



Establishing a Baseline for Outsourcing Decisions

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BACKGROUND

Many companies are considering outsourcing various aspects of their in-house operations. The driving force behind this decision is often cost reduction, organizational restructuring, mergers and acquisitions. In the Information Systems organization outsourcing can range from buying a software package to outsourcing all software development, support and data center operations.

Companies who have ventured into outsourcing arrangements have had both positive and negative experiences. The outcome often depends on the proper selection of functions to be outsourced, how the original contract is structured, how the customer/vendor relationship is managed and how the end results are measured. If done correctly, outsourcing can be a win-win situation for both the customer and the outsourcer.

MAKING THE DECISION

Making the decision to outsource software functions is difficult and is often based on frustration rather than facts. The decision should be based on a solid understanding of costs, departmental performance and business strategy. Software metrics should be utilized to establish a baseline for productivity, quality and the costs associated with providing services in-house. The company baseline should then be compared to other organizations and outsourcing providers. This analysis will result in the realization of activities that should be

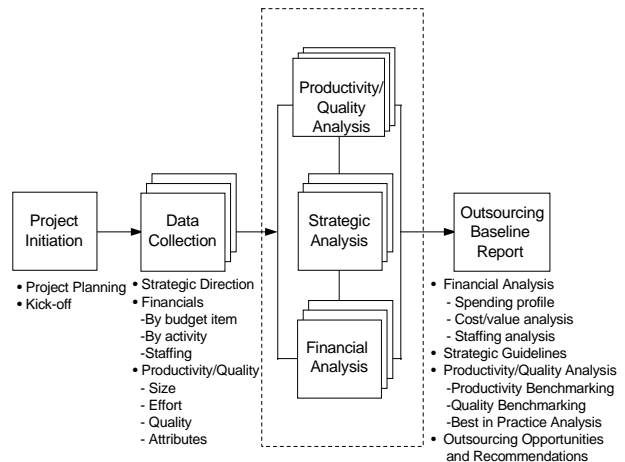
performed in-house and those that should be outsourced. Having quantifiable baseline data also allows a company to enter into an outsourcing venture knowing the objectives they want to achieve, the anticipated benefits and the metrics required to measure and manage the contract.

ESTABLISHING THE BASELINE

In order to identify the functions most appropriate for outsourcing, a broad reaching baseline of historical performance is preferred. This will ensure that the functions selected for outsourcing represent those that can contribute the most to achieving the expected goals from outsourcing such as cost reduction.

Developing the baseline requires a structured approach. The diagram below depicts such an approach and includes three primary analyses which are further described below.

Outsourcing Baseline Approach



STRATEGIC ANALYSIS

The Strategic Analysis evaluates the major factors that will influence the selection of outsourcing options. This analysis will answer a number of critical questions including:

- How will business competition and economics influence outsourcing decisions?
- Should we focus our resources on development, maintenance or operations?
- What are the options for outsourcing and what are the risks and benefits of each?
- How does the organization structure impact our decisions?
- What is our applications/maintenance strategy?
- How dependent should we be on outsourcers?
- Are there any major initiatives that may influence our outsourcing decisions?

The results of this analysis are guidelines which will be used in conjunction with financial, productivity and quality data to select those functions most appropriate for outsourcing.

FINANCIAL ANALYSIS

This analysis focuses on the Information Systems (I/S) budget items and spending patterns. An I/S Chart of Accounts is utilized to collect financial data in order to gain a detailed understanding of the costs associated with software and hardware. The analysis provides two primary perspectives on the budget. The first perspective is to analyze spending by cost category such as hardware, personnel, facilities and other. The second perspective is to analyze spending by activity such as maintenance, operations, development and support. These analyses are then utilized to identify those items that are candidates for significant savings.

The financial analysis will also examine spending trends over time as well as staffing levels and mix.

PRODUCTIVITY/QUALITY ANALYSIS

The Productivity/Quality Analysis will measure software development and support in order to benchmark the performance of the current organization. This analysis is critical in determining the potential benefits (if any) from outsourcing. For instance, this analysis will determine if the current organization is more productive in new development than maintaining legacy systems. The results will determine where the major opportunities for outsourcing are and what potential savings can be expected.

The data collected for this analysis often includes: function points, level of effort data, project technical attributes, problems and defects, and project practices (tools, methods and processes). The analysis of this data will provide valuable information including: productivity rates, quality statistics, maintenance requirements and improvement opportunities.

The analyses that are typically performed include:

- New development productivity analysis and benchmark comparison
- Enhancement productivity analysis and benchmark comparison
- Maintenance productivity analysis and benchmark comparison
- Cost rates for Development, Enhancements and Maintenance with benchmark comparisons
- Defect analysis and benchmark comparison
- Best in Practice Analysis (methods, tools and environmental factors)

OUTSOURCING BASELINE DELIVERABLE

The Outsourcing Baseline Report documents the findings and recommendations from the study. The report will describe the outsourcing opportunities available and the expected cost savings. In addition, this report will answer numerous questions related to software

productivity, quality, costs, development methods and improvement opportunities. The report will likely include:

- Overview of Project Approach and Methods
- Strategic Guidelines for Outsourcing
- Financial/Resource Analysis
 - Spending profile
 - Trend analysis
 - Staffing profile
 - Target areas for cost reduction
- Productivity/Quality Analysis
 - Productivity rates
 - Quality rates
 - Attribute analysis
 - Cost rates
 - Benchmark comparisons
- Recommendations
 - Outsourcing opportunities (functions and application areas)
 - Expected cost/staff savings
 - Other internal improvement opportunities
 - Guidelines for vendor selection and negotiating
- Next Steps

BENEFITS

The Outsourcing Baseline will eliminate much of the up-front ambiguity in determining if outsourcing is a viable alternative. The baseline will provide detailed recommendations based on

quantifiable data. This will allow the organization to save time and money by efficiently selecting the most appropriate activities for outsourcing.

The baseline will also provide the necessary measures required for contract negotiation and ongoing management. Lastly, the baseline measurements can be used as the primary tool for evaluating vendor performance for outsourced functions. Historically, these measures have been used in determining the contracted levels of productivity and quality to be achieved by the outsourcer. More recently, outsourcing baselines have been used to determine the actual price paid to the outsourcer for delivering software projects and maintaining applications.

SUMMARY

Outsourcing can result in significant benefits for both customer and vendor. A winning approach needs to be followed to help ensure success. The approach begins with a baseline to fully understand the environment from a strategic, financial and productivity/quality perspective. With this understanding the appropriate opportunities can be identified, negotiated, outsourced and managed.

About the author

Scott Goldfarb, President of Q/P Management Group, wrote this article. Mr. Goldfarb is an international consultant and speaker with over thirty years of software experience specializing in helping organizations improve software quality and productivity through measurement.