



ISRC Notes – April 2000

Negotiating and Managing Vendor Relationships

Based on Presentations by Tim Goles and Jim Crompton

The April ISRC seminar was a well-attended event featuring presentations by Jim Compton, Manager of Capability Management at Chevron Information Technology Co., and Tim Goles, PhD student at the University of Houston and formerly a Vice President with First City National Bank. The two speakers were able to draw on their personal experiences to outline a framework for successfully working in an outsourcing environment.

Introduction and Overview

It was clear from the two presentations that working with an outsourcer(s) involves much more than just writing a contract, receiving services, and paying fees. The successful outsourcing arrangement is the one wherein both parties realize that they are trying to manage a relationship and that that relationship is a long-term one.

Why Outsourcing?

The Gartner Group forecasts a rise in US spending on all types of outsourcing from \$140 billion in 1997 to more than \$350 billion in 2002. But even with the projected increases in outsourcing reflected by these numbers, problems are increasing in these relationships. According to Tim Goles' research, 70 percent of customers are not planning to renew their current outsourcing contracts. Fifty percent believe the vendor's quality declined in the past year. So why do firms enter into outsourcing contracts if the results are so poor? As our speakers point out, the technological, economic and organizational benefits customers are seeking can be attained; but success is only available with effort.

The Successful Relationship

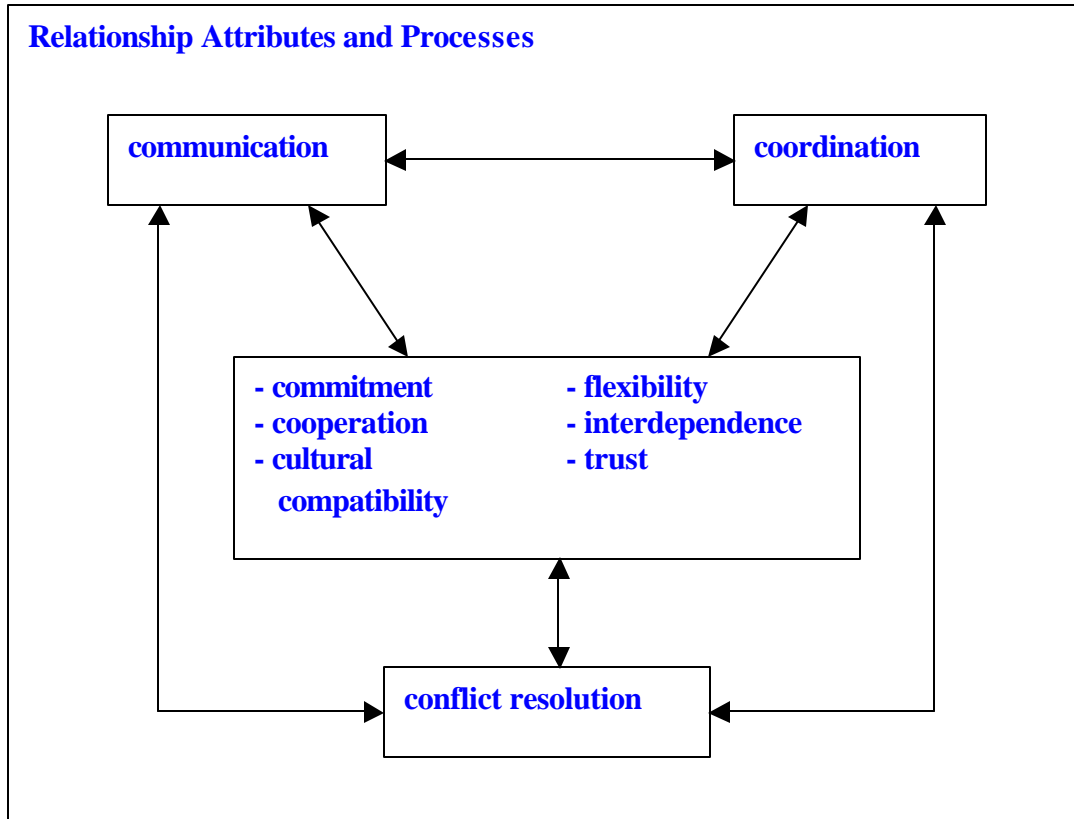
In the initial days of outsourcing, it was assumed that if the vendor had the technical competences that the customer needed, then that would lead to a successful arrangement. But failures have taught that there must exist a *relationship* between the two parties. The attributes of that relationship include:

- Commitment by both parties to the success of the relationship
- Cooperation in all phases
- A cultural compatibility must exist
- A respectful interdependence
- Flexibility in the terms and conditions of the contract
- Trust in each other

The administration of the contract between the customer and the outsourcer requires that there be:

- Determination of both formal and informal communication channels
- Procedures for conflict resolution
- Procedures for coordinating priorities and projects

These attributes and processes can be shown schematically as follows:



Determining the Success of the Relationship

The overall success of an outsourcing arrangement results not only from a good working relationship between the parties but also as a reflection of the quality of the outcomes. Quality manifests itself in three ways; systems quality, information quality, and service quality.

- Systems quality (performance characteristics)
 - Reliability- dependability and consistency of the system
 - Accessibility- availability of information
 - User friendliness- ease of use
- Information quality
 - Reliable
 - Relevant
 - Accurate
 - Precise
 - Complete
- Service quality
 - Reliability – vendor can be counted on

- Responsiveness – prompt reaction to customer requests
- Assurance - making the customer feel secure
- Empathy – a feeling the vendor understands and shares customer concerns

Customer satisfaction with the outcomes is also a multi-faceted construct. Overall satisfaction includes satisfaction with the economic, organizational and technological expectations.

- Were the economic benefits attained?
 - Reduced costs
 - Improved cost controls
 - Reduced capital expenditures
 - Provided business units a better understanding of their IT costs
 - Improved budget process
- Were the technological benefits attained?
 - Access to more knowledgeable IT people
 - Access to more advanced technology
 - Improved performance of IT
 - Reduced IT backlog
 - Focusing on strategic use of IT
- Were the organizational benefits attained?
 - Increased focus on core competencies
 - Filled in gaps in IT resources
 - Reduce risk and uncertainty
 - Burden reduced in managing IT
 - Enhanced organizational image

Alliance Management

Chevron has established “Alliance Management Teams” to forge a strong working relationship between their business units and outsourcers. These teams have a high degree of executive sponsorship and involvement. They are composed of a balance of strategic and operational personnel representing both the field business units and centralized management. These teams provide for a peer-to-peer discussion forum. The responsibilities of the team are to:

- Jointly develop business plans aligned with each companies’ objectives
- Review and report operational performance
- Identify quality improvement opportunities
- Resolve disputes quickly and fairly
- Improve communication and networking between both companies

Summary

The success of an outsourcing arrangement is measured by whether the overall benefits exceed the overall costs. Most of the variables in this calculation cannot be quantified. Success is therefore primarily determined by the perceptions of the parties. The quality of the relationship between the outsourcing parties will have the biggest impact of the realization of both the quantitative and the qualitative benefits.

Additional Information

<http://www.outsourcing-center.com>

“Outsourcing Center is the premier place for presenting information about the outsourcing industry. Our goal is to consistently bring those in the outsourcing industry a broad range of tools to help them get the outsourcing information they need.”

<http://www.cio.com/forums/outsourcing>

CIO Magazine discussion forum on outsourcing.

<http://www.tekptr.com>

TPI is a consulting company but does have some interesting news and announcements.

RELATIONSHIP CHECKLIST

- Does vendor and customer senior management share an understanding of how IT supports the business? Are they involved in setting priorities?
- Have vendor and customer management agreed on a technology plan based on business objectives?
- Is the plan communicated and understood by all customer and vendor managers?
- Is there a process for periodically reviewing and updating the plan? For making adjustments due to changing circumstances?
- Is there a formal process for information exchange concerning corporate plans, directions, and business policies?
- Are relationship-related roles, rules, policies, and procedures clearly defined and understood? Are they an integral part of both organizations?
- Do vendor and customer managers have overlapping, frequently used, formal, and informal channels of communication at all levels throughout the relationship?

- Do vendor and customer managers consult with each other regularly on business and IT decisions?
- Do vendor and customer managers have a mutual understanding of each other's roles and responsibilities regarding the relationship?
- Are vendor and customer managers satisfied with their abilities to communicate and negotiate with each other?
- Do all projects have clearly defined and accountable owners?
- Do both parties have realistic expectations of the other?
- Is the emphasis on business solutions, not just problem-solving?
- Is there a plan for monitoring and tracking emerging technology that could affect the business objectives?
- Is there a process for ongoing learning and knowledge sharing?
- Is common history documented and passed on?
- Are successes communicated throughout both organizations?
- Is there an emphasis on building relationships at all levels in both organizations?
- Periodically re-evaluate the purpose, resources, and structure of the relationship.
 - Establish common objectives and success criteria.
 - Develop appropriate measures. Benchmark to determine current capabilities and costs. This sets the baseline and helps refine the business objectives.
 - Determine targets and minimum acceptable levels.
 - Develop appropriate initiatives and penalties.
 - Review performance regularly. Respond with rewards or penalties as appropriate.
- Build trust. Take the first step unilaterally (and the second, and the third if necessary).