Matchmaking:
How to Choose Your Sourcing Provider

This EquaTerra Position discusses what companies need to do to ensure they select the right HR outsourcing (HRO) provider. It sets out to help HRO buyers establish what they want from their service provider by outlining the key questions in a series of assessment categories. With a plethora of HRO service providers in Europe, finding the right one, or right combination, for a particular company's business needs and culture is not always straightforward. As it can cost a company and its short-listed providers over one million Euro to compete for and enter into an HRO contract, it is important to do the right homework at the outset. Whether a company is buying payroll bureau services, outsourcing its learning function or negotiating more comprehensive multi-process transformational HRO, it needs a rigorous approach to understanding what it wants to buy, who it wants to buy from, and how it will be managed once the deal is done. Only when these items are agreed will a company be able to find a partner to meet its needs.

First, a company needs to know what it wants from its outsourcing contract. This can be harder than it seems, especially for HR in Europe, where there is so much potential for variation and complexity. To ensure the benefits and savings derived meet business objectives, and that providers prioritise the bid, EquaTerra recommends creating an HR Sourcing Strategy document that frames each requirement.

This Sourcing Strategy document typically encompasses:

- **Scope** – What processes, geographies and languages are required? What is the requisite level of excellence?
- **Delivery Model** – What delivery style? Which delivery channels? Where can service be provided from? What is the desired level of consistency?
- **Resources** – Whose assets will be used? How will in-scope and retained people be treated? How will severance costs be handled?
- **Change Approach** – How and when will the service transfer happen? What changes need to be made, and how fast?
- **Technology** – What new technologies are expected? How will these link to the rest of the company? What will happen to the old technologies?
- **Relationship** – What will the relationship with the selected provider be like?
- **Commercial** – What pricing model will be used? How variable and/or transparent should the price be? How long will the contract be for?

The HR Sourcing Strategy document should be used internally to socialise and agree the desired approach. Checks should be made to ensure the team responsible for assessing and negotiating with the service provider has the authority to make decisions, and that commercial expectations are compatible with likely purchase requirements. For example, when contracting for payroll services, do not expect wholesale change in the HR function, and do not buy transformational multi-process HR outsourcing and expect to use the company's temporary labour contract as a template.

As the strategy evolves, the team will need to build a solid set of data and information about its current situation. This is called baseline information, and should include:

- Definitions of the services to be purchased
- Details of the people costs currently incurred to provide the services
- Details of the third-party and other costs required to provide the service
- Details of the current HR IT environment
- Business volumes within HR
- Service levels provided by HR (not many organisations have this, so it does not matter if this is a small data set)

This baseline information is used to validate assumptions, create a business case and offer the contract to the market. Most large, distributed organisations find pulling this information together exceptionally difficult, but it is a necessary pain. The more facts a company has about its current situation, the better placed it is when shaping and negotiating the contract with the provider.

Once a company is sure of its own needs, it can assess these against what service providers have on offer. Diverse and dynamic, the European HRO market can be hard to navigate. Of the range of providers some are specialists, and many offer comprehensive HRO services, but all have strengths and weaknesses.

Using the following assessment categories can help establish which service provider will best meet a company's outsourcing needs. Each category is segmented into key factors or capabilities. Most companies take a team approach to this evaluation, with each team member ranking the categories and factors by applying different weightings to each and then comparing them to one another.

This "rack and stack" approach is common. Companies should perform this exercise in a series of successive iterations based upon frequent interactions with the most likely HRO providers. They will notice their rankings change over time as they become more educated on what service provider capability exists, and how the provider interacts with the company's selection and delivery team. An important action is to ensure the provider's delivery team, not just the sales team, is part of these interactions. After all, you will need to co-exist in the outsourcing relationship for five to 10 years, while the sales team is only around for six months.

Provider Assessment Categories

1. Relationship Skills and Culture

- Trust: What do your instincts tell you about the service provider? What do other clients say?
- Cultural fit: How does the team characterise the HRO provider? Are they relying on stereotypes or eyewitness accounts?
- People values and dedication: What level of HR investment does the provider have in its own operation? Is its head of HR well respected? Does the head of HR report to the CEO?
- Hiring client personnel: Is the provider willing to hire your key personnel? Are the compensation packages comparable? What is the retention rate of previous client personnel who have transitioned to the HRO provider?
- Governance approach: Is there a formal, structured plan for managing the relationship once it is consummated? Are there escalation policies and clear roles and responsibilities?

2. Functional Capability

Perhaps the most important category, HR functional capability, is critical to evaluate. Key factors include:

- In-place capability: Does the provider have the necessary resources? Or does it plan on making an acquisition or a set of key hires?
- HRO is core: Does this business line receive more than its fair share of investment, talent, and management attention within the provider organisation, or does it play second fiddle?
- Service centres: Where are they located? How many? How long have they been operational and in production?

- Third-party management: Is the provider willing to manage existing third-party HR service contracts such as benefits or training agreements?
- Alliances: What formal alliances exist for delivery of HR capabilities the provider may not organically have? Does it routinely work with HR consulting organisations?
- Centres of excellence: Are there formal, designated centres of expertise such as recruiting/staffing or compensation and benefits?

3. Technology

- ERP systems: Does the provider support HR ERP systems? Does it support more than one ERP platform (Oracle and SAP for instance)? Can it support more than just the HR module in the ERP system, e.g. finance and accounting?
- Transactional applications (current and future): Does it have any HR transactional applications currently in production, such as payroll or recruiting/staffing? Which applications does it plan on deploying and when?
- Skills and expertise: Can it handle complex IT integration, interface and conversion projects?
- Business continuity: Has it provided for disaster backup and recovery services? Can it move the work to different hot sites and/or geographic locations if a disaster necessitates?

4. Outsourcing Experience

- Reputation and track record: How do industry peers feel about the provider?
- Management: What are their levels of their strength, depth and breadth?
- Strategy and competitive position: What do equity analysts say about their prospects?
- Financial strength: What does the investment community think?
- Commitment to BPO: Does it possess a dedicated BPO unit or is BPO a sideline business? Is its success critical to the long-term success of the service provider?

5. Quality

Another category that should receive more attention, but often does not, is quality. While many outsourcers have embarked upon continuous improvement and quality programmes, others have not demonstrated the same commitment to these standards. Key factors to consider are:

- Six Sigma and Total Quality Management: How many black belts does the provider have? Does it have a formal quality programme? What levels of resources are devoted to it?
- Certifications: What certifications does it possess in the HR, IT and outsourcing industries?
- Service levels: Does the provider have a robust understanding of service levels by each of the 22 HR processes? What are its service levels for its internal HR department? What are the service levels in its processing centres? What levels of service are its customers experiencing? Does it practice what it preaches with its own personnel?
- Continuous process improvement: Does it track monthly and annual process improvements? Will it commit to continuous process improvement in your relationship, and for what period of time?

6. Transition and Implementation

After an HRO contract is signed the really difficult work begins, namely transition and implementation. This category includes capabilities such as:

- HRO provider delivery team: Has the company team interacted frequently with the service provider delivery team responsible for transition and implementation? Is it confident in the provider's abilities?
- Testing and acceptance: What approvals are in place for testing and acceptance prior to the provider transitioning work, rolling out new processes, or changing geographic scope?
- Offshore, nearshore: What approvals does the company team have for moving work to Canada or Mexico? India or China?

EquaTerra Get to what matters.

- Change management: Does the provider possess sophisticated change management skills, resources, and methodology? Are all the key stakeholders included in the change management programme?

7. Client Offering

The final category, and perhaps the most vital, is the client offering, or "what is this HRO provider going to do for the company?" Included in these key considerations are:

- Scope: Is this a Europe-only deal? Can it be extended to other countries? What HR processes are included/excluded? Are all active employees covered or only those that are non-union?
- Financial structure and pricing: Is it a fixed-priced deal or based on a per active employee basis? Is what is being proposed the best financial structure for the company? What if activity volumes increase or decrease dramatically?
- Net Present Value (NPV) and cost reductions: What is the NPV in year one versus year two? Does one provider understand your timing of the financial benefits better than its competitors do? What is the magnitude of the cost reductions? Where is the risk of the cost reduction on the company and the provider?
- Flexibility: Does the service contract allow for maximum flexibility over the five-to-ten-year term as the business changes, e.g., in the case of a merger or acquisition or divestiture? What happens, for example, if business volumes fall by more than 20 percent?
- Terms and conditions: Does the service contract contain key industry standard terms and conditions such as the right to use third parties and termination for convenience?

While this list is not exhaustive of all the potential categories that have been used to evaluate HRO providers, it forms a good basis for trying to assess the best fit with a prospective HRO partner.

Companies must decide how many service providers will be offered the opportunity to go through the "match-making" process. For a sizeable contract, it is worth running a comparative process with two (or a maximum of three) "finalist" providers. A company can work in much more detail with two providers than five, and will receive better proposals as a result.

If a company's assessment and analysis process of itself and potential service providers is tight, the result will be a smoother negotiation and contract phase, which in turn will lead to a more successful outsourcing relationship.

About EquaTerra

EquaTerra sourcing advisors help clients achieve sustainable value in their IT and business processes. Our advisors average more than 20 years of industry experience and have supported over 2000 transformation and outsourcing projects across more than 60 countries. Supporting clients throughout the Americas, Europe, and Asia Pacific, we have deep functional knowledge in Finance and Accounting, HR, IT, Procurement and other critical business processes. EquaTerra helps clients achieve significant cost savings and process improvement with internal transformation, shared services and outsourcing solutions.

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