

White Paper

By Kathleen Goolsby

Offshore is not Offhand

Recommendations for Effective Offshore Outsourcing

Introduction

The use of offshore capabilities is changing. Certainly, the most common activity still results from tightened budgets, causing U.S. firms to turn over their important, non-core processes either to outsourcers in other countries or to U.S. outsourcers with a component of skilled labor in other countries. Offshore outsourcing began as a solution for lower labor costs, enabling a U.S. firm's IT people to work on more strategic projects. It grew in acceptance with recognition of the high programming competencies of IT workers primarily in India doing legacy work on Y2k projects.

As acceptance has grown and risks have decreased, the types of work being outsourced to offshore firms include a broader selection of activities, most closely impacting a company's core competencies and competitive advantage. A growing number of offshore firms now deliver cutting-edge Web solutions for e-Business, and many provide higher quality capabilities in developing innovative software solutions than U.S. firms are able to accomplish in-house. Firms expanding their global reach depend even more on offshore outsourcers with cultural specialists in particular countries.

Even so, success is not guaranteed by using offshore outsourcers. In fact, there are potential problems unique to using offshore teams; but those problems can be minimized

by using best practices and taking the time up-front to ensure all potential difficulties are accounted for in the contractual documentation.

As with any outsourcing arrangement, an offshore deal must be structured with the following principles:

- clearly define the results the buyer wants to achieve;
- put in place clear, objective service level specifications to measure the results;
- build flexibility into the contractual documents;
- align the supplier's interests with the results that are key to the buyer; and
- provide an effective governance structure to manage the ongoing relationship.

Mistakenly, some companies go into offshore arrangements without realizing that these principles apply even if the offshore work is for a one-time development or implementation project rather than ongoing services.

Understandably, there are further principles that uniquely apply to minimizing risks and ensuring success in an offshore outsourcing arrangement; these, too, must be handled up-front before contracts are signed. This paper presents case studies of four current successful outsourcing relationships that were nominated for the Outsourcing Journal's 2002 Editor's Choice Awards for outstanding outsourcing relationships. The four include:

[Citicorp/I-Flex Solutions](#)

[Duty-Free Shop Group/Cognizant Technology Solutions](#)

[Datawatch/Vested Development](#)

[TIBCO/Aalayance](#)

With each of the four, we show the difficulties they encountered, the best practice solutions put in place, and the results achieved.

Overview of Advantages and Disadvantages

As the outline below illustrates, advantages or disadvantages of offshore outsourcing often are based on the same factor. Whether the end result is a source of benefits to the buyer organization or a source of problems depends on the up-front work done to minimize risks before the contractual documents are signed.

Advantages	Disadvantages
Significant savings in labor costs	Additional up-front costs because of distance
Time zone differences	Time zone differences
Corporate and country culture differences	Corporate and country culture differences
Higher quality of skills	Communication difficulties
Motivated workers who are career oriented	Contract jurisdiction if litigation becomes necessary

Case Study # 1

Offshore outsourcing proponents often tout the differences in time zones between the two parties as a highly beneficial arrangement that facilitates time to market. Marketing teams present the 12-hour time difference between India and California or the eight-hour difference from New York to Russia, for example, as a means of obtaining 24-hour work crews on development projects or 24/7 coverage for support projects.

The outsourcing arrangement in this case study highlights what can happen when there are time zone and distance factors impacting the relationship.

Case Study: Citicorp Development Center and i-flex solutions limited

BACKGROUND SITUATION:

Citicorp Development Center, a business unit of Citigroup, developed and produces a home banking software product (“Direct Access”), together with middleware that allows the product to integrate with all the front-end systems and mainframe systems throughout the Citigroup consumer businesses worldwide.

Because the Japanese marketplace has unique complexities from differences in coding for language characters as well as banking business requirements and offerings, Citicorp decided to outsource the application development and system integration of its Direct Access product for Citibank Japan. The decision to outsource was based on the need to ramp up quickly to meet the requirements of Citibank Japan, not allowing Citicorp enough time to find and recruit full-time employees with the right skill sets.

OUTSOURCED PROCESS:

Software development;
system integration.

CONTRACT:

One-year contract
signed in February 1998
with subsequent
continuing annual
renewals.

i-flex solutions limited was selected to handle the Citicorp projects because the outsourcer had staff on board with the requisite skills and also presented a compelling economic structure during the vendor evaluation process.

TIME ZONE FACTORS:

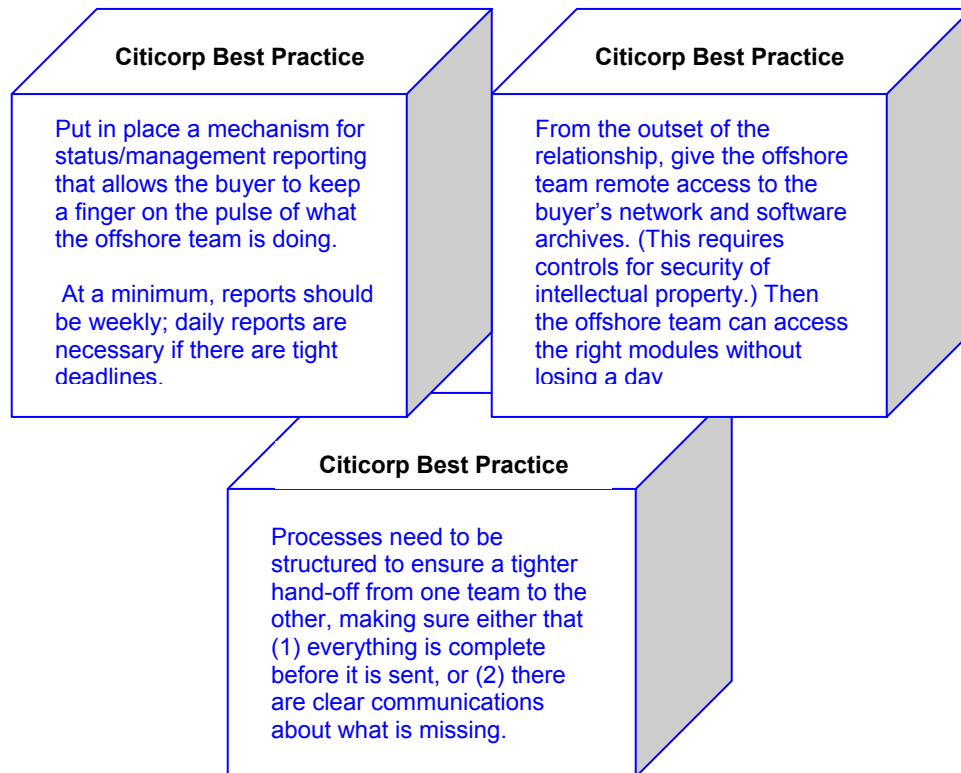
The parties began experiencing problems as soon as they started transitioning the work to the offshore outsourcer. Steve Saussy, Citicorp Development Center’s product manager, says the problems were overcome only through teamwork efforts from both parties. The

i-flex team is located in Mumbai (formerly known as Bombay), India. When it's 5:00 P.M. at Citicorp, it's 5:30 A.M. in Mumbai. "If we want to talk to them, we have to call them before they leave for work or after they get to work," explains Saussy, "and it takes most of them about an hour to an hour and a half to get to work. So we either have to stay up really late to catch them when they get in first thing, or we have to get up really early in the morning to talk to them at the end of their day." This limited window of time for communications means there must be minimal mistakes, for each mistake can cost a day's time.

In theory, Citicorp saw the offshore outsourcing as a way to achieve a 24-hour continuous development cycle. The people at i-flex would work their 12-hour day, and then they would hand off the project to Citicorp people who would plug it into their platform, finalize it and get it ready to ship to Japan, and then tell the i-flex team to send the next increment. In reality, there are problems if, for example, an i-flex worker hands off software via the server to Citicorp and, upon downloading, the Citicorp worker discovers it's missing a file. If the two teams are working side-by-side in the same time zone, that takes five minutes to resolve. Similarly, a 12-hour time difference can cause the parties to lose a day of production if a requirements document doesn't arrive when expected by the offshore team. The team members 12,000 miles away can spend a day sitting there twiddling their thumbs while waiting for the requirements.

Citicorp and i-flex worked through their time zone difficulties by taking a teamwork approach and ensuring that there were people on both sides of the world who were willing to get up early and stay up late. Building a good relationship among management of both teams is also crucial. Saussy says a buyer organization must build a relationship with its outsourcer so that the offshore team will let the onshore team know something has happened that may cause people to be idle and get behind schedule or otherwise run up the tab.

Citicorp's theory in using an offshore team as a strategy to get 24-hour development cycles was not misplaced. However, management controls need to be put in place up-front to overcome the obstacles in making sure that happens. Here's what they did:



Case Study #2

In any outsourcing relationship, there must be a concerted effort from both parties at the outset to build a new culture. They must understand how each company normally operates in such matters as proactive or reactive approaches; their decision-making processes; and the speed, flexibility and aggressive attitude toward escalating solutions to unexpected challenges. Adding language nuances, national differences in mannerisms and relationship approaches can inherently make an offshore outsourcing arrangement even more challenging.

Recognizing these potential issues, some companies are taking a more prudent approach toward working with an offshore outsourcer to minimize risks in cultural difficulties. Case Study #2 is an example of such a careful approach: starting with small projects and making sure things work well before ramping up.

Case Study: Duty-Free Shop Group and Cognizant Technology Solutions

BACKGROUND SITUATION:

Duty-Free Shop Group operates airport stores and off-airport stores in travel destinations. Located in Hawaii, Mid Pacific, Guam and Sai Pan, Asia, Singapore, Hong Kong, Malaysia, Korea, Sydney, and airport shops in throughout the continental U.S., Duty-Free sells liquor, tobacco and fragrance and luxury-brand items to travelers. Duty-Free's core expertise involves managing its supply chain from the manufacturer to the point where travelers purchase goods. In 1999, with 15 years old legacy systems that were complex to maintain, the company faced major investments in bringing its IT staff skills up to world-class level in order to achieve faster, higher-quality support services with lower operating costs. It chose, instead, to partner with an outsourcer with IT expertise.

Ron Glickman, Duty-Free's vice president of Information Technology, says his company looked at outsourcers in the emerging market of Eastern Europe but moved on because of political instabilities. Ireland and European outsourcers didn't present the long-term cost advantages. Their due diligence convinced them that India was a more mature market with significant market competition. Cognizant was selected because of its outstanding research and development capabilities and because it demonstrated flexibility and a willingness to change if things weren't working well.

OUTSOURCED PROCESS:

Production support and enhancement.

CONTRACT:

Master agreement signed May 2000.
Three-year contract signed August 2001.

STRATEGY OF STARTING SLOW:

They started by outsourcing the production support process to Cognizant, which uses an onshore/offshore model. At the outset, Duty-Free carved out only a small piece of its system, minimizing risks while giving the supplier the opportunity to prove it could make beneficial changes. Once the kinks were worked out, they moved to phase two, referred to as “Follow the Sun” support. In this phase, the supplier began taking production support calls from the data center and business users. The next step was a full-blown support agreement, turning over responsibility for maintenance and enhancements of Duty-Free’s legacy systems around the world. Support services for systems and applications in Duty-Free’s data centers in North American, Hawaii, Mid-Pacific, Asia, and Oceania regions are now consolidated at Cognizant in India.

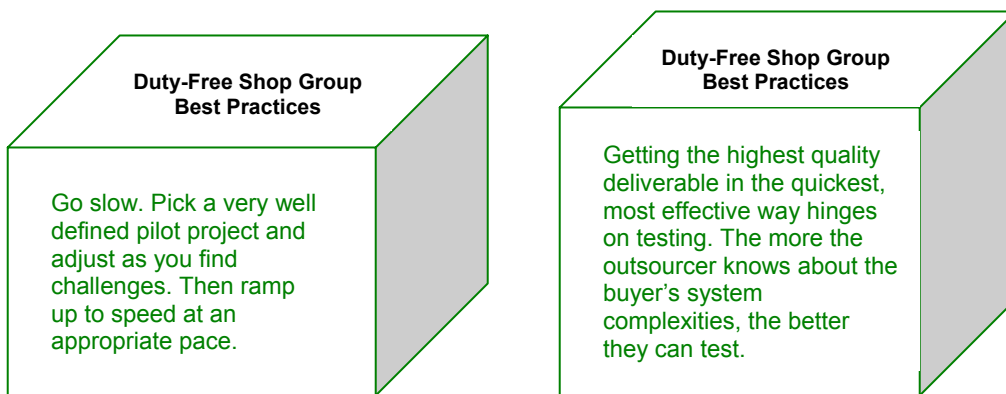
The progression in services has been accompanied by a progression in pricing structure. The parties began working together under a series of 90-day agreements as they learned about each other and experimented with the best ways to make their relationship work. For a year and a half, each new project or new phase of expanded services was handled with a separate work order under the umbrella master agreement signed in May 2000. Once the complete responsibility for support and maintenance was ready to be turned over to Cognizant, they signed a letter of intent in August 2001 for a new three-year agreement. The new outsourcing agreement includes gainsharing incentives for the supplier to reduce Duty-Free’s seven million lines of code and number of programs.

FLEXIBILITY:

Duty-Free’s best practice steady progression of increasing supplier responsibility, Duty-Free learned the value of having selected a supplier willing to be flexible and make changes. Glickman explains, “We found that the onshore resources were not as effective working with our business partners as we had hoped. So we sat down with Cognizant and talked to them about that, and two things happened. They changed some of the people.

Also we took more responsibility for the relationship and focused Cognizant more on the offshore components of technical delivery, which is their expertise. So we basically adapted the onshore/offshore model to work better in our environment. They are also good at bringing teams on demand to look at new technology opportunities for our new retail ideas. For instance, we are building a new store that will have plasma screens and video in the screens with content to attract customers to particular brands or products. So we brought Cognizant to help us look at what we can do from a technology side to make that work.”

Duty-Free believes the first key to success in offshore outsourcing is to perform due diligence to ensure the supplier selected is the right partner for the long term and is capable of bending to meet the buyer’s special needs. Two best practices resulting from this relationship are:



Case Study #3

Whether the distance between the parties in an offshore relationship becomes a problem depends partly on the number of interactions and whether face-time communications are required. The following case study presents a relationship that solved this potential challenge.

Regardless of whether the outsourced work is a one-time software development or implementation project or is for ongoing services, it is important to choose a supplier that provides value-added services. Case Study #3 describes the benefits of such a relationship.

Case Study: Datawatch Corporation and Vested Development Inc.

BACKGROUND SITUATION:

Datawatch is a leading global provider of enterprise reporting solutions, data transformation tools and support center software that help organizations increase productivity, reduce costs and gain competitive advantage. Its flagship product, Monarch, is a mining application that lets users filter and sort data in legacy reports for business intelligence purposes. Datawatch then wanted to build Monarch ES to store reports for analysis and filtering with the Monarch engine. Linda Lammi, vice president of Development and Technical Services at Datawatch, explains why this led to outsourcing. “Customization of the Monarch engine had been done by an OEM. Because someone else had developed the code, we did not have the rights to that source code. We were only entitled to use their enhancements and were not in a position where we could drive the development ourselves.”

Vested Development (VDI), a software development firm in Russia, was selected because it had experience working on a product with technology similar to the Datawatch project. Lammi says her company also appreciated VDI’s honesty in stating the supplier was not the best choice for designing user interfaces.

OUTSOURCED PROJECT

One-time development of code for new software product.
(September 2000)

CORPORATE CULTURE:

Datawatch had prior experience in offshore outsourcing with development firms in another country and noted a difference between that company and VDI. Lammi explains, “The Russian firm was more apt to voice its opinion. While firms in the other country had a culture of agreeing to do what they were asked, Vested Development stated pros and cons and technical opinions. We want the best product, not just someone to do what we say we want. We like to hear another point of view.”

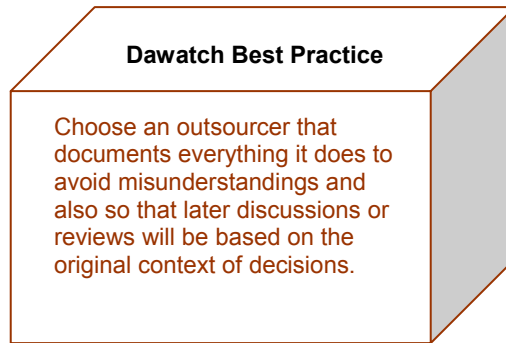
VALUE-ADDED SERVICES:

The Monarch ES coding project had been on the back burner for a while; at the time it was outsourced, Datawatch wanted to revisit some issues related to changing technology. In particular, the company had not made a decision whether to use Com+ or Corba. The Russian firm prepared documentation as to pros and cons of each option.

Twice a representative from the Russian team went onsite in the U.S. at the request of Datawatch, first during the specification stage. The U.S. firm felt it would be more comfortable if a Russian team member were available for face-to-face discussions in ironing out issues. During his month in the U.S., Datawatch found an additional benefit in that answer his questions kept the U.S. team more focused. A second Russian visit occurred when Datawatch was gathering its initial data. The two firms also conducted weekly conference calls.

The most valuable aspect of the relationship, according to Lammi, was VDI’s methodology and practice of documenting everything they did. This enabled:

- ease for someone to support or install it or go further with the code;
- fewer misunderstandings between the parties; and
- Datawatch now can rely on that documentation as the original context for decisions that were made.



Case Study #4

As in any outsourcing transaction, the parties need to ensure adequate knowledge transfer of the process and systems. Where an offshore team is involved, this can be a challenge. But where the offshore team is actually involved in the buyer's core processes, it becomes even more crucial. Case Study #4 explains one company's methodology for knowledge transfer. This case study also highlights the need for flexibility, especially during the transition phase.

Case Study: TIBCO Software Inc. and Aalayance Inc.

BACKGROUND SITUATION:

TIBCO is a software company that develops products for integration of applications and systems on an enterprise-wide basis. Aalayance is a U.S.-based technology company with development centers in India. TIBCO in 1999 sought an outsourcing partner that could do offshore implementations of TIBCO products for its global clients. Growing rapidly, TIBCO needed to develop and implement its products quickly in a fast-moving market. Unable to recruit the right talent pool within the U.S., they considered outsourcers in Ireland and Israel. Costs in Ireland were not as competitive as TIBCO would have liked,

and there were regulatory issues in Israel. And TIBCO was looking for a very specific set of skills.

Jayesh Shah, vice president, Active Portal Engineering and Operations for TIBCO, explains why the Aalayance model was best suited to TIBCO's needs.

“One of the main things that we were looking for was a resource to be an extension of our engineering teams in our core product development. We wanted to take pieces of our core product line and say, ‘You develop this and you support and maintain it.’ So we are actually giving them a chunk of our products. That was kind of important for us because otherwise you have somebody else develop it and then it comes in-house to support it and you don’t have the knowledge base to support it because somebody else developed it.”

**OUTSOURCED
PROCESS**

Offshore
implementation.

CONTRACT

Signed in 1999,
continues until either
party wants to
terminate.

The Aalayance model provides people onsite at TIBCO's location and also provides people onsite at TIBCO's clients' locations. Aalayance acts as a mediary between TIBCO's clients and the development/implementation team in India. Shah says his company has outsourced to other firms in India in the past, and the time zone differences have presented some difficulties for the real-time communication so necessary in a fast-moving environment such as TIBCO's. Aalayance has a couple of people onsite at TIBCO's location, who interface with their offshore team back in India. “When you are doing stuff operationally somewhere that is geographically different,” he explains, “you need to be prepared from a support perspective because now there is a time zone difference. We had times when their people actually worked nights in order to meet our time zone. And we still do that if there is a critical release coming out and we have customer deployment issues. The Aalayance team will either send people out to our customer or be available to talk with the customer on the phone and address issues. They

are willing to adapt to us. They have done a very good job in going to customers on a short notice in critical areas.”

STARTING SLOW:

As with the Duty-Free/Cognizant relationship described in Case Study #2 above, TIBCO believed it was important to start with small projects, learn how things happened while working together, fine-tune the process and then progress to the entire outsourcing services. “We needed to understand how each other works, how our cultures are, and the operating environment and those kinds of things,” Shah explains.

As they progressed, TIBCO also began outsourcing some of its platform engineering work, involving the offshore team in porting on different databases. The team in India also now does maintenance and support for TIBCO’s end-of-life products, which enables TIBCO to free up some of its IT resources to work on innovation and development of new products.

KNOWLEDGE TRANSFER:

Believing the Aalayance team needed exposure to TIBCO’s technology in order to be successful at developing TIBCO’s products and then providing ongoing support and maintenance for TIBCO’s customers, they set up a process for the offshore people to be trained at TIBCO. In some cases, TIBCO’s customer is also involved in taking the training. They learn first-hand, side-by-side with TIBCO’s services people about the kinds of issues that are really encountered in the field. “The kind of software we build and the projects we integrate are complex because we are actually automating a number of processes within a corporation, and every corporation has its own nuances. And when you build the software, we get it 80-90% right. But there will be some 10% tuning, especially in the early going to fit the customer,” says Shah. In addition to Aalayance management and technical people working onsite in the U.S. to learn the TIBCO core product, they sent representatives back to India to impart that knowledge to the offshore team and then to train some trainers there.

TRANSITION AND FLEXIBILITY:

TIBCO's initial plan in the outsourcing arrangement was to get first deliveries out in three months. "We wanted them to do some projects and deliver them very fast," recalls Shah. "But we should have done more homework to make sure the physical connectivity was in place. There was not a good infrastructure in terms of lab and QA facilities in place in Bangalore, and getting a T1 line internationally also takes time. It actually took almost three months just to get all the infrastructure in place." Although the issues were addressed by TIBCO rushing the missing platforms and machines from the U.S. to India, arrangements took time.

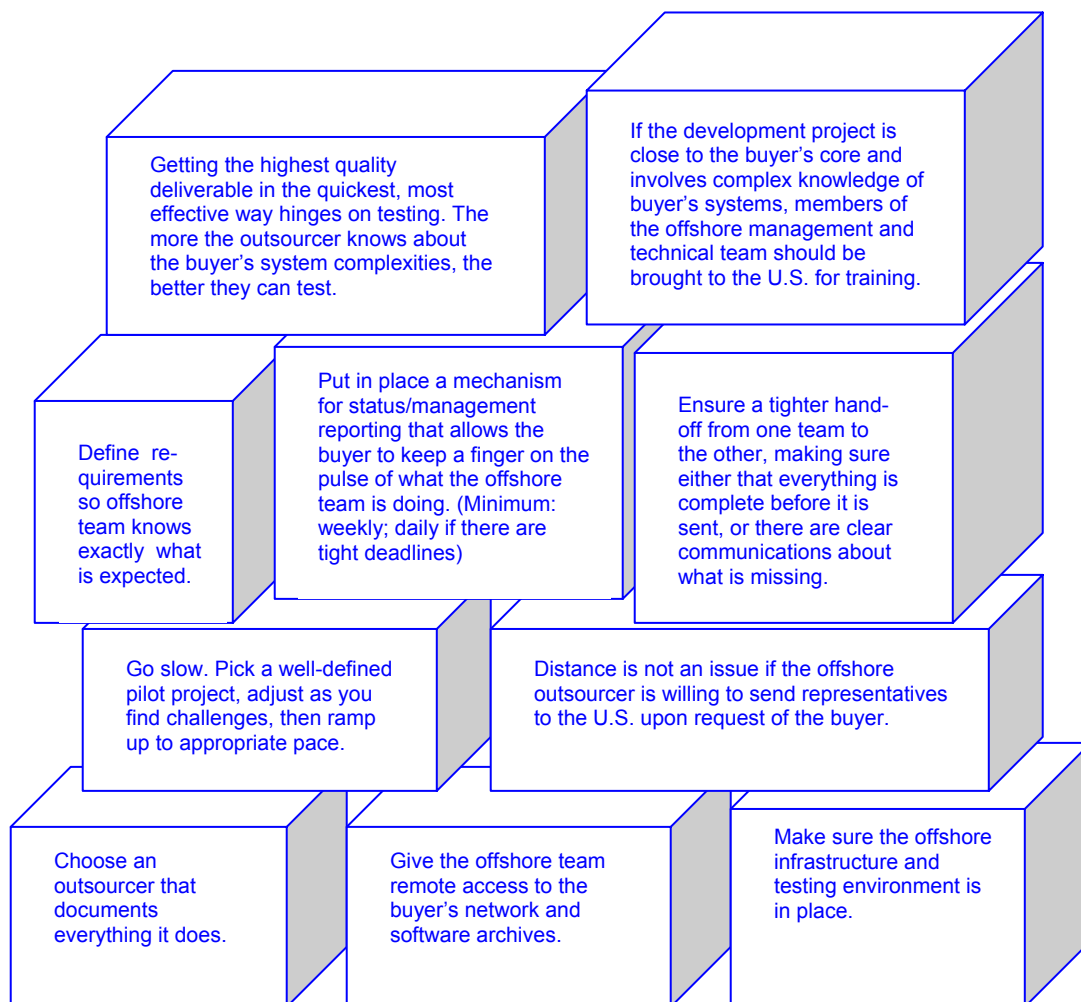
Further complications came from not having the different enterprise systems (such as Siebel or PeopleSoft) in place at Aalayance for testing. In an integration project testing, the customer's systems need to be set up in the testing environment. Some of those systems are legacy, and all need to be installed, configured and operating as they do in the customer environment. In more than one instance, Aalayance people were sent to the U.S. to do the final testing because the necessary system was not yet set up in India. The offshore team proved its flexibility and willingness to work as an extension of the engineering team at TIBCO. In outsourcing, this is vital. As Shah says, "The total success is a team success."



Summary

Because offshore outsourcing arrangements potentially hold both financial and legal risks, it is imperative that a buyer takes every precaution up-front to structure the arrangement so as to eliminate or minimize those risks. By not taking an offhand, incautious approach, buyers can expect to gain great benefits from offshore outsourcing.

Structuring Effective Offshore Outsourcing



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