Ascea

EXPERIENCE MATTERS

Are Your Commercial Models Fit For Purpose?

It is imperative to understand the importance of adopting the correct commercial model, this article looks at four tried and tested examples, but it is fair to say there are many variations on the theme. Which model you adopt will be driven by the type of services required and also the clarity of scope and deliverables, explained below.

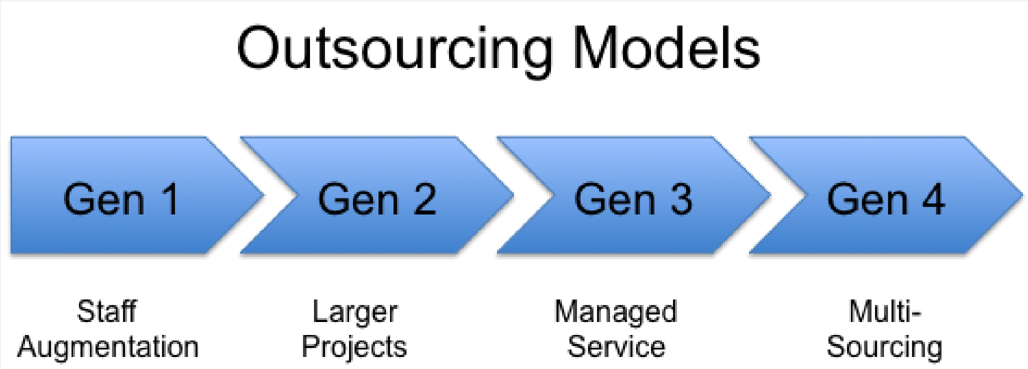
It is quite incredible to think that outsourcing and offshoring have been around for many years. Outsourcing crept into the business world in the 1980’s, with companies like IBM and EDS providing data centre services. In the 1990’s this morphed into application services, where companies rented space, typically on a mainframe, to undertake certain business activities, carried out over a private network. Sound familiar – yes – Cloud has been around for a very long time, it is just the want of the IT industry to re-badge something and pretend it is new. However, one of the most amazing facts is that the first offshoring project was undertaken in 1968, by the then unknown Tata Consultancy Services (TCS) for the US Detroit Police Department. Today TCS has over 600,000 employees and is the largest global IT services company, ahead of IBM and DXC.

Outsourcing models have matured over the years, all are valid today. The solution which should be adopted by your organisation will largely depend on:

1. What you want to achieve with the outsource service
2. What your medium to long term strategy is
3. Current position on the journey
4. Attitude to risk
5. Scale of the outsource
6. The shape of the retained IT organisation

7. Capability of in-house resources

One thing is for sure – one size does not fit all.



The characteristics of each of the models are:

Generation 1 – Staff Augmentation

This is where some roles within a project or service are taken by staff from a third-party service provider, either as a 'one off', or as a controlled introduction to further outsourcing 'a toe in the water'.

- ✓ One or two service providers
- ✓ Small value work packages (Statements of Work)
- ✓ Transactional
- ✓ Delivery risk remains with the client
- ✓ Predominantly an onshore model – therefore cost savings limited
- ✓ Dabble with offshore

Generation 2 – Larger Projects / Assignments

This is where the service provider takes on a lot more of the project delivery e.g. business analysis, build and testing, however the project management remains with the client.

- ✓ One or two service providers
- ✓ Larger value statements of work
- ✓ Introduce concept of 'fixed price' and 'milestone payments' (outcome/time based)
- ✓ Transactional – but leading to stronger relationship
- ✓ More work going offshore – therefore more cost savings realised
- ✓ Delivery risk remains with client

Generation 3 – Managed Service

The service provider is wholly responsible (contractually) for the delivery of the service – a clear shift in responsibility**.**

- ✓ Typically, a single vendor or a small number of vendors

- ✓ High value – mega deals (some of these deals have reached over $1bn and have lasted up to 10 years)
- ✓ The service is managed 'end to end' by the service provider
- ✓ Delivery risk transfers to the service provider
- ✓ Service provider is managed on outcomes (KPIs/SLAs)
- ✓ Partnership approach – the service provider becomes an integral part of the client's IT organisation
- ✓ This could involve client staff transferring to the supplier – in the UK this is covered by Transfer of Undertaking, Protection of Employment regulations 2006 (T.U.P.E), it will be different elsewhere
- ✓ Utilise a full onshore/offshore model – services delivered from Global Delivery Centres

Generation 4 – Multi-Sourcing Diagram

Go back to the 'T model' in the Scope section of this publication, this is where a number of service providers could deliver services to the client (maybe 5+ depending on the size of the client and IT spend), usually segmented by service towers, which are the verticals in the schematic. The Service Management Integration layer could be another service provider.

- ✓ A number of vendors, typically 5+, but this will depend on size and scope of the outsource arrangements
- ✓ High value – the size of the pie is the same as above, but is sliced into sections (segmented by service towers)
- ✓ Each service tower is managed by the service provider, but there is an overarching governance regime, managed by the client, this could sit within the Service Management Integration layer, or above within the client IT organisation
- ✓ Delivery risk is transferred to multiple vendors
- ✓ Service providers are managed on outcomes (KPIs/SLAs)
- ✓ Partnership approach – the service providers become an integral part of the client's IT organisation, especially if the SMI role is outsourced
- ✓ This could involve client staff transferring to the supplier
- ✓ Utilise a full onshore/offshore model – services delivered from Global Delivery Centres.

This model came into being following a number of high-profile outsourcing debacles, where the client locked themselves into long term Managed Service arrangements (Generation 3), benefiting from short term cost savings, but over time these savings were eroded, as the service provider failed to meet the expectations of the client due to on-going poor performance and missed SLA's. Unless you had a 'get out' clause in the contract for repeat performance failures, the client was stuck with an altogether unsatisfactory situation, in some cases for a number of years.

Many CIO's found themselves inheriting these long-term contracts, which stifled the business from innovation and moving forward. Exiting proved to be very expensive, but in some cases had to be done.

Multi-sourcing is the most complex outsourcing model; the cost of governance and change management should not be under estimated. The success of the model is based on how the client manages the eco-system and how well the third parties collaborate. If managed well, this should provide the best outcomes, however there is one school of thought that suggests that multi-sourcing stifles innovation, as it is unlikely the vendors will be open to sharing their Intellectual Property with their competitors, but to date that is not my experience, except in the case of using a third party in the SMI role (see below).

If the client is considering outsourcing the SMI role to a third party, careful consideration needs to be made as to who that third party is, as there is not only an issue around sharing IP, but it is also unlikely that a third party would want to share their commercial models with a direct competitor, so some activities normally undertaken by an SMI will have to be performed in-house by the client team.

The tip here is to make sure the sourcing event is undertaken in the correct sequence. I know of one organisation that got this wrong and paid a very heavy price.

Questions for Outsourcing Decision Makers

1. *How do I determine which commercial model best aligns with our organization's outsourcing objectives and long-term strategy, taking into account factors such as risk appetite, scope, and desired outcomes?*
2. *What strategies and governance practices can we implement to ensure successful management and collaboration among multiple service providers in a multi-sourcing model, while safeguarding against potential challenges in sharing Intellectual Property and maintaining service quality?*
3. *How do I approach the decision of outsourcing the Service Management Integration (SMI) role to a third-party provider, and what considerations should be made to overcome potential challenges related to sharing Intellectual Property and maintaining effective communication and commercial models?*

If you want to discuss these questions, or any other outsourcing challenges please do email us at experiencematters@ascea.co.uk and we can set up a call with you.

This article is taken from the short book **IT Outsourcing** – **11 Short Steps to Success** by Richard Cribb – available on Amazon.

Book review:

“Excellent summary of the critical success factors for IT Outsourcing .... A must read ..

Tim Laverick – former Head of Vendor Management – Home Retail Group

Ascea is comprised of highly experienced and knowledgeable people, who have worked for many years at senior level, in a variety of blue-chip companies. As a result, we have a diverse set of skills learnt at the coalface and not from the text book, we know how to get things done. Our sense of ethics and ‘doing the right thing’ is at the core of what we do.