Outsourcing Performance Management

June 2005 - Sam S. Adkins

According to a study conducted in April 2004 by the Conference Board, only 9 percent of companies “are entirely against outsourcing some or all of their major human resources functions,” compared to 23 percent in the 2003 survey. Clearly, companies are increasingly willing to outsource HR functions like performance management. In today’s business climate, the issue is not whether or not to outsource performance management, but how to measure the success of the effort.

Performance management professionals often use the so-called “SMART” method to measure success. This method was designed to establish clear expectations for individual performers in an organization. The framework described here uses the traditional SMART (specific, measurable, aligned, realistic and trusted) method as a baseline, but modifies it to apply to outsourcing efforts. It is a flexible framework designed to set clear expectations and measure success. (See Figure 1.)

Figure 1: Performance Management Outsourcing Framework

Specific	Ask the “W questions”: why, what, who, where, when and what if.
Measurable	Measure the key performance indicators: cost savings, service improvement and employee satisfaction.
Aligned	Align the performance management effort with internal technology, business strategy and workforce performance.
Realistic	Use the “seven C’s” to set realistic expectations: cost, compromise, control, culture, communication, contingency and compassion.
Trusted	Establish trust by meeting expectations, by willingness to compromise and by being dependable, predictable and ethical.

Figure 2: Performance Management Categories

User-Centric Processes	Management-Centric Processes
Individual Performance Objective Management	Organizational Performance Management
Individual Performance Evaluation	Compensation Management
Competency Mapping	Assessment Management
Self-Paced E-Learning and Decision Support	Learning Management and Training Administration
Career Planning	Succession Planning

Be Specific
Outsourcing contract negotiations require very specific task and service-level descriptions, and defining the why, what, who, where, when and what if can clarify things significantly:

- **Why are you outsourcing?** The decision to outsource is based on two business factors: value proposition and market-based outsourcing. The most common value proposition is reducing cost savings. Other value propositions include increasing operational efficiency, improving customer service, improving employee satisfaction, growing revenue or reducing capital expenditures. Market-based outsourcing is a comparison between internal skills and abilities and the capabilities of providers in the marketplace. The decision to outsource is based on whether an external provider can do the job better, cheaper or faster.

- **What will you outsource?** Customers can determine what to outsource by having a clear idea of the most common performance management functions. Perform-ance management functions can be segmented into user-centric processes and management-centric processes. (See Figure 2.) User-centric processes include individual performance objective management, individual performance evaluation, competency mapping, self-paced e-learning and decision support, and career planning. Management-centric processes include organizational performance management, compensation management, assessment management, learning management and training administration, and succession planning. In general, all of the user-centric performance management processes lend themselves to automation and outsourcing. Management-centric performance management functions also can be outsourced. Learning management and assessment management, in particular, lend themselves to outsourcing. Since vendors specialize in one or more of these functions, customers can map the functions they intend to outsource to the capabilities of the vendor. This makes the vendor selection process relatively straightforward.
- **Who will be your outsourcing team?** According to a 2004 study by the Gartner Group, there are three types of outsourcing partners: application service providers (ASPs), traditional external service providers and business process outsourcing (BPO) companies. It is common for companies to have all three types of relationships and several outsourcing partners. An ASP hosts the technology and the services appear to employees like an internal function. A traditional external service provider brands the service as its own, but the customer still controls deliverables. A BPO “owns” the entire business process and has near-complete control, often called “end-to-end outsourcing.” The “who” question has to be asked internally as well. Who will manage the outsourcers from the inside?
- **Where will the outsourcer work?** Outsourcers are not always physically located outside your company’s facilities. Occasionally companies prefer a representative of the outsourcing firm to be present on-site. But it is far more likely that outsourcers will work outside the buyer’s physical facility. Many governments have passed or are drafting laws governing the offshoring of business, so it is prudent to check existing regulations prior to engaging an offshore outsourcer. Defining where the outsourced personnel will work is an important legal aspect of the outsourcing agreement.
- **When will the work be completed?** Specifically defining service milestones is crucial to both the customer and the outsourcer. Business-process cycles are always time-bound, and customers and outsourcers alike are always constrained by time. Defining these time-bound constraints in terms of deliverables and milestones is a strong point of outsourcing firms since milestones map directly to payment cycles. Customers should be willing to ask themselves, “What is driving the date?” Dates are sometimes set by internal priorities (hard dates), but often dates can be flexible. Being flexible about time constraints allows teams to proactively deal with unanticipated challenges.
- **What if something happens?** “Expect the unexpected” is a good motto to have on an outsourcing project. Experienced outsourcers will probably want to put a change management clause in the contract. This is because they know from experience that business needs change and stuff happens all the time.

Answering all these questions results in specific goals that can be used to develop measurable performance expectations and contractual obligations.

Measurement

Every performance management professional is trained to ask a single question at the start of a project: How will we know if we are successful? Performance management professionals on an outsourcing project should ask many variations of this question, such as: How will the outsourcer know if they have met expectations? How do we determine internally what constitutes acceptable service levels?

According to the Conference Board, the three most common metrics that companies use to measure their success with outsourcing are: cost savings, service improvement and employee satisfaction. Being able to measure these things properly requires aligning performance management with the internal business strategy.

Alignment

The 2001 report by the Corporate Executive Board of the Working Council for Chief Financial Officers, titled "Beyond Measurement Alone: Optimizing Corporate Performance via Effective Performance Management," stated that 90 percent of companies consistently fail to execute new business strategies effectively. As companies grow, their technology proliferates, their business units grow more autonomous, and their workforce becomes resistant to change. Combined, these three trends are called "the alignment problem." Performance management outsourcers are experts at workforce performance alignment methods. They also use new performance management platforms that are designed to align technology, workforce performance and business strategy. Effective alignment methods enabled by sophisticated performance management technology create the infrastructure to support realistic goals and expectations.

Be Realistic

The process of establishing a realistic performance management outsourcing relationship can be summed up as sailing the seven C's:

- **Cost:** Cost is usually the primary reason companies outsource in the first place. Cost also can be a major cause of contention and conflict in an outsourcing relationship. Companies outsource to save money, and outsourcers are in the business to make money. At first glance, these goals would appear to be diametrically opposed. An honest and continuous recognition of this as a business reality is the foundation of a long-term trusted relationship. Hidden costs are more common than they should be and can quickly sour a relationship. Budget overruns and unexpected costs also can occur for a variety of reasons. The best way to deal with cost changes is to be prepared to compromise.
- **Compromise:** BPO vendors are process experts and are able to provide their services for the price they charge because they leverage everything they do across all clients. They use software to automate just about everything they do. Quite often, the outsourcers will slip into a "this is how we do it" mode, which is often interpreted by customers as inflexibility. What may seem like a minor request from a customer may actually require a great deal of work. On the other hand, some things are quite simple to change, and ethical outsourcers always will be willing to make minor changes within the existing budget. Compromise is the cornerstone to successful change management. It also is the best way to realistically handle control issues that arise.
- **Control:** Settling control issues quickly and equitably is vital in a performance management outsourcing relationship. Control of every phase and aspect of the relationship should be analyzed by both parties and discussed in detail. Boundaries need to be defined in order to manage expectations. Roles and responsibilities should be scrutinized carefully and continually. Business evolves, and projects evolve. Control issues are at the root of many barriers to success in outsourcing efforts. One barrier cited again and again in various studies is the resistance from internal employees.
- **Culture:** Studies show that the internal culture of the buying company can be a source of serious roadblocks to successful outsourcing. Internal resistance to change can occur if the goals and the rationale for the outsourcing are not clearly communicated. Culture clashes between the management style of the customer and the outsourcer have also been identified as a barrier to success.
- **Communication:** Communication is probably the greatest challenge in any outsourcing relationship. The lack of consensus on goals and expectations is often blamed on poor

communication. Both parties in the relationship may believe they are using the same language and may be justified in thinking they are resolving the same issue. But both parties commonly will come away from the conversation with fundamentally different conclusions. Constant and careful communication is a good way to build consensus and is particularly useful when unexpected things occur.

- **Contingency:** Contingency planning is not an exact science. It is about probabilities. Contingency planning is not just about what could go wrong, but also what could change. Professionals with outsourcing experience can be painfully aware of what can go wrong on a project. They also know that change is a constant in any business process. Change management is often a thorn in the side of any outsourcing relationship and must be dealt with early, honestly and realistically. Sometimes there are good reasons to change things, even if changing them will create stress.
- **Compassion:** Compassion is good for business. People are the primary resource in any outsourcing relationship. When providers are sympathetic to their customer's constantly changing organizational pressures, they establish a human-to-human relationship that can be the foundation of a long-term business relationship. Likewise, the customer can generate a strong sense of trust by being sensitive to the vendor's constraints. Compassion makes people feel like they are part of the same team, even if they work for different companies.

Trust

Probably the most important component of an outsourcing relationship is trust. Trust is a two-way street and has to be cultivated by both parties. Trust is built by setting realistic goals and expectations and by having objective ways to measure success.

Building trust is a process. It occurs naturally when providers know that their service matters and that what they do is directly aligned to the customer's business strategy. In an outsourcing relationship, trust is built by being willing to compromise and by being dependable, predictable and ethical.

Sam S. Adkins is chief research officer of Ambient Insight, where he specializes in learning and productivity research that spans converging trends, such as business process outsourcing, business process management, collaboration, mobile workforce management and wireless productivity.

---

10 Ways to Be SMART About Outsourcing

1. Do your budget homework before you sign the contract. Outsourcing may not be cheaper, and cost savings may not occur. It is a common misunderstanding that outsourcing automatically cuts costs. It is possible that outsourcing will actually increase costs, but achieve one of your other goals.

2. Accept that outsourcing is usually a one-way street. Once you outsource a function, you will probably not be able to bring it back in-house. It is almost impossible to bring a function back in-house once your head count and operating budgets are reduced. If you become unhappy with your outsourcer, your only option may be to select another outsourcer.

3. Resist the temptation to change project deliverables in midstream. Cost is fluid while the project is fluid. Unexpected change, second thoughts and spontaneous creativity can be expensive. A really good way to frustrate an outsourcing partner is to constantly change requirements. While it is rare that an outsourcer decides not to negotiate a new contract based on this, it is common for them to bump the prices on the next contract in anticipation of constant change.

4. Stay connected with your workforce. Transactional processes in performance management can be outsourced and automated, but not employee performance itself. The performance management outsourcer will give you advice and information to help you manage and improve workforce performance.

5. Read the fine print and let your legal department scrub the contract. The outsourcer will be legally bound to deliver on expectations, but you may have legal obligations as well. A growing number of compliance regulations are now being enforced with rigor. There are rules and regulations surrounding offshore outsourcing that you need to consider. Lack of awareness could expose your company to legal risk.

6. Protect the privacy of your employees. Your company has a privacy policy, and your outsourcer must agree to comply with it. Ask your outsourcer to review your privacy policy and commit to specific compliance in the contract.

7. Be aware of your company's security policies. Your outsourcer must comply with them. Intellectual capital and the data in a performance management system should be protected with the latest security protocols.

8. Become familiar with the technology used by your outsourcer. Your outsourcer uses sophisticated performance management technology that has to be aligned to your business strategy. Don't be afraid to "look under the hood."

9. Watch out for hidden costs. For example, if you already own a performance management platform, your internal software licenses can be transferred to the outsourcer, but transferring an internal software license to the outsourcer will generate extra costs. You may have to pay twice for the software.

10. Develop trust with your outsourcers. Outsource companies employ people and try to treat your contacts like team members. Remember that outsourcers can provide services more efficiently for you because they have similar clients with similar needs. They have a perspective on performance management that you can learn from. Trust their expertise.