# There is no IT Outsourcing without a Transition: An Introduction to ITO Transitions

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**Abstract**

Transition management practitioners have suggested that over two thirds of failed outsourcing relationships are due to transition-related challenges (Beulen, Tiwari, & van Heck, 2011). A transition can affect nearly every key aspect of the business.

Within an IT outsourcing (ITO) relationship, transition represents the phase, which starts immediately after contract commencement and finishes with service acceptance. In order to address the challenges of ITO transitions, most ITO providers have now defined transition management as a profession with associated specific methodologies.

The lack of specific literature on this subject, however, has led to many misconceptions, starting with vocabulary, which can sometimes lead to misunderstandings when discussing transition with non-experts.

The goals of this paper are to provide:

- A good understanding of the transition phase in the context of an ITO;
- The specific attributes that make an ITO transition different from many IT projects; and
- The key success factors to focus on successfully achieving an ITO transition implementation.

The information technology outsourcing (ITO) industry has been growing for decades and has become a key approach for many multi-national companies seeking to improve quality, reduce costs, or otherwise transform their businesses. In the context of an ITO contract life cycle, the transition represents a critical and complex phase that starts immediately after contract commencement or effective date. The transition often sets the tone for the outsourcing relationship because it provides the customer with the first operational experience with the new service provider. While transition management practitioners have suggested that over two thirds of failed outsourcing relationships are due to transition-related challenges (Beulen, Tiwari, & van Heck, 2011), research has shown that over two thirds of executives reported problems during a transition (Deloitte Development LLC, 2012).

The lack of specific literature on this subject, however, has led to many misconceptions, including terminology that is being loosely used, which sometimes makes non-expert transition discussions confusing.

For simplicity purposes, this paper assumes a first-generation outsourcing, in which the customer has not moved yet to standardized global processes through an outsourcing provider. Second-generation outsourcings, in which services are moved from one outsourcing provider to the other, would present very similar challenges, but would benefit from a global standardization already in place.

In this paper, we will define the transition phase within the ITO contract life cycle and clarify the key relevant vocabulary. We will then look at what makes an ITO transition different from many IT projects before going through the key success factors.

## THERE IS NO IT OUTSOURCING WITHOUT A TRANSITION

Most outsourcing contracts involve the handover of support functions to a service provider (i.e., the functions that exist to support the core functions of the company). IT is one of the critical support functions required to meet the customer's business objectives.

ITO can be defined as contracting a service provider to take over some or the entire customer IT support functions. The typical length of ITO contracts is 3 to 7 years, with a declining trend.

The goal of this section is to introduce the following points:

- ITO contract customer objectives
- The four phases of an ITO contract
- The definition of an ITO transition

### *ITO Contract Customer Objectives*

When outsourcing IT support functions, most customers focus on achieving three key objectives:

- **Reduce Total Cost of Ownership (TCO):** The customer seeks to benefit from the service providers' volumes and optimized cost structure and delivery model. This TCO reduction also often includes a move to an Operational Expenses model, in which costs are predictable recurring monthly fees — moving away from a Capital Expenses model requiring heavy investments.
- **Improve Quality of Service (QoS):** The customer seeks to benefit from standardization in line with industry best practices and the introduction of new technologies under the umbrella of a focused Service Level Agreement (SLA).
- **Flexible Resourcing:** As a result of an ITO, the customer will typically see a reduction in their IT staffing while gaining access to a pool of expert resources for new projects or innovation.

When these objectives are met, the customer organization can achieve:

- A strong IT operational simplification through a single point of ownership. This new support model reduces the customer vendor management workload and provides predictable recurring costs and flexible access to new technologies and skills.
- Improved IT services with the ability to focus on company core functions. This contributes to providing the customer with a competitive advantage in the marketplace.

Finally, once a company has outsourced its IT support functions, the new service provider becomes an "extension" of the customer organization. This situation requires a high level of trust, because the customer usually keeps the internal responsibility for delivering the services after having outsourced the associated tasks. The customer and the new service provider must build a long-term partnership model in which collaboration will provide further benefits for both parties. This can prove to be challenging when customer and supplier expectations are not properly aligned in the contract.

### *The Four Key Phases of an ITO Contract*

An ITO contract can be seen as a four-phase life cycle (Figure 1):

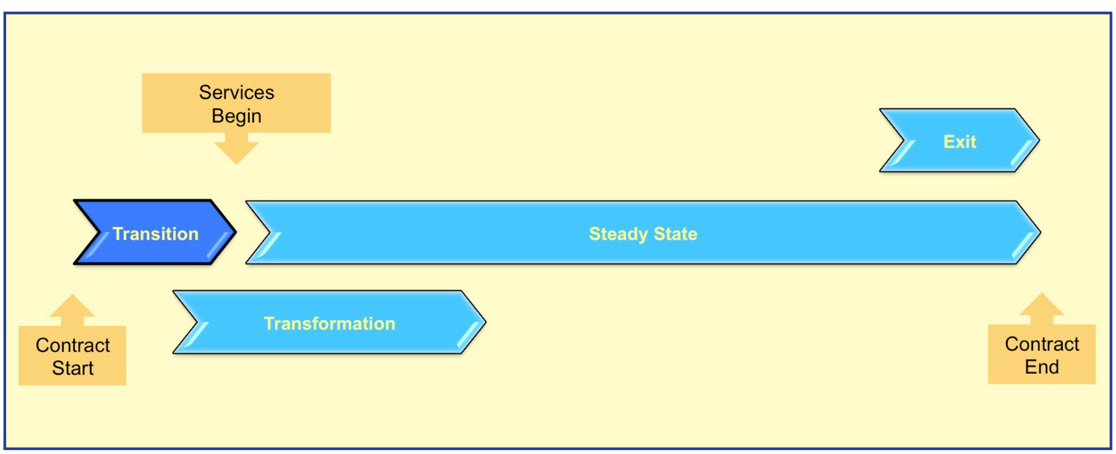


**Figure 1: The four phases of an ITO contract.**

*Transition Phase*

The effective date of an ITO contract triggers the start of the transition phase. During this phase, services are still operated by the customer (or the incumbent service provider[s]), while the new service provider is building the target service model that will host the services to be transitioned. The transition ends when services begin in the new service model to the satisfaction of the customer (transition acceptance).

*Steady State Phase*

The go live of new services defines the start of the steady state phase. The new service provider's focus is to provide high quality services to the customer, in line with the agreed on SLAs. In most ITO contracts, the service provider also commits to working with the customer to introduce new innovation projects that will be defined and implemented during the steady state phase.

*Transformation Phase*

Improvement projects agreed on in the contract are implemented during the steady state phase to further improve quality of service and reduce operating costs (technology upgrades, refresh projects, introduction of new tools). This phase is called transformation, and can sometimes start during transition.

*Exit Phase*

At the end of the contract, if the contract is not renewed, there is an exit phase, which is a separate project in addition to the delivery of the steady state services. This phase, which should be viewed as a "reverse transition," consists of transferring services from the incumbent service provider exiting the contract to the new provider setting up the target service model. The incumbent service provider exit phase is a key dependency of the new service provider transition phase.

**Key Vocabulary**

- **IT outsourcing:** Contracting a service provider to take over some or the entire customer IT functions.
- **Transition:** Transfer of existing IT services to the new service model.
- **Transformation:** Improvement projects aimed at reducing costs and improving services.
- **Steady state:** Services are operational and the focus for the service provider is delivering the services to the agreed on SLAs.
- **Exit:** Hand over of services from incumbent service provider to new service provider in the context of switching suppliers.

### *What is an ITO Transition?*

An ITO transition is the very first phase of the IT outsourcing contract (see Figure 1) and should be approached as a complex, risky, and challenging phase of strategic importance for the success of the outsourcing contract.

The transition consists of transferring the existing services from the customer service model to the new service provider target service model:

- The existing customer service model is called the **Current Mode of Operation (CMO)**
- The service provider target service model is called the **Future Mode of Operation (FMO)** — this is the new way of operating the services.
- An ITO transition is therefore **the transfer of IT services from CMO to FMO**.

An ITO transition is a temporary endeavor (Figure 2):

- Start date: Effective date of the contract
- End date: Service acceptance by the customer.

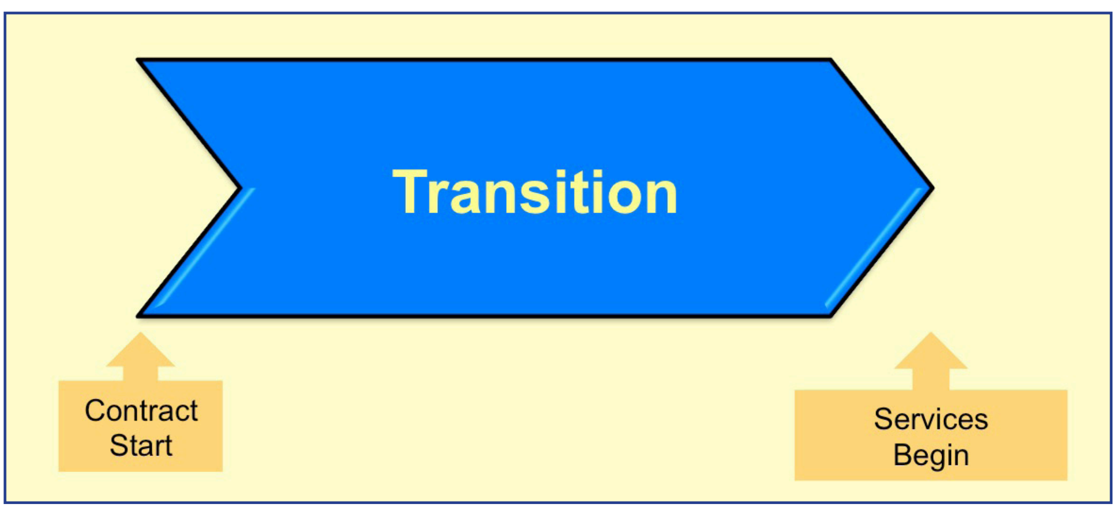


**Figure 2: The transition phase.**

The transition service acceptance is based on a predefined set of agreed on acceptance criteria that define the conditions to be met for closing. It is common to have the customer push for the services to be delivered in the FMO even if the transition is not yet formerly closed. In such a case, the steady state would start with a number of clearly identified issues still to be resolved.

A key challenge of the transition from CMO to FMO is to make sure that operational continuity is maintained, so that transfer of services does not negatively impact the customer business operations.

## WHAT MAKES AN ITO TRANSITION DIFFERENT FROM OTHER IT PROJECTS?

ITO transition manager is now a recognized profession and most service providers specialized in ITO have developed specific ITO transition methodologies. This is due to the fact that ITO transitions have specific characteristics that differentiate them from other IT projects.

An ITO transition has three main characteristics:

- It is a transfer
- It is a program
- It has a hard deadline

### *An ITO Transition is a Transfer*

We have defined an ITO transition as "the transfer of IT services from the CMO to the FMO." In order to achieve this transfer successfully, most activities during transition will be focused on building up the FMO components to deliver the required services and associated service levels. This transfer will bring specific challenges, risks, and dependencies associated with taking over existing services from another party. We will cover these topics when looking at the key success factors later in this paper.

This transfer consists of three main components:

1. **Knowledge Transfer**: The transfer of the CMO information required to successfully set up the FMO (people, processes, and tools).
2. **Staff Transfer**: The transfer of the customer IT staff to the new service provider as part of the FMO.
3. **Asset Transfer**: The transfer of the customer assets to the new service provider.

Although knowledge transfer always applies, the requirement for staff and asset transfers depends on the agreed target service model.

### *An ITO Transition is a Program*

ITO transitions are usually programs: a group of projects with a common business objective. Given its strategic value and complexity, an ITO transition program will typically have high visibility at senior levels in the customer and provider organizations.

Building the FMO requires the implementation of several projects that will compose the building blocks of the broader transition program.

For example, an ITO transition program typically includes the following projects:

- Setting up a project management office (PMO) and governance
- Service towers implementation projects (The more services to transfer, the more projects)
- Knowledge transfer project
- Staff transfer project
- Asset transfer project
- Tools implementation project
- Connectivity project (data, voice, and security)
- Others…

### *An ITO Transition has a Hard Deadline*

Cost overlap during the transition phase will create a hard deadline for the program.

We have already explained that during the ITO transition, the new service provider will work on building the FMO that will form the basis of the target service delivery model. During this period, IT services are still provided by the customer organization.

The result of this situation is a cost overlap that ends only with the completion of the transition when the new service provider takes over the responsibility for delivering the services and the existing CMO service model is terminated.

The cost overlap during transition comes from:

- Legacy service delivery costs and contracts supporting the CMO (recurring operational costs that can only be terminated once the FMO is operational).
- New service provider costs related to the transition

The end date of the transition is usually also impacted by customer constraints, such as legacy contracts termination dates or specific business constraints that impact transition.

While this cost overlap should be factored into the customer budget, the longer the costs will overlap, the further away the new reduced FMO recurring costs. It is therefore likely that transition delays will create financial pressure to the customer, which will in turn increase the pressure on the service provider to meet the agreed transition deadline.

### *ITO Transition Cost Drivers*

There are several cost drivers that can impact the budget requirements for an ITO transition. Each ITO transition will have its specifics based upon the complexity of the requirements, the quality of the existing CMO, and the subsequent efforts required to build the FMO.

As for most projects or programs, the ITO transitions costs are typically more impacted by complexity than sheer volumes.

Here are some examples of cost drivers that may impact the cost of the transition:

- **The maturity of the CMO:** Centralized and standardized services will be easier to transfer to FMO.
- **Quality of CMO knowledge:** The better the CMO documentation, the easier it will be to gather the knowledge.
- **Geographic spread of the CMO:** The larger the geographic spread and the more local ownership (including documentation in different languages), the more complex and costly the knowledge transfer will be.
- **Number of services:** The more services to transfer to FMO, the more complex the program will be.
- **Requested timeline:** The more aggressive the timeline, the higher the risks, and the higher the cost of the organization to monitor and control the program.
- **Clear and flexible contract:** The less ambiguous the contract is and the easier it is to adapt to the likely changes, the faster the implementation can be completed.
- **Customer internal communication and expectation management:** When an organization is aware of the coming changes, the adaptation to these changes will be faster.

## KEY SUCCESS FACTORS

In this section, we will look into the key success factors to ensure transition success.

A study analyzing the influencing factors of sourcing options found that firms that decided to switch providers or to back source typically experienced high service quality and low relationship quality (Whitten & Leidner, 2006). One of the critical objectives for the transition is therefore to set up a trust-based relationship during transition, which can pave the way for a successful long-term outsourcing relationship.

IT outsourcing is a team sport: the closer the customer and supplier teams are, the higher the probability for shared success!

The following key areas of the transition phase will have a strong impact on customer satisfaction and relationship quality:

- Knowledge transfer
- Governance
- Staff transfer
- Transition manager

### *Knowledge Transfer*

The goal of knowledge transfer (KT) is to transfer, absorb, and utilize the information from the CMO in order to build a successful FMO. It should be noted that the "absorb and utilize" portion of this statement is the most difficult to achieve.

Several studies showed that knowledge sharing and transfer are major predictors for outsourcing success and that not only explicit but also tacit knowledge sharing plays an important role in outsourcing success (Lee, 2001).

Poor knowledge transfer may result in disruptions of operations, lowered service levels, and frustrations and dissatisfaction among the client's and the new vendor's employees (Alaranta & Jarvenpaa, 2010).

A successful knowledge transfer must therefore be considered as a key success factor for an ITO transition.

#### *ITO Knowledge Management Life Cycle*

KT is the component of the knowledge management life cycle that is critical to the success of an ITO transition.

The ITO knowledge management life cycle can be divided into three steps:

- **Due Diligence:** This is performed before the contract is signed. The goal of the due diligence step is to answer the question: "What information is needed to deliver the best commercial proposal?" This mostly consists of validation of the assumptions, dependencies, requirements, and risk reviews between the customer and the potential new service provider.
- **Knowledge Transfer:** This is performed during the transition phase. The goal of KT is to answer the question: "What information is needed from the CMO to deliver the agreed on services in the FMO?"

- **Knowledge Improvement:** This is performed during the steady state phase, once the transition is closed. This is a continuous improvement cycle that aims at updating the information and adding new required information to provide the outsourced services.

### *KT Main Challenges*

The KT process should start as early as possible in the transition. A KT plan is developed and typically implemented through face-to-face interviews with subject matter experts (SMEs), workshops including all key stakeholders (customer, new service provider, and incumbent supplier[s] as applicable), handover of documentations, and site visits. The new service provider will integrate the data obtained in their systems and use it to build the FMO. Any knowledge that is not transferred during the KT process most likely will be lost for the project.

During this process, the key challenges are:

- **CMO staff motivation**: The CMO staff perception of losing control may create a risk that knowledge could be lost due to lack of motivation by the staff that holds the information.
- **Suppliers' collaboration and customer engagement**: In all cases, the new service provider has to work with the CMO's incumbent supplier(s) to complete the knowledge transfer. This must be facilitated and controlled by the customer to ensure that incumbent supplier(s) — that are losing the business — collaborate with the new service provider, who could be a direct competitor. The customer must be confident that relevant knowledge has been correctly and completely transferred.
- **Explicit versus Tacit Knowledge**: Knowledge that is to be transferred is of two different natures: explicit or tacit.
  - Explicit knowledge is the easiest to transfer because it is documented (documents or drawings that can be physically handed over).
  - Tacit knowledge is difficult to put into words or just hard to document (skills, intuition, physical experiences, "job secrets," or environmental knowledge concerning the customer environment or technology) and is more challenging to transfer; however, tacit knowledge is required to fully understand explicit knowledge.
  - Effective transfer of tacit knowledge requires personal contact and regular interaction between individuals. This is why it is recommended to have face-to-face interviews and workshops, site visits, and a period during which the CMO experts work jointly with the incoming FMO experts on the actual customer services (often called "shadowing").
  - *"We can know more than we can tell"* (Michael Polanyi, 1966) summarizes the issue of communicating tacit knowledge.

It should be noted that in the context of international engagements, language and cultural issues can add a serious challenge to the KT process.

## ***Governance***

"The main purpose of governance is to specify decision rights, clarify accountabilities, and encourage desirable behaviors" (Kerzner, 2010). The governance framework will define the structure and processes by which decisions are made, through collaboration between the service provider and customer organizations, ensuring that there is clarity between the parties in terms of purpose, responsibility, and direction in order to achieve the customer IT governance objectives.

The priority is to provide all stakeholders working on the account with a clear understanding of the customer's mission. While setting up the program governance, the focus should be on:

- Having a clear understanding of the customer business, and why the services provided are vital to the customer's customers to help the account team to put their work in context.
- Documenting and communicating both 'why' the customer exists and the outcomes they are expecting.

"Research on outsourcing governance has focused on two modes: formal governance based on a legally binding contract, and relational governance based on a psychological contract between the vendor's relationship manager and the client's project manager" (Leimeister, Yetton, Wullenweber, & Krcmar, 2010).

Relational governance is more flexible and encourages efficient collaboration over written contracts for the governance of long-term complex services arrangements, such as outsourcings.

The relational governance will be influenced by:

- **Corporate cultures:** Because the new service provider will become an extension of the customer organization in the transition process, the closer the corporate cultures and way-of-working of the customer and the new service provider organizations, the better the chances of building a sound relationship based on trust.

- **Customer transition maturity:** The probability of a transition's success will increase when the customer already has experience in previously managing transitions. This experience will also contribute to the strength of the relational governance.

In a Deloitte survey, 62% of the organizations surveyed reported that managing outsourcing relationships took more effort than expected (Deloitte Consulting, 2005), which may result in losing contract value. Successful governance set up must therefore be considered as a key success factor for an ITO transition.

Practical means of contributing to effective and efficient governance include:

- "Mirrored organizations" between the customer and the new service provider.
- Steady state program management office (PMO) ramp up during transition

### *Mirrored Organizations*

In order to deliver the transition, the new service provider builds a temporary organization to manage the transition program. The core of this organization typically consists of a program sponsor, a transition manager, project managers for each work stream, and subject matter experts (SMEs) contributing to each project or cross-functional streams as required.

Transition governance will typically benefit from the customer putting in place a "mirror organization" (i.e., replicating the same functions on the customer side of the program so that each function in the service provider transition organization has an equivalent role in the customer transition organization). This will help the service provider transition team to easily identify their counterparts in the client organization. It will also help define the most effective escalation paths between the two organizations and make communication paths more direct. The goal is to set up an efficient working relationship based on interpersonal contact.

The availability, skills, motivation, and influence of the customer staff in the transition organization are likely to have great impacts on the efficiency and agility of the joint delivery teams.

The mirrored organizations formally interact through a set of regular governance meetings. These meetings are typically organized into three categories to provide the right level of information to the right people between organizations:

- Program sponsor meetings (strategic)
- Transition manager meetings (tactical)
- Project-level meetings (operational)

This set of meetings, as well as their recurrence, participants, and agendas should be agreed on and implemented as early as possible after contract start.

The transition governance meetings should involve at least the customer organization, the new supplier, and the incumbent supplier(s) if required. If the customer central organization does not have full power on remote customer entities, it is recommended to also include those in some governance meetings.

Typical governance meeting agendas include:

- Key metrics review
- Status reporting and variance analysis (cost, schedule, scope)
- Escalations resolution
- Key assumptions, risks, and issues review
- Strategic decisions
- Change requests approval

### *Steady State PMO Ramp up during Transition*

As part of the implementation of the transition program, the service provider transition team will include a program management office (PMO), which will provide the transition oversight through key transversal functions (program management, contract management, financials, program reporting, etc.). The transition PMO is primarily focused on the set up of the new operational target model, which also includes a steady state PMO that is fit for purpose.

Involving the account manager and the service delivery manager early through the transition PMO will give them the possibility to set expectations early and identify improvements, which can be included in the account plan or transformation program. Most importantly, this will also help build the steady state customer relationship, while increasing the probability for a smooth hand over from transition to steady state.

The successful set up of the transition PMO and its contribution to the steady state PMO will support the success of the IT outsourcing governance for the long term.

## ***Staff Transfer***

Staff transfer may be requested from the customer and/or required by law in certain jurisdictions. In such cases, the contracting parties may have the following benefits:

- Reduced risks for go live in FMO because CMO key personnel remain on the job. This will increase the chances of achieving operational continuity.
- Reduced KT and training costs because CMO staff is not required to be trained on the customer specifics.

The staff transfer should therefore be considered as a key success factor for an ITO transition in order to ensure the realization of the above benefits on services and costs.

### *Staff Transfer Regulations*

The authorities often regulate staff transfer between companies in the context of an ITO. The goals of such laws are to protect affected employees by ensuring that:

- Employees are not dismissed before or after the transition
- Employees' most important terms and conditions of contracts are not worsened before or after the transition
- Employees are informed and consulted through representatives

In Europe, this regulation is called **Transfers of Undertakings Directive**, but it is commonly referred to as **TUPE** (Transfer of Undertakings, Protection of Employment Regulations, 2006 — UK Law) or **ARD** (Acquired Rights Directive — European Union Law).

Due to the regulatory context and the risks associated with staff transfer, HR and legal specialists must be involved early in this process.

### *Staff Transfer Key Challenges*

Work is an important part of our identity as human beings, and a job transition is a big and very personal event for the employees involved. Studies on the psychological effects of outsourcing show that outsourced employees feel an increased level of anxiety and for some this experience is long-term (Morgan & Simon, 2006).

In most cases, the CMO staff could be demotivated because, as a result of the outsourcing contract, they will either: lose their jobs, change jobs (stay with the customer organization but move from a "doer" position to a "vendor management" position), or transfer to the new service provider. In most cases, the affected employees face increased anxiety due to a reluctance to change, the fear of losing their jobs, a lack of trust in the new service provider organization, or concerns about their new job descriptions and compensation.

Key employees must be retained and motivated (Barthélemy & Adsit, 2003). Motivating them in this context can be challenging. The new service provider must aim at performing a good integration into the new service provider company by making them feel welcome and valued and getting them on board with the new corporate culture as fast as possible.

The job transition impacts productivity, job satisfaction, and customer satisfaction. The actual impact will depend on the quality of the staff transfer management. Research has shown that the reactions of affected employees are 90% about the process and 10% about the actual change itself (Andersen & Ankerstjerne, 2010).

At the end of the day, a successful staff transfer process in which employees' engagement and commitment are renewed can take productivity and job satisfaction to a higher level than before the outsourcing process (Andersen & Ankerstjerne, 2010).

### ***Transition Manager***

The transition manager, as the leader of the transition implementation, also has a strong impact on the success of the transition.

ITO transition management is now considered a profession. One of the reasons for this is because transition management not only requires strong competencies to manage complex programs, but also requires a strong IT service management background.

To build a trust-based relationship and good relational governance, the transition manager should also have good relationship building, communication skills, and stakeholder management skills.

The transition manager should also be involved in the pre-contract phase, specifically on the quantification of the required resources, timelines, approach for the transition, and management of the customer pain points. Not only will this ensure continuity from bid to delivery, by this will also allow for a quicker start of the transition implementation.

Finally, nothing replaces experience, and it is safe to assume that the more transitions you have delivered, the better you will become at it!

## CONCLUSION

We have seen that an ITO transition is a transfer of IT services from the customer service model to the new service provider service model. This is achieved through transferring knowledge (always) as well as staff and assets (if applicable) to the FMO.

We have seen that an ITO transition has the following specifics compared with classic IT projects: it is a transfer, a program, and it typically has a hard deadline.

The key success factors needed to set up a trust-based relationship during transition to pave the way for a high quality outsourcing relationship are:

- **Knowledge transfer,** where the required information for the FMO target model is transferred, absorbed, and utilized by the new service provider;
- **Governance,** where relational governance will be encouraged through mirrored organizations and

involvement of key steady state resources during transition;

- **Staff transfer,** where the focus will be on keeping key employees transferring to FMO motivated; and
- **Transition manager,** where a mix of project and IT service management, along with good relationship-building skills is required.

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