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UNISYS

Compared with traditional IT outsourcing, business process outsourcing can mean greater risk — and greater reward. Here's how to avoid slip-ups and score high.

Diving Into BPO

Five Mistakes and How to Avoid Them

Eric Schoeniger

Outsourcing is like diving into a swimming pool. Once your feet leave the platform, you're committed. It's not the time to discover the water is only a few inches deep.

That's particularly true for business process outsourcing (BPO) — the offloading of entire business functions, as opposed to single aspects of IT. Such functions can be as focused as payroll or as broad as the entire HR practice. They aren't core competencies — or you wouldn't outsource them — but they are certainly crucial to your operations.

Handing off such business-critical processes involves a certain amount of risk. The outsourced administration of employee benefits may not give you any direct competitive advantage. But you're certainly at a disadvantage if benefits administration grinds to a halt, or even if it's a source of employee dissatisfaction.

Still, a growing number of organizations are taking the BPO plunge. Nearly half of all organizations outsource at least one business process, says Gartner Dataquest (San Jose, Calif.). Worldwide, spending on BPO will almost triple from $107 billion in 1999 to $302 billion in 2004, a compound annual growth rate of 23 percent. That makes BPO one of the fastest-growing areas of technology services, expanding at more than twice the rate projected for overall IT spending.

That's no surprise to organizations reaping the benefits of BPO. Because BPO involves not only the IT infrastructure but also the workflow, talent and best practices that support the function, there's tremendous opportunity to reduce costs and improve efficiency. BPO enables organizations to get out from under the pain of fixed overhead, the cost and hassle of building IT infrastructure, and the responsibility of recruiting, training and retaining staff. It also means a single point of accountability for re-engineering and continuous improvement.

But for every BPO success story, there's a cautionary tale of outsourcing gone awry. Before you place your key processes in the hands of another company, learn from the most common BPO blunders. It could mean the difference between a costly, difficult exercise and a strategic move that delivers measurable business benefits.

Mistake #1: Not Knowing Why

"The number one mistake companies make is not knowing why they want to outsource," says Brad L. Peterson, a partner in the IT and outsourcing practice of Mayer, Brown & Platt (Chicago) and co-author of *The Smart Way to Buy Information Technology* (AMACOM Books). "You need to have a clear picture of what you want to achieve."

Rebecca Scholl, senior analyst for Gartner Dataquest, agrees: "There are numerous reasons to outsource, and it's important to understand upfront what you want out of it. Do you want to reduce costs? Do you want to increase service levels? Do you have a talent shortage? Do you want to integrate new technology?"

In broad terms, BPO should create value — value for your customers, value for your enterprise, value for your shareholders. "BPO can create value by focusing internal resources on more strategic activities," says Scholl. "Instead of spending its time on payroll, benefits and personnel administration, for example, your HR department could be focused on compensation strategy, organizational management and human capital development."

BPO can also create value through integration — between HR and finance, say, or between procurement and finance. It can provide access to technology — and the talent to support it — that your organization couldn't otherwise cost-justify. And it can add value through analytics and business intelligence, says Scholl, such as relevant reports that can help improve the way you run your business.

Barclays and Lloyds TSB, two of the United Kingdom's leading retail banks, created tremendous value by outsourcing check processing. In fact, the banks took BPO a step further, partnering with Unisys to create a new check processing business, Intelligent Processing Solutions Ltd. (iPSL). The firm handles check processing for Barclays and Lloyds TSB, which share the risks and rewards with Unisys. It also offers related services to other organizations, resulting in a new revenue stream for the partners.

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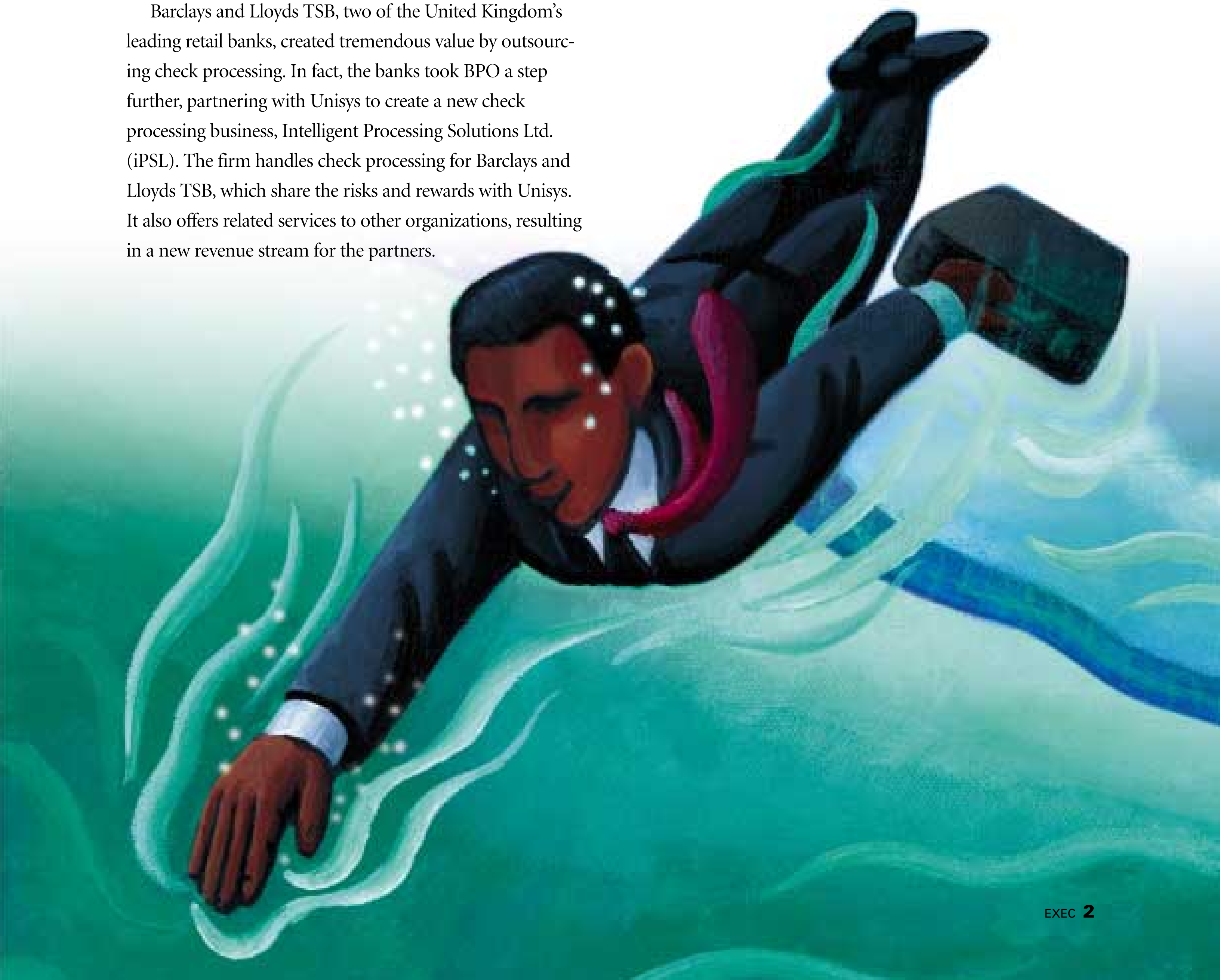


SLAs: 10 Questions for Outsourcers

A service-level agreement (SLA) defines the level of performance your outsourcer promises — and your rights should it fail to deliver. But the best time to address problems is before they occur. Don't sign the contract until you've asked these questions:

1. **Which service levels will you measure?** A good SLA aligns incentives for outsourcer and client. For example, a fixed-price deal gives incentive to the outsourcer to cut corners, whereas the SLA should focus on quality.
2. **What will you measure for each service level?** Define the service level precisely. Is a system considered "available" if the server is working but the application has crashed or the local-area network is down?
3. **How will you measure?** There must be a process for measuring performance — from software that monitors system availability to user satisfaction surveys.
4. **What is the measurement period?** Common intervals are monthly or quarterly. But does that cover 24x7 or only 9-to-5?
5. **How will you report results?** The SLA should define exactly what information will appear in performance reports.
6. **At what level will you perform?** This isn't the first question, because the answer is meaningful only when you know what will be measured and how. An SLA can include both minimum and target service levels. Missing minimum levels means breach of contract; missing target levels might mean some form of make-good. Remember: Don't put off discussions of service levels until later in the relationship; hammer them out before you sign.
7. **Will service levels change?** Long-term, large-scale agreements can specify that service levels increase over time.
8. **Will the SLA include service-level credits?** Following a service-level failure, the outsourcer may be required to write a check or give a credit toward future services.
9. **Will the SLA include service-level bonuses?** Bonuses for exceptional service levels can foster a spirit of partnership in the pursuit of mutual goals.
10. **When does failure to meet service levels allow termination for cause?** Generally, agreements can be terminated for cause upon a material breach such as a severe service-level failure. But the SLA should be as specific as possible.

Adapted from "Ten Key Questions for Developing Effective Service Level Agreements," by Brad L. Peterson, OutsourcingJournal.com, *October 2001. Used by permission. Peterson is a partner at Mayer, Brown & Platt.*

Key to the venture's success was a firm understanding of what the banks wanted to achieve, says John Little, director of U.K. regulated sales and service for Barclays. "You don't want to outsource a problem," he advises. "You need to have your house in order first. You need to understand why you're outsourcing and be clear about business objectives."

Mistake #2: Not Performing Due Diligence

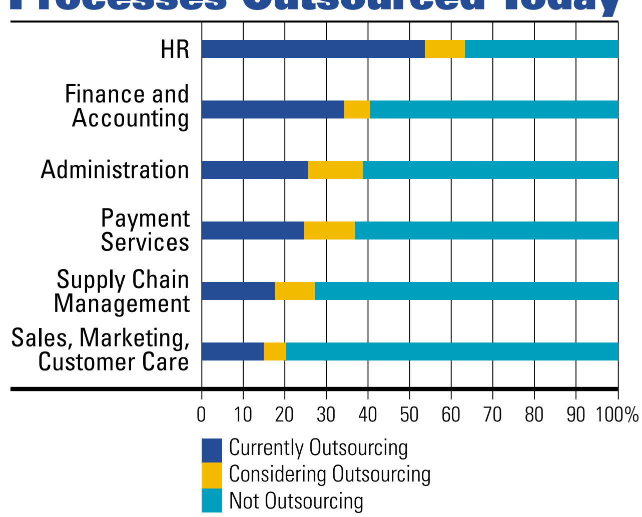
Eighty percent of companies expect to outsource at least one IT function by 2003, reports META Group (Stamford, Conn.). Yet 70 percent of IT managers lack experience making outsourcing decisions.

So it behooves an organization to develop a detailed, stepwise approach to reviewing potential outsourcers. Experts agree that the three most important criteria to look for are a proven track record, technical excellence and the ability to deliver process improvement.

"In evaluating an outsourcer, ask whether it possesses both the technology and business expertise to make your business functions work more efficiently," suggests Hae Han, vice president of business process outsourcing, global outsourcing, for Unisys. "Does the company have sufficient enterprise computing strength? Does it have global reach? Does it have best-of-breed IT and business skills in the particular function to be outsourced? If I am a transportation company, has the outsourcer done this for transportation companies before and been successful?"

Most important, talk to existing customers. Try to speak

Processes Outsourced Today



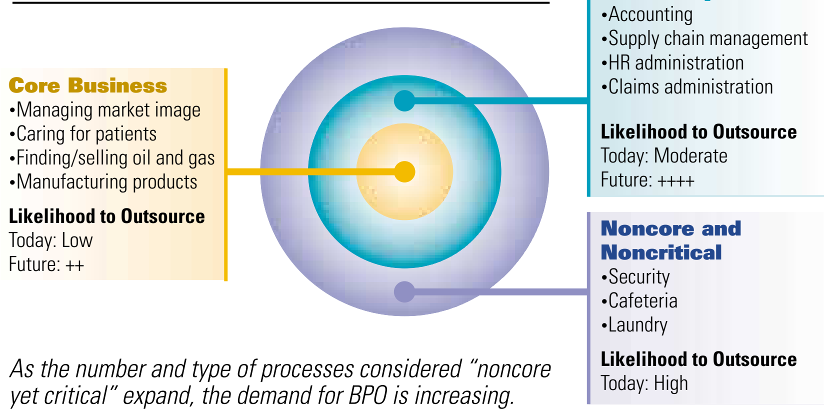
HR, finance and administration are among the most popular business processes to outsource.

Source: Gartner Dataquest.

with at least five, advise experts, and try to speak with organizations in your industry. Find out what problems they encountered and, more important, how they resolved those problems. Get opinions on the outsourcer's strengths — and weaknesses. And find out why the organizations selected that outsourcer over the others they evaluated.

"You want to find out how long the outsourcer has been providing the service, what type and size of clients they're working with, what kind of volumes they handle, and what types of systems they use," says Bruce Berkey, vice president of finance, global business services, for Ingersoll-Rand (Woodcliff Lake, N.J.), a maker of industrial equipment.

Which Processes to Outsource



As the number and type of processes considered "noncore yet critical" expand, the demand for BPO is increasing.

Source: Gartner Dataquest

Ingersoll-Rand outsourced its back-office travel and expense processes to Unisys to centralize activities that were being handled by more than 40 internal accounting groups, and to establish a consistent approach to managing travel across the company. "We don't have that expertise in-house," explains Berkey. "By outsourcing, we avoid the cost of maintaining the talent and trying to keep up with the latest technology."

Berkey also recommends a site visit. "We visited Unisys twice, because we wanted to make sure this wasn't a sideline business, that they had the right facilities and the right caliber of people running it," he says.

Finally, due diligence also applies to your own organization. "You need to measure internal performance before you outsource," says Scholl of Gartner Dataquest. "If you don't do benchmarking beforehand, how will you know if you are achieving benefits by outsourcing?"

Mistake #3: Not Having a Transition Plan

Satisfaction levels are lowest in the first year of outsourcing, suggests research by Gartner Dataquest. They improve in the second year, and improve again in the third year. But "the transition period is where most of the pain points are," says Scholl.

That makes sense, because in the first year you're still migrating systems, you may be re-engineering processes, and most significant, your people are still adapting to a very different environment. That's particularly true for the employees responsible for the function before it was outsourced. In many cases, some of those people become employees of the outsourcer. But those who remain on your staff may try to hold onto old roles, unintentionally undermining the process.

"The transition period is the riskiest and most uncertain time," says Peterson of Mayer, Brown & Platt. "You're trying to transfer knowledge, employees are dealing with the 'me' issue, and you're handing off the function to a company that doesn't yet know exactly how to run your particular operation."

What you need are a cross-functional transition team and a detailed transition plan. One person on that team should be responsible for day-to-day details, and that individual should have a counterpart on the outsourcer's side. The outsourcer should also be the source of the transition plan, using proven methodologies that are flexible enough to adapt to your needs.

"A transition plan is as important for the outsourcer as it is for you," says Ingersoll-Rand's Berkey. "That was key to the success of the project. We all worked toward a common objective, because it was well-defined at the beginning."

Bear in mind that a large outsourcing project can be a complex, long-term undertaking. You can't expect it to be trouble-free. But you certainly can expect the outsourcer to respond quickly and appropriately to problems, and to provide constant improvements over time.

"There were some initial technology difficulties," says Little about Barclays' relationship with Lloyds TSB and Unisys. "But you have to expect some hiccups. That's why you need to be clear about requirements." Following the transition, Little reports, "the technology program is on

The Value Proposition of Managed Network Services

Today, organizations feel increasing pressure to control IT costs. The reason: Many are struggling to maintain profitability.

One way to reduce costs is to outsource those IT operations that do not provide a competitive advantage. More and more organizations are turning to managed network service (MNS) providers to oversee and run their day-to-day internal IT functions, such as management and support of distributed desktops, servers and networks.

By doing so, businesses and governments are receiving the same type of service or higher for a lower price than it would cost them to handle operations in-house. At the same time, they are easing the strain on their own IT staff and focusing on tasks that further strategic business objectives.

"Typically, a managed network service provider will lower your costs 15 to 20 percent," says Brett Husselbaugh, principal in the MNS service at Unisys. "Plus, this option can provide a predictable monthly cost model so you can plan your budget better and not have to worry about a spike in IT costs."

An organization with a highly skilled IT department usually does not have a team of personnel who have the expertise to customize internal operations to ensure that the organization is getting the most from its IT investment.

An MNS provider possesses this level of expertise and is able to leverage integrated processes, common toolsets and a shared-services infrastructure to reduce the cost of service. At the same time, it can predict future costs, because it anticipates your operational requirements.

The City of Chicago, for example, has embraced managed network services to improve the running of the government's business. In the late 1990s, finding itself behind the technology curve with an IT staff that could not support the needs of 10,000 users, the city chose to outsource key IT functions. Today, a Unisys MNS team handles the city's network, servers and desktop management, and helps with desktop configuration and staging, asset management, maintenance, remote desktop management, helpdesk support, training services and maintenance.

"[Using managed network services] has allowed us to deliver the different types of services that we need without necessarily having to manage them," says Chris O'Brien, CIO of Chicago. "As a result, we are able to focus on our strategic business issues without having to worry about operational IT issues."

Jim Martin is senior editor of Exec. *He writes about business and technology issues.*

track, the service levels have held up, and the operational stability has been tremendous."

To ensure a project's long-term success, experts recommend that organizations focus first on transition and then on transformation. "Too many companies try to take a big-bang approach, in which they attempt to do business process outsourcing and business process re-engineering at the same time," observes Gartner Dataquest's Scholl. "But users haven't yet seen the benefits of outsourcing, and they're already being forced to change their habits. You're more likely to be successful if you wait till you see the benefits of outsourcing before you pursue the benefits of transformation."

Mistake #4: Not Getting It in Writing

The contract, of course, is the linchpin of the entire undertaking. At its core are service-level agreements (SLA) that specify what you expect from your outsourcer and what your outsourcer promises to deliver. A good contract will delineate which service levels will be measured, how they will be measured, how reports will be provided and at what level the outsourcer promises to perform.

The contract should also specify what happens if service levels don't meet your satisfaction, and provide an exit strategy if the relationship isn't working. "Legally you want to have rights to cancel the deal if the transition isn't moving fast enough or if the whole project is going badly," says Peterson. "Establish milestones, with penalties if they're not met."

Make the contract as specific as possible. SLAs typically address operational metrics such as network availability. But what does "availability" mean? What is the response time to fix a problem? When do users have access to a helpdesk? "You don't want to find out later that what I thought wasn't what you thought," says Ingersoll-Rand's Berkey.

Note that BPO contracts aren't the same as those for traditional IT outsourcing. "In business process outsourcing, your SLA should be business-based, not IT-based," recommends Scholl. "For example, if you're outsourcing HR, you should measure time to hire, quality of hire, retention rates, that sort of thing. Those aren't the kinds of things you measure in traditional IT outsourcing."

The contract should also spell out how much you are paying and what you are paying for. It should be clear about what costs extra and whether costs will change over time. But the contract shouldn't be built around price alone. If you constantly squeeze your outsourcer, the result can be an adversarial relationship. The focus should be on value, and the outsourcer should be compensated accordingly.

Mistake #5: Not Building a Relationship

"Outsourcing needs to be a partnership," says Berkey. "That's an overused phrase, but it remains true."

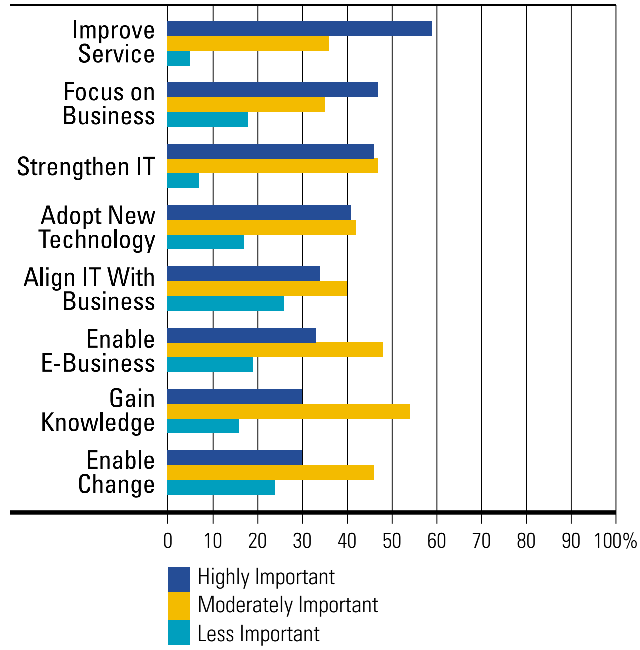
Barclays' Little agrees: "If you enter this sort of relationship, you need people you can work with, people who share your ideals and whom you can trust."

Such a relationship goes beyond contracts and SLAs. "We have cost agreements and service-level agreements, but those are legal formalities," says Ron Whatford, director of group operations for Lloyds TSB. "The reason [the relationship with Barclays and Unisys] works is that we are truly in partnership. That's the key ingredient."

Organizations that have been successful with BPO say that it's a relationship of trust that delivers value over the long haul. "Dollar savings are fine, but they tend to deteriorate," says Berkey. "You need a strong cultural fit, where you're sharing the same values and objectives. There needs to be a long-term give-and-take where both organizations benefit." If both you and your outsourcer benefit, there are greater incentives on both sides to invest the resources and effort necessary to make the relationship successful.

What's more, BPO relationships are rarely neutral. "When there isn't a relationship of trust, there's a cycle of mistrust," says Peterson of Mayer, Brown & Platt. "If one side doesn't trust the other, they start to look for problems, and they want to protect themselves." The result is a breakdown in communication and a decrease in both service and satisfaction levels as energy is diverted from the task at hand. "The relationship spirals downward," he says.

Key Drivers of BPO



Key reasons for outsourcing business processes include improving service levels, increasing focus on core business, and supplementing IT resources.

Source: Gartner Dataquest

Failure to foster a relationship of trust can be the hardest mistake to avoid, because trust is difficult to characterize and measure. It's complicated by the fact that it needs to extend across all the departments involved in the project, such as IT, HR and finance. And it's an issue less likely to be addressed by the outsourcer. "IT outsourcers recognize the importance of a strong cultural match," says Scholl, "but few business process outsourcers do."

But for organizations that get it right — that know why they want to outsource and perform due diligence, that manage the transition and get it in writing, and that forge a relationship of trust — the result is more than lower costs or greater efficiencies; it's transformation. "Our costs are in line, and the service has been good," says Whatford of Lloyds' partnership with Barclays and Unisys. "But the real indication that [BPO] is meeting our needs is that it has encouraged us to look at other areas where we can do the same thing. We believe this is the blueprint going forward."

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