

The Outsourcing Shell Game

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“We’re doomed! It doesn’t matter one bit that we’re lower cost. They’re going to outsource us anyhow.”

“Why do you say that, Harvey?”

“Well, you know the games those vendors play. They promise to do 50% of the work for 80% of the price. And the execs think that’s a 20% cost savings!”

“But that’s comparing apples to oranges. Don’t people understand that the outsourcing proposal only covers a subset of what we do?”

“Debbie, I’ve told them that. But I can’t I prove it. The outsourcing vendor lists in their proposal all the things they’re going to deliver; and to the execs, that looks real good. We can’t match them.”

“Harvey, we can do better than match them. . . . We can beat them!”

“In price, like for like, I’m sure we can. But what I’m saying is, we can’t list all our deliverables and put a cost on each.”

“Why can’t we?”

“It’s sad, but we just don’t know how. We like to talk about all the things we do, but you know how the team struggles to put it in the language of products and services that we deliver.”

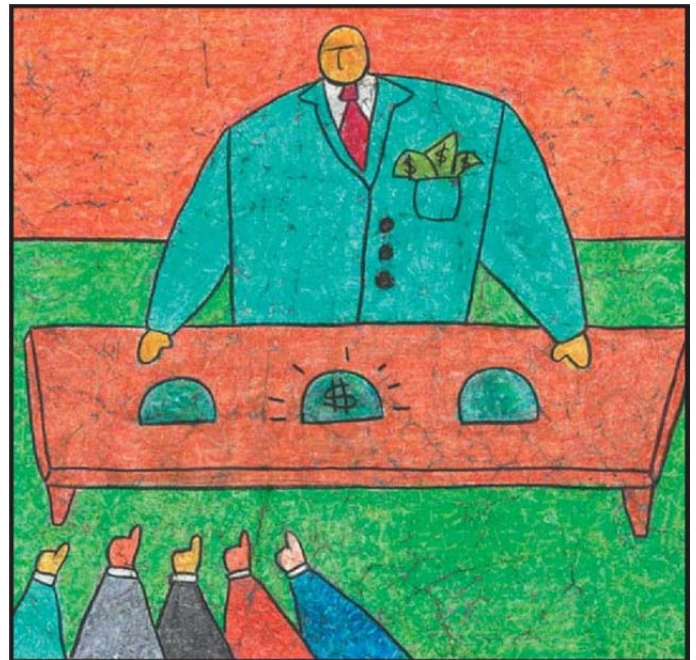
“What about that service catalog that we did a couple years ago?”

“Debbie, let’s be honest. It was a mess. . . a mixture of some products and a bunch of tasks that clients have no interest in buying. Inconsistent levels – some huge bundles and some little nit-picky stuff. Much of it’s language people would never understand. I couldn’t show that to clients.”

“Well, let’s say you and I cleaned it up a bit?”

“We still can’t put costs alongside those deliverables. Sure, we could figure out the direct costs. But so much of our cost structure is fixed. How do we get all those costs spread to the right places? I’m sure we’d put too much here, and not enough there, and all our costs would be out of whack.”

“Okay, then how about we just compare rates – like our cost per developer-hour, or per megabyte of storage?”



“We’ve got problems there, too. The rates we’ve published are for these huge bundles, like ‘desktops.’ We throw in networking, EUC software, email, help desk, the kitchen sink! Then the vendor comes along and promises to put a PC on their desk for \$60. How can we compete with that?”

“Mmm, we’ve got a lot of work to do....”

“And by the way, we’ve got all the same problems with rates that we have with the budget. How do we know where to put all those fixed costs?”

“It would take some thinking....”

“And to top it off, you know all that stuff we do for the ‘corporate good’ like policies, standards, PC vendor evaluations, all those darn committees we all get dragged into. All that gets spread into rates. And that’s stuff the vendor will never get asked to do. We haven’t got a chance of appearing competitive.”

“Yes, we’ve got a LOT of work to do...”

“Debbie, I don’t think we even know where to start.”

The Root of the Problem

Vendors know their product lines, and know their costs. They have methods, tools, and lots of experience costing proposals.

When they’re working for you as an extension to your staff, their clarity on their costs is a good thing. But when they’re selling your boss on replacing you, it’s a powerful competitive advantage on their side.

Unfortunately, it’s tough for internal service providers like IT to match their clarity. Internal staff are used to defending a budget for general ledger accounts like compensation, travel, and training. Most are ill prepared to counter an outsourcing bid with a like-for-like comparison of the true cost of deliverables.

The Way Out

Recognizing the problem, one would think that IT leaders would simply document their products and services, and assign costs to each.

Then, it would be easy to say, “We can beat the outsourcing proposal for this list of deliverables, but that other list we should source. And what about all these other things we’ve been doing for the corporate good? If you want the benefits, here’s the cost. If you want to save money, tell us which you’re willing to forego.”

Casting your budget as the full cost of each project and service to be delivered is called “investment-based budgeting.” It’s the only way to fairly compare internal costs with outsourcing, like for like.

Practicalities

Investment-based budgeting is a powerful exercise, but doing it requires a documented method and principles.

IT leaders have to learn how to document their catalog of products and services at a consistent level. Then, they have to categorize those deliverables to distinguish client services, corporate-good activities, venture capital to develop the IT organization’s capabilities, and internal products like overhead.

Next, they have to come up with a sound method to properly apportion all indirect costs. This would have to recognize what one group does to support another group, as well as organizationwide overhead that supports everybody.

And once they assign the costs of one group to another, and the costs of that other to the one, circularity makes calculating costs challenging.

Then, they have to assemble costs from all the members of each project team to get the total cost of projects and services.

And finally, they learn to massage the data to extract a set of rates that reflect the true cost to shareholders.

If you had to start from scratch, it could take years to develop the methods and tools you need to do this in a believable, consistent, transparent manner.

But the outsourcing vendor's proposal is on the table. Years are not an option.

In practical terms, you have only two choices: You could scramble to put together a one-time analysis. Or you could acquire a tool and method that you can use now to understand your internal costs of services, and year after year to plan your budget, justify your costs, and continually optimize your sourcing strategy. □

For a library of information and case studies on investment-based budgeting, the method, and the tool, go to fullcost.com. And CIOs interested in a private sounding board on their resource-governance processes may enjoy a private consultation with Dean Meyer. Contact NDMA at 203-790-1100, or info@ndma.com.