

It's the "P" word stupid!



In considering how to start this paper on the Management of Third Party Suppliers, I was drawn to my front garden where my gardener was working away. He only comes for two hours a week on a Thursday afternoon but it is amazing what gets done in that time. Then I thought how does he know what to do and where is he taking instructions from since I rarely speak to him about anything other than the state of English Cricket.

Now that's another story!

Ah of course, it's the wife!

So I started thinking and realised we have outsourced the management of our front garden to this guy and the relationship is being managed by my wife. Our gardener is content and works hard but most importantly we get the service we want from him to a high quality, when we want it and at a fair price.

So relate that scenario to services you have outsourced in your business and interestingly enough isn't that what everyone who outsources is broadly trying to achieve?

So what is the secret since many outsourcing relationships seem to struggle to achieve a quality service at a fair price?

Well of course the first thing to say is that compared to a major outsource of processes, services or delivery by a significant corporation to a large service provider serving multiple clients with a highly varied range of services the case of my wife and the gardener is irrelevant in scale but some of the principles, if applied across a major relationship, could make the whole service provision a lot smoother.

What are the key elements to the relationship which make the garden work get done which could be looked at in a corporate context that many of us try to make work.

The overall process can be broken down into four main components to be considered; the contract, the rewards, the relationship and communication

1. The Contract

In the case of the gardener there is no written contract. My wife talks to him and they decide, working together, on what needs to be done and the priority of the work. This may change from week to week because both of them operate flexibly and there is a level of trust between them. Sometimes he works a bit longer than his two hours and others a bit less, but the job gets done and no one is watching the time to the nearest minute are they?

Sometimes this is where the problem starts, even before any services have commenced. It is not unusual for relationships to become soured between the buying company and the service provider during this part of the process which carries over to when the contract is up and running. This can be caused by a range of different issues.

The buyer being too aggressive on pricing, and sometimes the supplier then also being too desperate for the deal in order to satisfy a sales pipeline, demand from Head Office or to gain a bonus or promotion, which leads to an unprofitable contract at the outset. See rewards below.

Often the sales team from the provider either oversells the capability of the provider or doesn't understand what they are selling or doesn't understand the service the client wants to buy. Equally the buyer may be unclear about their specific requirements or be speaking in a "different language". This can lead to protracted remedial work once the contract is live and can develop into a long running dissatisfaction between the two parties.

Sometimes the client negotiating team are working on a service which affects other areas of the business and in drafting the contract they do not fully take into account the needs of other parts of their business for services being provided by the third party. This certainly can cause major friction within the company buying the service and a lot of internal management time can be wasted in managing inter departmental finger pointing.

Finally it is important to note that if the contract is negotiated well, to the mutual benefit of both parties, then it should be able to stay in the company safe (other than those sections which are naturally fluid such as the SLA). If either party is regularly referring to the contract then it is likely that the relationship is not working well. In negotiating the agreement, both sides should have the word "partnership" in their minds at all times. These transactions should be looked at as long term partnerships, not short term transactions otherwise they probably will not be successful.

It is very important that management at the highest level get involved early and ensure that issues are resolved quickly to avoid turf wars developing. In addition it is important that both parties set realistic short and medium term expectations for the relationship, it won't all work like clockwork on day one.

Furthermore, in the current environment arrangements must be capable of surviving mergers, acquisitions, restructurings in either party which are becoming inevitable.

2. The Rewards

Again this was agreed up front and reviewed regularly when the rate is discussed with him. Our belief is that the rate needs to be fair and it is always us who raises the issue of pay with the gardener. Funnily enough the rate rarely rises as a result. We do occasionally give him some tickets for the cricket as a surprise bonus!

It is really important for both the client company and the service provider to come out of the negotiation phase feeling good about the financial aspects of the contract. The client must be happy that they are paying a fair price for the

service both from their own point of view but also from a benchmarked view of what others are paying in the market for a similar set of services, delivered in a comparable manner for an equivalent size of business. They need to have done the "supermarket" test on their numbers i.e. Are they a "Waitrose shopper" or a "Lidl shopper." What this means is, are they willing to pay a premium for a better quality more flexible service or do they want to pay a lower price for a basic less flexible service. Provided contractually you are happy with the service level versus price comparison then the price you are paying the service provider should be right.

Basically the same applies from the service provider perspective. Issues can arise if there is a mismatch in expectations. This is usually most successfully negotiated when there is an open and honest dialogue between the parties where there is a desire to build a long term relationship.

The effect is important e.g. if an emergency arises and some urgent or remedial processing is required, where there is a strong flexible relationship the service provider will typically do the work and worry about payment later or may even do the work gratis. However, if the provider is on a low/no profit margin arrangement then they are more likely to look to agree terms for payment before going the extra mile.

So it is important to leave some flexibility in the pricing "leave a little bit for the next man", and work together for mutual reward from the contract. It is also worthwhile trying to build some incentives into the reward structure e.g. reward the supplier for outperformance or reward the client for making it easier for the provider to service them. Importantly it is effective if employees are rewarded in a manner for making the relationship work at all levels and working in a spirit of partnership.

3. Relationship

This is always friendly, open, honest and courteous. Is there any other way? It is important to observe that our gardener wants to be a gardener and loves his work.

Already it is becoming clear that the art of a successful outsourcing is in building a strong, open, honest and trusting relationship between individuals and across the two enterprises. Like all relationships these take a long time and much effort to build up but can be destroyed in an instant. In addition most organisations set up a team or have specific relationship managers to work with the third party provider. Whilst this is very important the relationship has to be across all aspects of both organisations but structured in a way that the right people in both organisations talk, regularly and candidly, and build relationships with each other. Rarely does a service from a provider only affect one area in a client company, more often than not it goes across multiple functions not all of them obvious at the outset. It is important that everyone in both organisations

understand the impact of their service and actions on staff and clients throughout the other organisation. Issue resolution is vital and it must be confronted up front in an open and honest manner. People make mistakes, very few people make mistakes deliberately so there needs to be sufficient trust between the two parties that they can work together to resolve issues quickly and not spend a disproportionate amount of time trying to lay blame on each other or stubbornly defend their respective positions rather than reaching an equitable compromise. Of course issues need to be investigated, and if it is a systemic problem then processes need to be reviewed and where necessary changed to avoid a repeat of the problem but this can only happen if the relationship is strong enough that the two parties can work together to resolution.

It's that partnership thing again!

4. Communication

In covering the contract, rewards and relationship the one thing that stands out is the spirit of working together as a team, as a partnership, the feeling of mutual benefit. This derives from an atmosphere of mutual openness, honesty and trust brought on by very open communication.

Communication is the key to management of expectations, problems and solutions and building a partnership that works.

So if that is the case study of a very small outsourcing that works really well then let's consider those positive attributes and see if, and how, they might be applied in the case of a significant outsourcing transaction.

It is important to note that the concepts we are talking about in a corporate world can relate to all types of outsourcing from major processes to call centres, from HR payroll to finance departments and others.

It is evident that communication will play a vital part in the success of any partnership between a client company and a third party provider. But it does not necessarily happen automatically and it is useful to put in place organisational structures that make transparent communication possible and positively encouraged between the right people in each organisation. In the more complex arrangements this can

involve significant numbers of people on both sides of the deal communicating with each other at any time and the trick to making this a success is to ensure that the relevant people are communicating pertinent information to each other. There is nothing worse than a piece of information being passed on to the incorrect person, they may misinterpret it's importance or not pass it on to the correct person at all. The result is then one side saying they have communicated an issue and the other side denying it which ends up in a conflict situation which can then use up a lot of time to sort out.

It is important, therefore, to establish good, regular and formal communication mechanisms to keep on top of all aspects of the arrangement. Many organisations fight against the formality of such arrangements but the larger the outsource the more important it becomes. Quite often



an agreement is made between two parties for services and the key stakeholders in getting the negotiations done and implementing the outsource are the only people who really understand all aspects of the deal, how it affects both organisations and the "spirit of the deal". Whilst those stakeholders remain involved in the arrangement then many issues can get resolved using their deep understanding and "spirit of partnership". However it can unravel rapidly when they move on and the new owners of the relationship revert back to running the outsource by the letter of the contract. It is fair to observe that in most cases the contract becomes out of date almost as soon as the service commences as there are always processes or actions that both sides have missed in the preparation for the transition.

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