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Feature Article

Less Is More In Off Shore Outsourcing Contracts

James River's background in both private industry and government contracting sets us apart from most other management consultants and business advisory-minded accounting and law firms. We see how governmental ways of transacting business—without the bureaucracy—can become powerful tools for any size company.

Take offshore outsourcing for example.

Deloitte's latest report on global outsourcing, "Why Settle for Less? Deloitte Consulting 2008 Outsourcing Report," (Deloitte Consulting LLP, December 2007), has garnered a large response ranging from the Wall Street Journal to blogs, though probably not the response Deloitte intended.

In sum, the report's survey shows that 83% of offshore IT outsourcing deals achieve 25% cost savings. For two thirds of outsourcing deals, price is the key motivation. But instead of delving into these figures, the report focuses on the belief among one third of respondents that off shore outsourcing relationships are not innovative or transformative enough.

Strategic partnering is where Deloitte will make its money, not on mere "labor arbitrage" (staff

augmentation). Off shore outsourcers ("Double O's") would also like to move up to the relationship management echelon, as more countries get in the outsourcing act and labor rates are driven down.

Given the practical gaps of language and time zones, and the multiple legal concerns brought on by entwining with Double O's or buying them out, partnering would appear to be an expensive and problematic proposition. Deloitte and the Big Four are free to make their case for partnering. But for the present, what Deloitte's report reveals is that price is the real reason why companies use off shore outsourcing.

Which brings us to how the US Government buys services. When price is the only deciding factor, and there are multiple providers interested in the work, by law Government agencies must contract for the services through "sealed bidding" (instead of the more didactic and solution oriented "competitive negotiation" approach).

The important point here is not sealed envelopes, but rather how sealed bidding works and the reasons behind it. Sealed bidding requires the Government to determine all of its requirements for the work up front and to put them in the invitation for bid. In response, providers are required to quote a fixed price for the work.

These are not arbitrary rules; sealed bidding

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About James River

James River Consulting is a New England-based company specializing in the development, negotiation, and management of IT and non-IT services contracts. James River's offerings range from short-term staffing of contracts personnel, to sales contract process and policy implementation, to competitive bid announcement and management, to SaaS and BPO contracts negotiation and management consulting. James River's president, Eric Esperne, has over 15 years experience as an in-house legal counsel and director of contracts for both large and small IT companies.

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represents a well-rationalized commercial trade off. Providers are relieved from having to figure out what to propose in order to win the bid; they only need to meet the requirements and do some basic pricing. If the provider can't meet some of the requirements, it only need team with others who can. Certainly there is no innovation involved. In return, the Government doesn't risk cost overruns and avoids costs of contracting and ongoing management.

In commercial off shore outsourcing, transaction costs are huge. Sealed bidding's streamlined transaction model alone would be a boon.

The trick is capturing and documenting requirements. But in the Deloitte survey, three fourths of respondents felt their outsourcing deals suffered from poor vendor selection and lack of service levels, meaning that a better way of contracting needs to be

found anyway. Survey data on dissatisfaction—scope creep, cost overruns, poor communication, lack of transparency—further argue for taking a sealed bid-like approach to off shore outsourcing contracts.

The final requirement in sealed bidding is that bidders affirmatively show they are “responsible.” Here too, a streamlined transaction model like sealed bidding fits off shore outsourcing like a glove. According to Government regulations, responsibility means showing the following: financial resources; facilities, management and personnel sufficient to perform the work specified (instead of vetting by abstract standards); compliance with local laws; and integrity as shown by past business dealings. Sounds like a text book approach to vetting Double O's.

If we accept that off shore outsourcing is all about price, sealed bidding becomes a powerful tool.

Company News

Free Monthly Webinar Series

Beginning in June, James River Consulting is offering monthly webinars on service provider contracts. Look for postcards in the mail announcing upcoming dates and times. You can also visit our Web site for dates/times, access info and slide downloads.

There is no charge for the webinar (other than the cost of the call). The webinars are 30-45 minutes with Q&A and provide practical, every day advice that you can put into effect immediately and inexpensively,

with huge returns on investment.

MTLC SaaS Cluster Public Event on Service Level Agreements

James River will be presenter at a 2 hour seminar on service level agreements (SLAs) in technology-based services industries. The event will be hosted by the Mass Technology Leadership Council in the September-October time frame. Go to www.masstlc.org for more info.



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