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The Changing Face of Outsourcing and the HR Function

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This article assesses the likely HR implications of recent changes in the structure of the outsourcing market. It also suggests ways in which the HR function can become a contributor of solutions, not obstacles, to the smooth running of outsourcing projects.

Outsourcing has come of age over the last decade, with resulting shifts in the pattern of employment. More and more organisations have outsourced both core and non-core functions to specialist service providers and, as services have passed one way, jobs and employees have passed the other way, from customers to service providers. But despite the maturity of the outsourcing model and its by now broad acceptance as a management tool to increase companies' efficiency and profitability, in many cases the biggest stumbling blocks to the smooth progress of an outsourcing project remain the HR issues. This need not be the case. There are some basic structural steps which, if followed in an outsourcing transaction, will help to reduce the potential for HR issues to de-rail a project or get blown up into potentially deal-threatening problems.

OUTSOURCING HISTORY

Outsourcing is the transfer of internal business processes and capabilities to an external service provider. The basic commercial proposition is that the service provider will do what the customer currently does, at the same or a better level of performance, and for the same or a lower price. It's possible that there may also be an element of business or process transformation or quality improvement.

The concept of handing over functions to a specialist service provider is not new, but the practice acquired the outsourcing moniker twenty or more years ago. Since that time, outsourcing has moved from basic facilities management through outsourced IT service provision, to networks, back office processing and into increasingly core areas of customers' functions. Many organisations are now almost "virtual" in some areas, such is the extent to which they rely on external service providers.

Alongside the growth of outsourcing came the offshoring trend for services that could be delivered remotely – and for customers who perceived even greater savings from leveraging lower labour rates offshore. Many large companies even set up their own "captive" outsourcing units in attractive offshore markets.

And then came the recent global recession. But, in fact, the outsourcing market held up well during the recession, although with changes in the pattern of distribution of outsourcing work. Specifically, the amount of business process outsourcing (BPO) that companies undertook was reduced whereas IT outsourcing (ITO, which typically produces more immediate direct savings) increased, and most companies took the opportunity to re-negotiate existing contracts.

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Now, the outsourcing market is undergoing a process of change in 2010 as world economies recover. CIOs and CFOs have saved most of the costs that can be saved and are turning again to fresh outsourcing projects and, in particular, to the pent-up demand for BPO. This is bringing back on to the table a range of issues for the HR professional.

OUTSOURCING AND HR

HR issues have always loomed large in outsourcing projects. Organisations underestimate the potential negative impact of HR mis-management at their peril. By its very nature, outsourcing involves a change in the pattern of service delivery – and that service delivery depends on employees, mostly well-trained and experienced, continuing to do what they have always done but ideally with better management and training and an improved subject-matter skill support network provided by the service provider. If those employees are treated badly, at best they lack motivation or incentivisation, and at worst they may end up leaving their employment altogether, being made redundant or being left employed by the “wrong” employer when their actual job function has moved elsewhere.

Traditionally, the task for HR professionals in outsourcing projects has been to manage smoothly the issues arising from the proposed transfer of job functions. In the UK and the rest of Europe, this means anticipating the effect of the Acquired Rights Directive and the Transfer of Undertakings Regulations which mandate that employees whose job function is transferred to a service provider follow their jobs. Some of the issues which the Acquired Rights Directive and TUPE throw up are second-nature for seasoned HR professionals, *e.g.*, consultation with employees “affected” by the transfer, not just with those whose job functions are in-scope to transfer to a service provider. For HR professionals within outsourcing customers, the bulk of such work occurs when a service is first outsourced, and it is their own staff who are to transfer to the “first generation” service provider. However, customer HR teams also have a role to play on exit and in “next generation” outsourcing when one contract ends and a secondary transition of staff from one service provider to another takes place. The task on those occasions is to work with outgoing and incoming service provider HR teams to ensure the smooth transition of their staff.

During the recession over the past two years, the prevalence of re-negotiated outsourcing projects over “as new” projects has meant that many customer HR professionals have found that the impacts of outsourcing have been less on their recent radar screens, *i.e.*, since any redundancies or HR issues associated with re-negotiations have tended to be for the outsourcing service provider and not for customers. This has left HR teams free to deal with internal streamlining or downsizing issues.

HR AND THE “NEW” OUTSOURCING

As noted above, the emphasis in the outsourcing industry is changing and this will have consequences for HR professionals.

Already, the duration and size of an average outsourcing project has become smaller – as companies have realized that full-scope, end-to-end outsourcing of their entire operations is unwieldy and there are more efficiencies to be had from smaller, more targeted outsourcing deals. One impact of this trend is, of course, a more rapid turnover in outsourcing projects and the need to manage TUPE/ARD issues in the next generation. It's tempting to say that the issues in such a situation are for the respective incoming and outgoing service providers to manage. But, in reality, it's the customer's service that suffers if employees are not properly dealt with (or, even worse, if the right employees are not transferred or are cherry-picked off on to other work) so it's in the customer's interests to engage fully in the process, even if only as referee, to oversee fair play.

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As economies emerge from a recession, the outsourcing focus is once again on offshore outsourcing. The increased prevalence of offshoring (and, especially, the presence of “mixed” teams providing perhaps onshore service delivery of front-line services but backed-up by a strong offshore-based support function) also causes HR issues because, of course, TUPE doesn’t apply to the transfer employees overseas, or so most people believe. In fact, TUPE does apply to any outsourcing from the UK. Accordingly, if a service is being offshored for the first time, TUPE will apply and HR teams will have to inform and consult in the usual way. That, however, is as far as TUPE usually goes, as employees are treated as redundant in their UK roles and do not normally transfer across to work for the offshore service provider. This means more work for HR teams in looking either to redeploy staff prior to transfer, or manage the redundancy process with an offshore service provider.

Additionally, many companies are looking again at the option of either setting up a captive outsourcing entity or some kind of hybrid offshoring structure model – an approach that was in vogue in the early days of offshoring as companies dipped a toe in the water, but which is now showing signs of a return to fashion. This will require HR teams to work out how to manage blended internal and external workforces operating the same set of services, how to remotely supervise their outsourcing service provider’s HR management, or to grapple anew with the HR and employment laws of foreign jurisdictions.

The current rise in prominence of BPO as opposed to ITO produces issues associated with the prolonged investment nature of many BPO deals (*i.e.*, whereas ITO deals tend to be of the “short, sharp shock” variety with changes in the workforce taking place rapidly and at one time at the start of a deal, many BPO projects involve investment and a process of transformation which means that the HR implications are spread over a period of time and are not immediately known at the time when the outsourcing project is initiated). This means that HR professionals will increasingly be faced with more complex consultation and transition processes to manage, and they need to be involved much more closely in the outsourcing process.

Beyond the “big event” issues of employee transfer, the increased acceptance of outsourcing as a fact of business life requires HR professionals to adapt to “indirect” management of key service delivery teams via service providers’ own HR functions. While many service providers naturally resist their customers’ attempts to micro-manage their internal HR processes, there ought to be a role in the governance processes for any successful outsourcing that allows HR co-operation between the customer and service provider HR functions. Their joint goal ought to be the make sure that employees on whom the service depends are motivated, incentivized, well-trained and aware of both customer and service provider priorities.

PRACTICAL INVOLVEMENT OF HR IN OUTSOURCING

Although very few, if any, proposed outsourcing projects have been abandoned purely because of HR issues, deals can very easily be temporarily derailed if these issues are not dealt with appropriately and at the right time. Best practice suggests that the more successful projects occur when HR teams are closely embedded into outsourcing projects throughout their lifecycle, in order to reduce current and future HR issues. What this means in practice is early engagement of HR professionals, *e.g.*, to scope out potential “red flag” issues. Once the decision to proceed has been taken in principle, HR professionals should be involved pre-tender to determine the agreed position on TUPE, so that it can be made clear to prospective service providers in the tender documentation what’s going to happen as regards staff transfer. This will allow those bidding to factor into their bid associated staffing costs, thereby avoiding unpleasant surprises for both parties down the line.

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HR professionals should also help the business early on to identify key employees within their own organisation and key roles within the service provider's. HR professionals' involvement should continue during the tender process to ensure that bids accurately reflect the customer's position on TUPE.

During the contractual negotiations, advice from HR professionals should be sought on some of the contractual terms, e.g., restrictions on changes to staff terms and conditions and movement of staff in and out of scope pre-transfer, and also on the appropriate restraints to be placed on service providers post-transfer. These often include a requirement to maintain terms and conditions or avoid redundancies for a fixed period after transfer.

Finally, and perhaps most crucially, HR must play a key role in employee communications. This will involve both briefing managers so that the correct messages flow down to staff, and also being prepared themselves to handle direct questions from staff. This is a pivotal role, and crucial to the success of any outsourcing project.

At go-live, HR professionals will be responsible for overseeing the transfer of transferring employees and their data to the service provider. HR professionals will also have an important on-going role once the outsourcing has started, especially during the critical early months when the project is bedding down. This will include communicating to retained staff, as well as assisting the business in monitoring the success of the project.

Finally, at exit, HR professionals may need to assist the outgoing and incoming service providers with issues related to staff transfers and the handover of employee data. The "fair play" role is crucial here as the customer has an overriding goal to ensure a level playing field between bidding entities and, without a steadying hand, incumbent service providers often hold back as much employee data as possible so as to secure an edge in the bidding. Claiming that HR data cannot be released to competing bidders may be correct for some data and at certain times, but the HR professionals ought to find ways to produce a common baseline of bid-relevant data (especially HR cost data) even if the data is largely or wholly anonymised.

This level of HR involvement throughout the whole process will ensure that the HR function is a real contributor, and in some respects key facilitator, of solutions, not obstacles, to the smooth running of outsourcing projects.

CONCLUSION

Outsourcing is here to stay. The challenge for HR professionals and their teams is to keep up with the changing shape of outsourcing projects initiated by their organisations. The HR issues and their solutions may differ depending on whether the company is an outsourcing newcomer or an old-timer into its second or third generation of outsourcing. The degree of exposure to offshore outsourcing may also affect the challenges facing HR professionals. The common thread that links successful outsourcings, however, is early engagement of the HR function in the outsourcing process. First-time outsourcers often leave HR issues until later in the process. For a range of good reasons, they rarely do so twice.

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