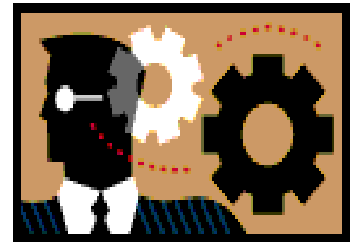




Tips & advice for purchasing professionals

Welcome to Transform, the source for comment, news and information for organizations and procurement professionals whose goal is increased added value and improved corporate performance through effective management of procurement and the supply chain.



Strategic Outsourcing – Part 2

Establishing Effective Governance

A guide for CEO's, CFO's and CPO's on establishing a key tool for outsourcing success to remain competitive and support their core business goals

What's in it for you? Discover how implementing an enterprise level OS governance organisation can increase outsourcing success and capture the intended value to keep your organisation competitive.

Reading time: 10 minutes

Introduction:



Effective governance is critical to the success of any outsourcing deal. Yet many organisations fail to give outsourcing (OS) management and governance the attention it deserves. As a result, despite the high stakes and initial optimism with which many outsourcing arrangements are entered into, too many of them fail to deliver the anticipated benefits, resulting in significant scepticism among executives whenever outsourcing raises its head.

The main cause for outsourcing relationships failing is that they are poorly managed from the start. Typically, organizations consider governance too late in the OS process, and often not until they go live with their chosen provider.



Herein Purchasing Practice argues the case for an enterprise level governance framework to manage from the strategy & planning phase and continue through every phase of the outsourcing process ([See Strategic Outsourcing – Part 1](#)). In this way, organizations can align their outsourcing efforts and goals with the governance programme, and they can plan to monitor service levels based on specific corporate goals.

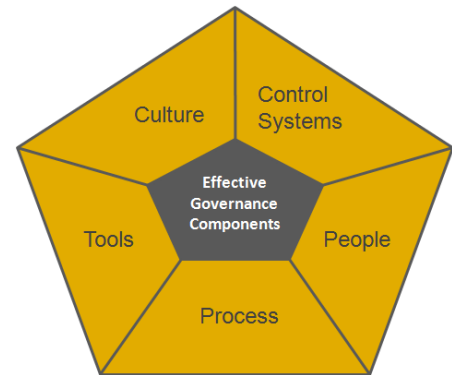


Figure 1

Governance comes from the top

At the enterprise level effective governance is an overarching system that seeks to align business priorities, funding, and resources. It also influences company culture, and steers the decision making process, decision rights, and accountability to the appropriate levels.

The leadership must critically recognise that requirements will change over the life time of an OS contract. The governance framework must therefore facilitate a focus on the process of how to deal with change, instead of blindly prescribing predictive contractual requirements and outcomes for unknown events and market developments. The leadership must therefore ensure the skills, processes, tools and resources are available to manage this change (See Figure 1).

To remain competitive, organisations must link this enterprise level governance framework with their customer service deliver experiences, long-term objectives and corporate goals when defining the way an organization manages decisions.

Why CPO's need an Enterprise Level OS Governance Structure:

Without this top-down perspective, each business unit will continue to manage its own OS requirements according to its own needs, without the assurance that they meet the overarching strategic goals of the entire business. The CPO (or any other executive) then has no way to measure the total effectiveness of the outsourcing relationships at the enterprise level, and has insufficient information upon which to link OS and business level strategy.

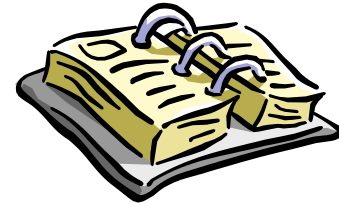
In contrast, enterprise level OS governance focuses on providing structure, methodology and resources, across all phases of the outsourcing lifecycle throughout the enterprise. Its sole purpose is to identify outsourcing opportunities and to capture the targeted value from these activities.

Gaining the support for an enterprise-level governance structure is a key factor for CPO's to enable them to provide all the necessary management inputs required to support business strategy. This includes,



monitoring the effectiveness of OS relationships and ensuring they support the top-level corporate strategy. The challenge for CPO's therefore is to stake their claim as the natural owner of the OS process and OS relationship management.

[Visit the Buying Magician blog to read 10 reasons why procurement should own the OS relationship.](#)



Such an approach is also helpful for suppliers. The supplier gets scheduled quality time with the buyer's senior executives to share long-term strategy. This helps them develop an execution plan that more closely aligns to the buyers' goals and add value over the life of the contract. In addition, it helps suppliers establish enterprise-wide standards and best practices which would not be possible if every OS relationship had its own rules.

Benefits

Implementing enterprise wide governance can produce several key organisational benefits:

1. Alignment of OS targets and resources to wider business objectives.
2. Provides a standardized methodology to manage multiple service providers and ensure they are working effectively. This enables the sharing of resources and the creation of a centre of excellence to leverage best practices – which we argue is the natural domain of procurement.
3. Ability to determine if the service provider is consistently delivering on commitments over the lifetime of the contract, and whether the buyer is actually getting what it's paying for.
4. Provides a set of guidelines for the outsourcing relationship.
5. Offers a forum for dealing with legal and service level issues.
6. Creates structure for buyers to measure the success of the relationship as business conditions and requirements change.
7. Reduction of sourcing cycle time.

Risk

The main risks from failing to implement an effective governance organisation are transaction failure and lost opportunity. OS short history has plenty of examples from early [outsourcing] adopters that did not know that governance was necessary for successful OS relationships. These relationships were characterized by:

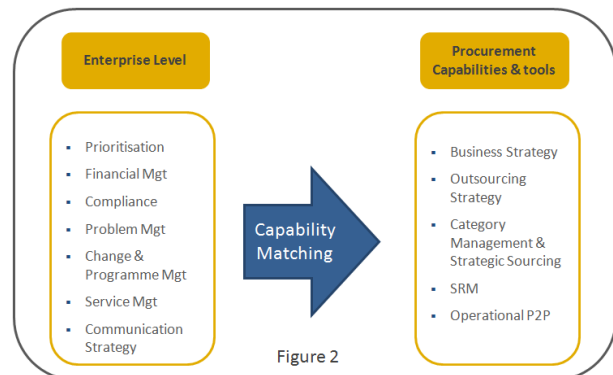
1. misaligned goals and objectives
2. disincentives for collaboration



3. over-reliance on the contract, and mutual distrust

Such characteristics lead to a loss of value and dissatisfaction. The absence of effective governance results in a lack of clarity about the goals and outcomes of outsourcing with a resulting loss of value.

Indeed having learned from their past experiences resulting in failed or at best tarnished relationships some service providers now seek to protect their reputation by profiling prospective buyers to make sure they have governance capabilities in place before signing a contract. The **“Brave CPO”** will be proactive in ensuring their organisation is not found lacking.



Building Governance into the Outsourcing Lifecycle:

The starting point for procurement in gaining support for enterprise level governance is to clearly understand current state governance capabilities in their organization. These capabilities must balance the competing priorities between risk mitigation and value realization. Key capabilities are shown in Figure 2. CPO's must focus on building these capabilities, by identifying gaps against established best practices and implementing improvement plans.

The governance organization is also responsible for ensuring the resources moved into governance position have the processes, tools, and capabilities to be successful. They must therefore ensure training is offered to teams taking on the task of managing OS relationships, and provide the necessary tools to fully enable the governance team to focus on the strategic priorities to drive transition and delivery of the services.

Governance Structure

A well thought out enterprise governance structure is usually multi tiered, comprising various decision making groups and individuals. Each tier needs to consider how it aligns with the wider organisation, its mandate, responsibilities and the frequency with which it will meet and work with key stakeholders and the OS provider.

A one size fits all approach is not effective. Best practice governance organisations don't simply describe the governance structure and how it will work, they also describe how the governance structure will change to meet the challenges of each OS deals unique goals. In other words, demonstrate ability to



customise the governance structure according to the targeted goals, complexity of the transaction and the type of relationship with the OS provider.

Figure 3 shows an example of a successful procurement governance structure:

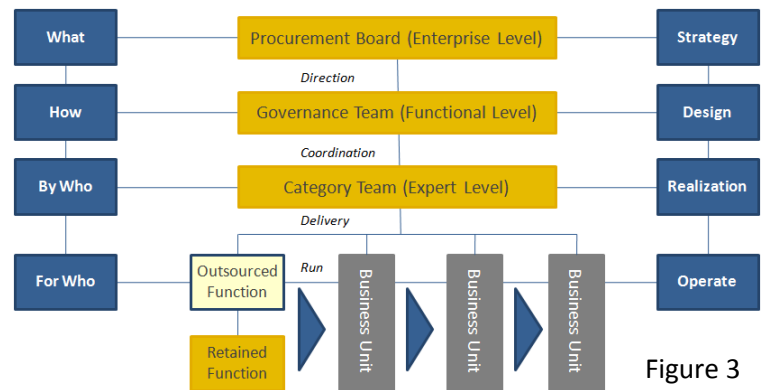


Figure 3

Enterprise level team - comprising of the senior executives that takes strategic level decisions, assesses the outsourcing strategy, and charts the future road map.

Functional level team - comprised of the key cross functional leaders working closely with the OS provider and outsourced process departments. This team evaluates the outsourcing programme, ensures process compliance, identifies process enhancements and formulates recommendations.

Expert Level Team – made up of cross functional specialists seconded from the business unit and functional level who conduct the sourcing and selection phase and deliver the OS contract for transition and implementation.

Business Unit Level - is the stakeholders of the Expert Level team that manages the day-to-day activities of the outsourcing initiative.

A successful, governance organisation provides empowerment and open communication through the hierarchy. It builds a culture of discipline and defines the operational context of a successful outsourcing relationship. This creates an equal playing field among all parties in which the management rules of engagement, behaviours and processes are well documented and known.

The OS Contract

When designing a contract for outsourcing transactions it is best to include the governance model and processes in the highest precedent group of documents. For Purchasing Practice the key contractual components include:

1. outsourcing governance model
2. service definition
3. service levels
4. fee methodology



We also argue for the core components of the governance model to be incorporated in the RFP. In this way the buyer demonstrates capability, understanding and respect for the mutuality of interests with the service provider and seeks an outsourcing partner with similar values.

OS tools

Strategic outsourcing tools can be encompassed into the governance plan that fall into five broad areas:

1. **Relationship tools:** SLA's, KPI's, Trust, Communication, Openness and Cultural awareness, Relationship Health monitoring
2. **Operations tools:** Performance dashboards, User satisfaction dashboards
3. **Financial & Commercial tools:** Spend analysis, Contract
4. **Compliance tools:** Compliance audits
5. **Automation tools:** Portals for demand management, SLA management and invoice management

For every key management responsibility of the governance organization, tools can help put stakeholders on the same page, automate routine tasks and provide a system of truth that transcends individual self interest and corporate politics.

Conclusion

Building and retaining OS competency is not easy. Most, if not all, companies have trouble getting the right skills into key governance positions during the outsourcing lifecycle. Filling these positions with whoever is available at the time is unlikely to deliver the desired results and usually comes about largely due to the absence of a corporate level OS strategy with a clearly designated owner. As the natural owner of such a strategy the "Brave CPO" must make the case for owning the OS process and the OS relationships in order to lead a charge towards enterprise level governance. Only when this has been achieved can procurement truly claim to be at the "heart of the business".

For More Information

Purchasing Practice Inc can work with your organization to develop a strategic procurement capability that will add value and positively affect your top and bottom line. To learn more, call 1-778-988-1052 to arrange a free consultation, or visit us at www.purchasingpractice.com



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Spend Analysis: We provide spend transparency to our customers as part of our broader service offering, and this data can then be utilized to perform an opportunity assessment on the mapped data, pointing out potential areas for savings.

Opportunity Assessment: By working directly with those staff responsible for committing expenditure, or managing suppliers, we will carry out a rigorous review and present our recommendations

Sourcing Management: Using our strategic sourcing service enables clients to realize full value from their supply base through leveraging our proven processes

Category Management: We work with clients to analyze spend data, define suitable categories then working on a category by category basis to deliver significant benefits

Supplier Relationship Management: We will carry out a rigorous review using proven tools and methodologies to present our recommendations.

Mergers & Acquisitions: We will work with your M&A team to carry out a rigorous review using proven tools and methodologies

Private Equity: Working across your portfolio of companies we will drive value from procurement across business units

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