Securing Transformation Through the Outsourcing Contract

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Introduction

- Companies outsource for a variety of reasons and use outsourcing as a means of transforming an element of their business.
- When the outsourcing is transformational, the delivery of the benefits against a business case and a TOM becomes magnified.
- Using the contract as a tool - to cover what it needs to cover and to be used in the way it should be used can achieve the delivery of these benefits ...
Why outsource?

- Cost savings
- Focus on core business
- Quality improvement
- Capacity management
- Catalyst for change
- Commoditisation / harmonisation
- Risk management
Why do outsourcings fail?

- Unspecified expectations
- Hidden costs
- Poor communication
- Poor governance
- Poor performance
- Multi-supplier environments
- Misalignment of interests over time
- Poor cultural fit
- Failure to appreciate why the other side is doing the deal
Reason 1 - unspecified expectations
Reason 1 - unspecified expectations (cont)

- If the contract does not specify it, the Supplier does not have to do it!
- Or it will do - for extra money so eliminating benefit delivery / business case delivery
- But is that right…
  - those tasks reasonably required for and incidental to the proper performance of the services…
  - provision of the tasks performed by the in-house team / transferring employees…
  - provision of services under contracts "transferred" to the Supplier
  - provision of all reasonable assistance
Bear in mind that the requirements are likely to change over time, so it will be important to deal adequately with:

- the impact of changes in law
- the change control procedure, including emergency and mandatory changes
Reason 2 - hidden costs
Reason 2 - hidden costs (cont)

- The price is the price?

- Critical to understanding the TCO, and determining the business case

- Various pricing mechanisms but all need to have the same factors:
  - clarity
  - capable of being understood
  - a link to the services
  - inherent flexibility

- Assumptions might be ok - so long as the impact of them proving incorrect, and their "life span" is clear

- Include provisions that say no other charges are payable for the performance of the obligations
Reason 2 - hidden costs (cont)

- Use the relief event mechanism to control claims for additional payments
- Consider where the tax liability falls and any obligation to "gross up"
- Should there be "hard-wired" pricing reductions?
- Are indexation mechanisms properly applied?
Reason 3 - poor communication / poor governance
Reason 3 - poor communication / poor governance (cont)

- The outsourcing relationship does need to be worked at…
- Needs a robust but flexible governance structure
- Consider the personal side of the relationship as well:
  - key personnel provisions
  - ability to call for the replacement of the supplier representatives
- Make sure that the reporting requirements are fully described:
  - ability to ask for further reports and other information, without additional charge (?)
  - access to Supplier reporting tools
Reason 4 - poor performance
Poor performance can relate to:

- failure to achieve milestones
- underperformance against service levels
- simply not delivering against the scope

All have the impact of slowing / eradicating transformation, and probably require the customer to spend additional money to try to resolve the problem.

Milestones:

- clearly specify the Milestones in the agreement, not post signature!
- link payment to achievement of the Milestones
- delay payments for failure to achieve acceptance
Reason 4 - poor performance (cont)

- Service Levels:
  - service levels need to address business need and be measurable
  - service credits that "ramp up" in relation to the diminution in performance
  - only a price adjustment not a remedy
  - ability to change weightings, and swap KPIs for existing service levels
  - "root cause" analysis to remove possibility of reoccurrence
- Early warning notices
- Relief event mechanism for customer defaults
- A liability cap that focuses the mind!
Reason 5 - multi-supplier environments
Multi-supplier environments can deliver best in breed services
But they can also create:
- increased cost of management (and therefore the TCO)
- finger pointing
- insufficiently joined up services

Prepare the scope as a whole and then divide - and keep an eye on what falls out of scope!

Joint governance / dispute resolution processes
A "fix first / argue later" philosophy
Co-operation obligations
Ability for other vendors to use outputs of the services, systems and other IP provided by each supplier
Finally...

- Transformation and benefits achievement is undoubtedly achievable - with the right tools
- Get the contract to focus on the key areas and the right basis will be there
- Use the contract as a tool to govern the relationship - on a day to day basis
Thank you

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