

September 2011  
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# Inside Outsourcing™



INTERVIEWED BY LARRY JANIS

## Ed Hansen, Partner Information Technology & BPO, Baker & McKenzie

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**LJ: What are the most important values that a law firm brings to the process?**

**EH:** I would start out with the value of a well crafted and negotiated contract. I think most lawyers experienced in this area can do a respectable job of papering a deal, and this is certainly an important value that a law firm can bring to the process, but I don't believe a client should be satisfied with that.

Anyone who is anticipating a significant outsourcing should think about using the contracting process as one of the first steps in its change management program. In this light, the ability of the vendor and client to form a high performing team is very important, and the sourcing/contracting process is a great place for that to happen. Once you're in transition, your new outsourcing deal is being judged by your users and that's not a great time to be storming, norming and all the other stuff that comes along with team building. If you have a deal lawyer who understands this and knows how to work this into the pre-execution process, it can be a huge value.

### FROM THE EDITOR

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Inside Outsourcing's goal is to provide you with articles of interest and with a forum for the exchange of information in this rapidly evolving industry.

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A good deal lawyer will also bring the ability to help the parties develop the economic drivers that will encourage behavior on both sides to achieve the intended outcomes. Unfortunately, in too many complex deals, such as outsourcing, the parties believe they can overcome basic economic flaws with strong contracting, and that really doesn't work very well. This is why customers can have dozens of service levels that are all in the green and still be dissatisfied. The contract has to work because the deal works, and not the other way around. Bringing that experience is a value the lawyer should add.

In addition to crafting a good contract, encouraging the right working relationship between the parties and helping with the commercials, if the deal lawyer is with a good outsourcing law firm, he or she will have the ability to bring resources to bear that can confirm the viability of the deal and help avoid unintended consequences. For example, when the deal is multi-country, having outsourcing-savvy local country expertise to make sure there aren't privacy, compliance, tax, HR and other issues that would prevent the deal from achieving the intended benefits is invaluable. The right deal lawyer, backed by the right law firm should provide real value on the commercial side and help avoid some serious unintended consequences.



***“ In addition to crafting a good contract, encouraging the right working relationship between the parties and helping with the commercials.”***

### **LJ: Have the buyers of outsourcing become more sophisticated?**

#### **Explain.**

***EH:*** These deals have had notoriously high rates of dissatisfaction on both the buy and sell side, so I think we'll have to wait and see how this generation of outsourcing compares to the past especially after the economy stabilizes. I also think there is a difference between getting better at closing deals, and getting better at closing deals that work.

In the early days, we saw customers treat outsourcing in the same manner they treated their most important and confidential deals. It wasn't unusual to conduct all of the planning, vendor selection and negotiations off-site with a small handful of customer personnel. In those days there were only a couple of law firms who worked in the area, and very few consultants, and the industry was really trying to figure out what success meant.

As time went on and outsourcing became more common, much of this mystique went away (I think for the better), but companies still treated outsourcing as a very serious step. Experienced in-house resources were scarce, and outside help began to emerge as its own industry. Sourcing processes evolved that were aimed at standardizing vendor selection, and when you think about it – that makes sense. Even “easy” outsourcing deals tend to be complicated, and through standardization a buyer is able to feel comfortable making decisions on a quantitative basis that, with more experience or less complexity, would be better made qualitatively. Unfortunately, many deals in this generation created unhappy customers and unhappy vendors and I believe that the procurement process was a major contributor to that. When you have a situation where both parties are unhappy in a deal but neither is breaching the contract, that should be a wake up call that something is amiss. .



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Fast forward to today, and we have a more mature market. Some customers have been through outsourcing and understand value and others are still making cost plays. I think the customers who really “get it” understand the relationship between cost and value and don’t confuse one for the other. A process that over-emphasizes cost may be a viable tactic in the short term, but there is opportunity cost to consider and you often see the strategic failures in these tactics when it’s time to renegotiate. The more sophisticated customers are able to drive cost, but do it in a way that doesn’t neglect value. And the really good ones can do it in a way that encourages the longer term benefits to mature as well.

**LJ: What do the third party advisory firms (e.g., TPI, Deloitte, and KPMG) add to the process?**

**EH:** I think the advisory firms would probably tell you that each has a unique skill set and that they bring different values to the process. Having done deals with and without advisors I can say that a good advisor can be an incredible asset, particularly when the customer requires strong subject matter supplementation. It’s always great to work a deal with a good advisor who brings strong subject matter expertise and an open mind.

That being said, there are a couple of traps that customers can fall into, through no fault of the customer or the advisor, that really need to be avoided.

The first is that, unless there is a very good reason for it, a customer should not outsource their outsourcing to the advisor. The *process* of buying outsourcing has to form the foundation of the ongoing relationship in order for the long term deal to work. It doesn’t help the customer to have the advisor forming the relationship on the company’s behalf. I have seen deals where the customer was absent from nearly every important discussion with the outsourcer, and, in most cases, that’s a mistake.

None of this is in any way meant to be critical of advisors – just some observations for customers to think about so that they don’t put their advisors into a position where they can’t provide the best benefits.

The other trap is doing the advisor’s last deal. Of course, advisors are hired for their experience. But part of that experience should allow them to help the customer fully understand how the customer’s objectives meet what the market has to offer at that time. It is notoriously difficult to fully understand requirements in certain types of transformational work. When that’s the case, the process needs to be designed to flesh them out based on market conditions and the customer’s unique value proposition.



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What the market may be able to offer changes over time, and sometimes that change can be substantial. As long as a customer is going through all the trouble of doing this, it may as well get the most out of what the market will give at that time and not be burdened with a rigid process that reflects the last requirements from the last deal for a different company.

***LJ: What are the top five goals your clients are hoping to achieve in outsourcing a function?***

***EH:*** This is an interesting question. If you read the objectives section of outsourcing contracts they usually talk about goals like process standardization, operational efficiencies, favorable accounting treatment, scalability and cost savings. When we talk to clients about renegotiations, the most common complaint about the supplier is a lack of partnership. This is interesting, I think, because even when the stated objectives were met (including cost savings), the ability to partner with the provider is a pretty consistent underlying requirement that is often neglected. This is why, even when cost savings and other objectives are critical and must be met, the deal that is struck has to drive the desired behaviors economically, and the governance model has to give the parties the ability to make the relationship work for the requirements that aren't necessarily in the contract.

***LJ: From a legal perspective, are there significant differences in the approach to an ITO versus a BPO deal?***

***EH:*** There are a set of baseline issues that have to be dealt with in any outsourcing. There are always privacy concerns, choice of law, tax, dispute resolution and similar issues that have to be addressed. The major difference is that a BPO is more likely to require substantive expertise in the legal environment surrounding the area outsourced than in an ITO, and the supplier may be more likely to have substantive obligations, more along the lines that the customer has in providing the services itself.

Interestingly, Baker & McKenzie recently conducted a survey of outsourced customers (both ITO and BPO) to determine where they perceived the greatest value leakage in their deals. The most significant cause for value leakage in the customers' minds was poorly defined or incompletely described services in the statement of work. We need to remember that the SOW is part of the contract and treat it that way. This is where a strong partnership between the lawyers on the deal and the subject matter experts (internal or from an advisor) really pays off, and is a good lesson for both ITO and BPO.

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**LJ: What has allowed you to be successful?**

**EH:** I have been fortunate over the years to have worked with some very talented and creative colleagues and clients. I have had the privilege of working with some of my clients for close to twenty years, and many have gone through massive structural changes in that time. When someone in my position has that opportunity, you see how teams form and how internal organizations succeed and how they fail. You also have the opportunity to play a part in dispute resolution and see which negotiating and contracting tactics work in the long term, and which just make you feel like you've won something at the table but come back to bite you later on. When I look back, I'm very proud that many of the teams I have been on have done some really good, innovative deals. I can also say without any hesitation that the best deals were done by the best teams, both on my client's side and on the provider side, and I was lucky to have been a part of that.



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