

# Playing to Win

*How do the best companies win at the game of outsourcing their supply chain? Here is an overview of how to build stronger relationships and gain greater value from your outsourcing relationships, based on the book **Vested Outsourcing: Five Rules that will Transform Outsourcing.***

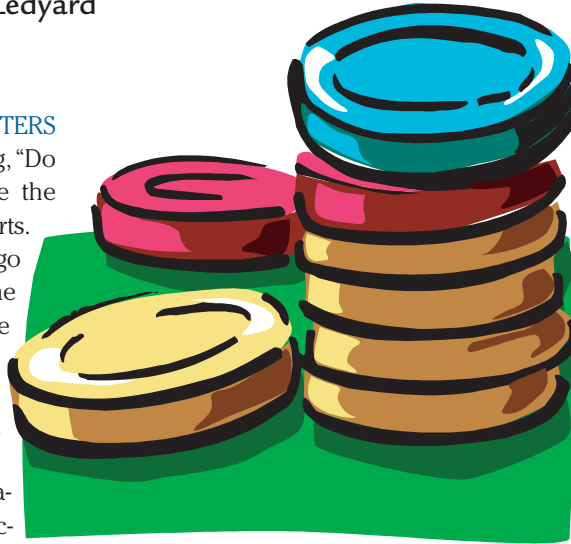
By Kate Vitasek and Mike Ledyard

PETER DRUCKER AND TOM PETERS have both been quoted as saying, “Do what you do best, and outsource the rest.” Both are highly credible experts. But what they don’t say is how to go about doing it the best way. The result? Today companies outsource more than \$6-trillion worth of services; some are clear winners, some are clear losers, and most fall somewhere in between.

So how do the very best companies win at the game of outsourcing? That is the question that the University of Tennessee has been studying as part of a research project funded by the United States Air Force. The findings? Companies with the very best outsourcing agreements all followed five unspoken rules for building strong relationships and contracts with their service providers. We codified our learnings in our book *Vested Outsourcing: Five Rules that will Transform Outsourcing*. This book serves as a handbook for practitioners to build stronger relationships and gain greater value through their outsourcing agreements.

## The Definition of Winning – WIIFWe versus WIIFMe

A key component to winning in the outsourcing game is to change the definition of winning. While many organizations tout they have “partnerships,” our experience and research



found that most organizations have an internal desire to optimize their own self-interests and this comes across loud and clear in the contract terms and language of today’s outsourcing agreements. Unfortunately, this self-interested, “what’s in it for me” (WIIFMe) approach leads to sub optimization, higher transaction costs, and what we identify as 10 common ailments of outsourcing, which we outline in chapter three of our book.

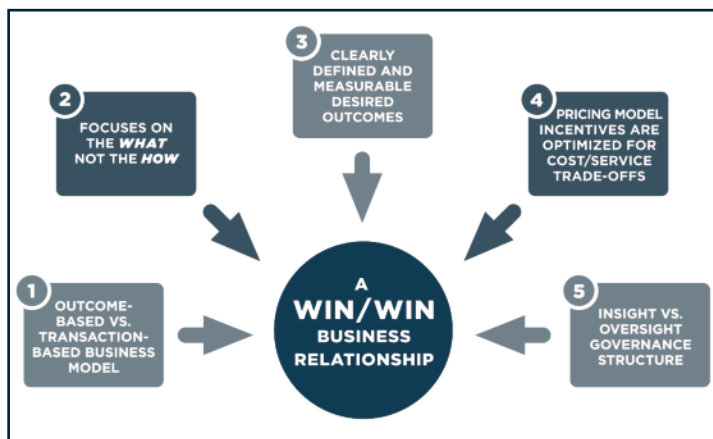
Our research revealed that the most successful outsourcing agreements

changed the definition of winning — creating a true win-win relationship — with both the company and the service provider each obtaining greater value from the relationship by working together. The best companies moved beyond WIIFMe thinking to a “what’s in it for we” (WIIFWe) philosophy with the goal to strive to increase the size of the entire pie (unlock a greater opportunity than is currently realized by either party) versus maximizing the size for any one player (e.g., lower costs at the expense of the outsource provider’s profits).

## Rules of the Game

The most successful companies not only changed the definition of winning to win-win, they also adopted the following five unspoken rules to help them craft solid contracts that supported their relationships:

• Outcome-based versus transaction-based business model



- Focuses on the “what,” not the “how”
- Clearly defined and measurable desired outcomes
- Pricing model incentives optimized for cost/service trade-offs
- Insight, versus oversight governance structure

In *Vested Outsourcing*, agreements are based on achieving results — not on the service provider

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tion to another possible supplier would be made easier.

#### **Access to and Pricing of External Software Solutions**

Traditionally, pricing of software license fees often prohibited the adoption of new technology. Most software providers required the expensive purchase of the full license to allow use of the software. In addition, software providers didn't like usage of the software for many companies outside of the company actually using the license (e.g., 3PL customers). As a result, it was sometimes difficult for a 3PL to adopt and implement new functionality to be used across their customer bases.

Recently, new pricing models, including Software as a Service (SaaS) which allows paying based on amount of use, have made it easier for 3PLs and their customers to evaluate the value of software solutions. There is also more flexibility in pricing and some supply chain software providers are actually targeting 3PLs as their main sales demographic.

#### **Communication**

Communication issues also contributed to the IT perception gap for 3PLs. Being able to clearly show how 3PL technology could benefit shippers wasn't easy in the past, particularly if legacy systems were used to link 3PLs and customers. Now, third-party providers have become better versed in providing concise answers to questions on how they can create value for their customers. Having experienced and addressed integration issues has made 3PLs more conversant in showing value for the use of information technology. Overall, the level of IT knowledge shared over time for both 3PLs and their customers has increased, thereby reducing the fear of IT issues.

While there is still a sizable gap in the perceptions of 3PL IT capabilities, it has been reduced significantly over the last several years. Since admitting a problem is the first step in resolving it, the visibility of the 3PL perception gap has brought attention and focus to this important area. Based on progress in the 3PL IT area, the gap should continue to narrow.

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performing tasks and getting paid for transactions. The organizations work together upon a foundation of trust, with mutual accountability for achieving the outcomes. The emphasis moves from measuring detailed service level agreements towards mutual accountability for outcomes. The service provider is challenged to put skin in the game to bring innovative solutions that yield improved performance and lower total cost of ownership. When the service provider achieves the results they are rewarded with additional profits. This is all managed under a carefully thought out governance structure based on insight rather than having a conventional vendor account management team micro-manage the service provider.

#### **Investing in Vested Outsourcing**

For the service providers, vested outsourcing is an opportunity to exercise greater flexibility in deciding how support is provided, to ensure cash flow stability through long-term contracts, and to increase revenue by rewarding the service provider's investment in improving processes. For the company that is outsourcing, it is a chance to obtain improved performance while decreasing costs and assets by partnering with a highly competent and properly motivated firm.

For those wishing to explore vested outsourcing further, we offer four resources:

- Our book, *Vested Outsourcing: Five Rules that will Transform Outsourcing*, has been published by Palgrave Macmillan and offers a comprehensive guide for developing successful vested outsourcing partnerships. It is available at Amazon.com.
- The University of Tennessee offers a three-day open enrollment class at its Center for Executive Education, "Vested Outsourcing: Buying Results, Not Activities!": <http://VO.utk.edu>. You can contact Bric Wheeler at the University of Tennessee to learn more at [BWheeler@utk.edu](mailto:BWheeler@utk.edu).
- Visit our blog at <http://www.vested-outsourcing.com> and receive additional resources, tools, and insights offered by the authors.