needs these staff members' support and focus to assist with the transfer of knowledge, as well as their motivation to keep the normal day-to-day activities up and running.

A delicate balance of severance and retention benefits, plus wellness activities and some sense of normality in the work environment, help to keep staff as positive and motivated as possible considering the circumstances. The sensitivity of the vendor's staff conducting the transfer of knowledge is also important.

In the end, the Company found most staff very cooperative and as positive as one could expect, given the situation. Most moved on to new jobs, either within or outside the company. Some took it as an opportunity to make a change and pursue an entirely different avenue. The keys to the HR component of a deal are to measure twice, cut once. Plan, plan, plan and then plan some more and when you have done doing that, over-communicate all relevant aspects of the deal, its timing, how it will impact staff and most important, what is in it for them.

At this point, there is really only one motivation to stay… money. This decision is personal to staff members and their first instinct will be to plan for what comes next. It is the management team's job to anticipate questions and be as open and honest about the transition period as possible. This up-front work and planning will help alleviate bumps in the transition process… at least from an HR perspective.

THE BIGGER PICTURE: PROCESS TRANSFORMATION

Transformation was not the carrot that caused the Company to send request for proposals (RFP's) to various outsource providers; it was not what we initially considered in determining whether to go forward with the selection process; it was not what we spent most of our time on, during the initial phase of paring down vendors. It was, however, something we came to focus on more as the numbers started to crystallise and our focus changed from short-term to long-term.

Process transformation is the engine that keeps outsourcing going. It's difficult to cultivate Six Sigma process experts internally; and costly to staff full-time project and process improvement resources. "It's not what we do," is something I've heard a number of times during our contracting process. The Company realised that if we wanted a best-in-class shared services operation, we either had to expend the capital and resources to build and develop that core competency internally, or we had to seek help. The Company decided that it was not in the business of performing processing activities. It was in the business of making auto parts and that is what it wanted to focus its resources on.

Going to an outsourced provider allowed the Company the flexibility to tap into quality and process experts as needed, without having to staff them on a full-time basis. It allowed for flexibility in project staffing. In general terms it gave the Company a virtual bench to put into the game when projects came up, but the added flexibility of not paying for them when the project was complete. While the Company is focused on improving its business and cutting costs to remain competitive, a third party provider is focusing on improving business processes.

These business process improvements have a two pronged benefit. First, they allow the outsourcer to provide a contractual year-over-year fee reduction. Second, they provide upstream efficiencies elsewhere in the Company by replacing an inefficient process with one optimised for efficiency (at least within the constraints of your ERP or legacy system).

GOVERNANCE

Once the deal is done, and processes begin to stabilise, having a strong governance organisation and a set of governance operating procedures will keep the deal on track. In the Company's model, the governance organisation is comprised of a lean layer of management, paired with like management at the vendor.

The governance organisation can be put together several ways, but the way the Company did it is as follows: a global lead, a regional lead in North America and Europe, a finance manager, a project manager and a supply chain resource manager for contract changes. This is augmented by legal counsel from a firm specialising in outsourced deals, which we use as needed for contract questions and clarification. The legal counsel was also party to the original contracting process.

Governance is first about running the operations, but also about resource deployment, project prioritisation and relationship building. The governance organisation must work together on both sides in order to maximise the chances for success of the initiative. One piece of valuable advice we received from our legal advisors and consultants throughout the contract period and into the transition stage was that you need not be afraid to have difficult discussions or to say "no" to each other once the contract is signed. The difficult discussions generally revolve around additional fees for services or the scope of services provided.

Depending on the level of diligence during the contract phase, and the level of familiarity with the contract at the client company, these discussions can either turn into long drawn out discussions about fees and compromise, or can turn into short discussions if 1) the services are clearly covered and you can prove that by referring to contract wording, or 2) the services are really incremental and you can agree on an adjustment. Either way, the key is being knowledgeable in your contract verbiage, which starts with being diligent in the contracting phase.

Although we are relatively new to the world of outsourced services, the experiences described here are real, recent and were either lessons learned before, during or after the transition period. So take these tips to heart, and if you think outsourcing is an option also consider hiring outside help to contract a deal. There are legal and consulting firms specialising in all types of outsourcing deals. Whether your focus is outsourcing for HR, F&A or IT there are legal and contractual pot holes that a seasoned expert can help you navigate.

Our consultants and legal advisors paid for themselves versus trying to do the deal without them. So if you think outsourcing is right for you, get that senior management support, build your team, find qualified consultants and legal counsel, pick a provider and hold on. It's a difficult process, but the flexibility it can provide, combined with the potential for significant cost reductions, may be enough for you to jump into the fray. If you do, best of luck."