MANAGING THE OUTSOURCING PROCESS

Research Assistant C. Cüneyt ARSLANTAŞ

I.U. School of Business Administration

Introduction

Outsourcing is a management strategy that helps organizations to focus on their core competences in order to gain a competitive advantage and to provide non-core functions or activities with efficient vendors. Outsourcing represents a sophisticated relationship between the organization and the vendor. Outsourcing process helps the organization to find its outsourcing vendor. Outsourcing process, which should include nine steps, is very, impotant in order to select the right vendor for the organization. (Arsiantaş 1999):

STEPS	OUTSOURCING PROCESS
1st step	Requiring Outsourcing
2nd step	Defining Organization's Needs
3rd step	Making Outsourcing Decision
4th step	Evaluating Outsourcing Strategy
5th step	Formulating Request for Proposal
6th step	Evaluating Vendors
7th step	Selecting The Best One Among Vendors
8th step	Negotiating Contrast with The Vendor
9th step	Building and Managing Effective Relationship with The Vendor

Exhibit 1. Outsourcing Process (Arsiantaş 1999)

A-Requiring Outsourcing

There are many reasons for an organization to consider outsourcing. Organizations require outsourcing in order to (Arsiantaş 1999);

- *achieve strategic goals*
- *reduce costs*
- *reduce investment expenditures*
- *improve core competence*
- *reduce risk*
- *downsize and increase flexibility*
- *accelerate reengineering benefits*
- *access the world class capabilities*
- *manage out of control function*
- *access to improved technology*
- *transfer assets*
- *increase quality*
- *redirect resources*
- *manage financial resources available.*

B-Defining Organization's Needs

When organizations require outsourcing, they should define their organizations' needs. Especially, top managers determine which functions or activities should be completed internally and which by a vendor or vendors. There are two important criteria for deciding what functions to outsource:

- The strategic importance of the functions.
- In-house personnel's ability to perform the functions.

Functions or activities that are not strategic to the organization's core competence and that the personnel cannot perform cost effectively are excellent candidates for outsourcing. Conversely, functions that are strategic to the core competence and that the personnel can perform cost effectively should be kept in the organizations because of their strategic importance for organization's future (Gerston 1997).

C-Making Outsourcing Decision

Outsourcing initiative is a very important process that influences all organization's future. According to this, top management should consider on this subject carefully. Top management should decide whether it is better for the organization to outsource its functions, determine which functions are completed by vendors, consider how well organization's culture will support an outsourcing decision (Laabs 1993). In addition to this, three factors that directly influence the top management's decision are the number and the capability of outsourcing vendors, advances in technology, and competition (www.corbettassociates.com/main/resource/research/preview/outrev.html).

D-Evaluating Outsourcing Strategy

After making outsourcing decision, top management should evaluate the outsourcing strategy. Top management initiative is so important for a successful outsourcing application. When top managers evaluate outsourcing strategy, they should consider on the organization's core competences, the barriers raised by the corporate culture, the cross-functional impact, goals they want to achieve from outsourcing, kind of relationship with a vendor, the personnel issues (www.outsourcing.com/news/calendar.htm); make sure that organization's goals for outsourcing are clear; decide whether it is better for your operation to be centralized or decentralized; look at outsourcing over the short and long term (Laabs 1993).

E-Formulating Request for Proposal

Request for proposal (RFP) is a very important process in outsourcing process when selecting available vendor for organization. Using an RFP will help keep the scope of the project focused and contained, generate more realistic and favorable pricing and terms from each of the vendors, inform the organization of the range of technology and expertise available, prevent vendor lock-in, and keep vendors honest throughout the process (Moore and Van Ailen 1998).

RFP should contain severai main sections (Grupe 1997):

- *Overview:* This section describes the objectives for the outsourcing project and lists the reasons for creating the RFP.
- *Background:* This section describes the organization's business, mission, locations, and organizational structure.
- *General requirements:* This section, bften the largest section of the RFP, describes guidelines for proposals, a time schedule for the evaluatiori, contract terms, and the logistical requirements for the project.
- *Required service levels:* This section is used to describe the expected quality results.
- *Selection method:* This section describes the criteria and method for choosing the outsourcing vendor. A partial list of possible selection criteria includes vendor stability, management organization, flexibility, facilities, service capabilities, training, price, implementation plan, and references. The selection criteria should be ranked by priority.

F-Evaluating Vendors

This process begins as vendors respond to the RFP with their own proposals. If many vendors respond to the RFP, a cursory evaluation of the responses may be sufficient to eliminate marginal vendors. The most important thing is to determine the vendor's comprehension of company requirements and the quality of the proposed solution. This evaluation include severai steps (Grupe 1997):

- *Reviewing proposals,* when organizations evaluate vendors' proposals, they consider on these key questions:
  - ❏ Does the proposed solution meet the organization's objectives described in the RFP?
  - ❏ Does the vendor have the experience and resources to implement the solution?
  - ❏ Does the vendor have a reasonable implementation or transition plan for phasing in the outsourcing service?

❏ Does the vendor's personnel have an adequate knowledge, skill and ability to provide the required support?

❏ Will the vendor's personnel exercise confidentiality regarding sensitive issues such as business objectives, technology plans, and business data?

❏ Is the vendor stable financially and managerially?

❏ Does the vendor have some knowledge of your business and can its people adapt to the types of personnel in the organization?

❏ Does the vendor handie smoothly and to each party's mutual benefit when contractual problems have arisen?

❏ What is the vendor's reputation for meeting service commitments?

❏ Does the vendor have positive references?

❏ Does the vendor have resources to remain competitive in the outsourcing arena?

❏ Does the vendor have an appropriate price strategy in return for its given services?

Proposals should be evaluated with an evaluation matrix (Exhibit 2.) containing the evaluation attributes, their weighting, and a column for each vendor. Each vendor's solution is ranked for each attribute on a scale from 1 to 10. These scores are then adjusted by the appropriate weighting factor and added to produce an overall company score.

108

Category/Attribute	Weight	Vendor 1		Vendor 2	
		Raw Score	Weighted Score	Raw Score	Weighted Score
Comoany					
Reputation	A	B	AXB	C	AXC
Financial Stability					
Quality Programs					
Flexibility					
Location					
Staffing Ability					
RFP Compliance					
Employee Practices					
Total Company			*******		*******
Services					
Comprehension					
Solution					
Methodology					
Management					
Technology					
Implementation Plan					
Total Services			*******		*******
Price					
Price Score					
Risk/Reward					
Total Price			*******		*******
Total Score			*******		*******

Exhibit 2. Vendor Evaluation Matrix (Grupe 1997)

- *Visiting the vendor and checking references,* this is the most effective way of gaining insight into the vendor's practices.

G-Selecting The Best One Among Vendors

Carefully following the selection process just described simplifies final vendor selection, because it is likely that one vendor more clearly meets requirements than others. There are many factors to be taken into account when selecting a vendor to provide outsourcing services. Price is an important consideration but lower price alone may not provide the highest value (Grupe 1997). This can lead to the downfall of a project. A good vendor should have an adequately staffed, financial, customer-oriented organization with a long range business plan, explicit disaster recovery provisions and be making strategic use of its resources (Martinsons 1993). Vendor selection criteria also includes (Platt 1996);

- combined strength that is complimentary to the organization
- mutual commitment
- mutual trust
- compatibiiity-a cultural fit

H-Negotiating Contract with The Vendor

After a vendor selected, a contract setting specific measures for performance and detailing the policies and procedures which will govem the relationship must be negotiated. It is worth considering whether such an contract will improve the organization's probability of business success (Martinsons 1993). The contract is the only mechanism that establishes a balance of power in the outsourcing relationship. In other words, the contract is the number one key to a successful outsourcing relationship (Lacity and Hirschheim 1993). The success of outsourcing contract is fundamentally based on the ability of the involved organizations to place themselves in a win-win situation (Rubin 1997). Good contracts are the foundation of good relationships (Lacity and Willcocks 1999).

The main issues that the contract should include service-level agreements, reporting, determination of service adequacy, staffing and scheduling, implementation, location, equipment, termination and renegotiation, payment

and costs, change service orders (Grupe 1997). Following are some of the key issues while making an outsourcing contract:

- *Thoroughness* and *Comprehensiveness,* parties understand and agree to the terms and obligations. The contract should be as comprehensive as possible, defining all pertinant issues that must discuss the obligations of each party, costs, duration, terms, and conditions (Judenberg 1994).

- *Flexibility,* the contract should provide flexibility for future situations. It is easy to anticipate changes in a short-term contract, but it is not easy to say same thing for the long-term contract (Klepper 1999). Flexibility is a necessity in any long term relationship as technology, personnel, and business objectives change over time. Flexibility also enables the supplier to add new services to the relationship (Samuel 1999).

- *Duration,* although the vendor wili require a minumum time frame to make the effort worthwhile, there also needs to be some escape clause in case the effort does not work out as envisioned. This can be accomplished through objective criteria for termination (where possible), payments to the vendor to compansate for early termination, and lead time for termination (Grupe 1997).

- *incentive,* the vendor should have an incentive (ex. share in the benefit) to improve the stability of the systems. Such improvements can provide benefits to the organization through better customer service or reduced cost of processing (Judenberg 1994). Most successful outsourcing relationships include vendor incentives for performance (Lacity and Willcocks 1999).

I-Building and Managing Effective Relationship with The Vendor

How does the organization make its outsourcing relationship a source of value that drives ongoing benefit and asset to the organization and the value chain? That's the overriding guestion every organization consider outsourcing

wants answered (Samuel 1997). Critical factors for successful outsourcing relationship are(Tarsh 1998):

- creating a shared vision for the outsourcing and reflecting this vision in the contractual arrangements
- mutual objectives
- establishing a clear contract
- including effective performance measures and maintaining control
- building a clear communication mechanism
- developing a clear contingency plan.

It is very necessary for ongoing relationship to maintain healthy collobaration between the two parties and outsourcing contract between the organization and the vendor is doomed to failure if an environment is not created for the relationship to succeed. Mutual trust is so important in these arrangements (McFarland 1997).

Conclusion

Following the steps presented in this article will help the organizations build a successful outsourcing with the vendor. Organizations should follow these nine steps when they think outsourcing. Selecting an appropriate vendor for your organization and preparing a clear contract are critical to success of outsourcing relationship. Successful outsourcing starts with the contracting process. The contracting process is educational and can be seen as a road map to a successful, ongoing relationship. Right planning, careful selection of partners and good sound business reasons for outsourcing will ali help the organization to move towards achieving its goals.

References:

Arsiantaş, Cem Cüneyt (1999), "Yeni Bir Yönetim Stratejisi Olarak Dış Kaynaklardan Yararlanma ve İlaç Sanayiinde Faaliyet Gösteren Firmaların Dış Kaynaklardan Yararlanma Uygulamaları", Yüksek Lisans Tezi, İ. Ü. İşletme Fakültesi.

Gerston, Joel (Spring 1997), "Outsourcing in Client / Server Environments", Information Systems Management, 14, 74-78.

Grupe, Fritz H. (Spring 1997), "Outsourcing The Help Desk Function", Information Systems Management, 15-22.

Judenberg, Joseph (Fail 1994), "Applications Maintenance Outsourcing", Information Systems Management, 34-38.

Klepper, Robert (1999), "When Partnerships Make Sense", www.outsourcing-academics.com/html/acad10.html

Laabs, Jennifer (October 1993), "Successful Outsourcing Depends on Critical Factors", Personnel Journal, 72, 51-60.

Lacity, Mary C. and Rudy Hirschheim (Fail 1993), "The Information Systems Outsourcing Bandwagon", Sloan Management Review, 73-85.

Lacity, Mary C. and Leslie P. Willcocks (1999), "The Elements of Success", www.outsourcing-academics.com/html/acad2.html

Martinsons, Maris M. (1993), "Outsourcing Information Systems: A Strategic Partnership with Risks", Long Range Planning, 26, 18-25.

McFarland, Keith R. (May/June 1997) , "Outsourcing: Reading The Fine Print", TMA Journal, 17, 41-44.

Moore and Van Ailen (1998), "Doing Outsourcing Right", 1-800 Support Doing Outsourcing Right, www.888support.com/Reference/out_right.html.

Platt, Rodney K. (June 1996), "Outsourcing the HR Function", ACA News.

Rubin, Howard A. (Spring 1997), "Using Metrics For Outsourcing Oversight", Information Systems Management, 7-14.

Samuel, Peter Bendor (August 1999), "Slant on Success", Outsourcing Journal, www.outsourcing-journal.com/issues/aug1999/.

Samuel, Peter Bendor (July 1997), "It Ali Begins with a Plan", www.infoserver.com/July1997/html/everest.html.

Tarsh, Simon (1998), "Managing the Outsourcing Relationship: A Shared Vision produces Greater Rewards", www.outsourcing.com/howandwhy/trends/.

"Outsourcing: The U.S. Business Revolution", www.corbettassociates.com/main/resource/research/preview/outrev.html.

www.outsourcing.com/news/calendar.htm.