

Effective Governance on Maintenance Outsourcing

The role of maintenance organizations has changed. Even in the eyes of general management it has grown from a mere cost centre to a value driver. Different trends influence the changing role and demands of the modern asset management and maintenance organization. The changing economic climate requires maintenance organizations to reduce costs or make both costs and resources more agile. Many organizations have acknowledged the opportunities of outsourcing as a way to decrease maintenance costs and increase the flexibility of maintenance and its costs. A significant number of maintenance service providers have also recognized this proposition and have started offering integrated services such as main contracting.

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However, not all outsourcing deals achieve the benefits that were foreseen and desired at the start. What makes some partnerships succeed and others fail? In this article we will focus on the effect of professional commissioning on outsourcing success and stipulate success factors and pitfalls derived from our practice.

Effective Maintenance Outsourcing Is a Joint Responsibility of Client and Supplier

Maintenance organizations increasingly focus on developing their core competences and are improving core maintenance tasks, resulting in a growing number of maintenance

tasks that are carried out by external suppliers. With this trend, the role of the maintenance organization changes from being an internal service provider to a governance organization, that is a client for several external suppliers. Due to this changing role, the maintenance organization has to start focusing on the governance of sourcing relationships instead of the preparation and execution of merely operational maintenance tasks.

Success in outsourcing relationships is a shared responsibility. Just choosing a top of the bill supplier does not naturally lead to satisfying service delivery. The internal governance organization should be adapted to the new situation to effectively govern

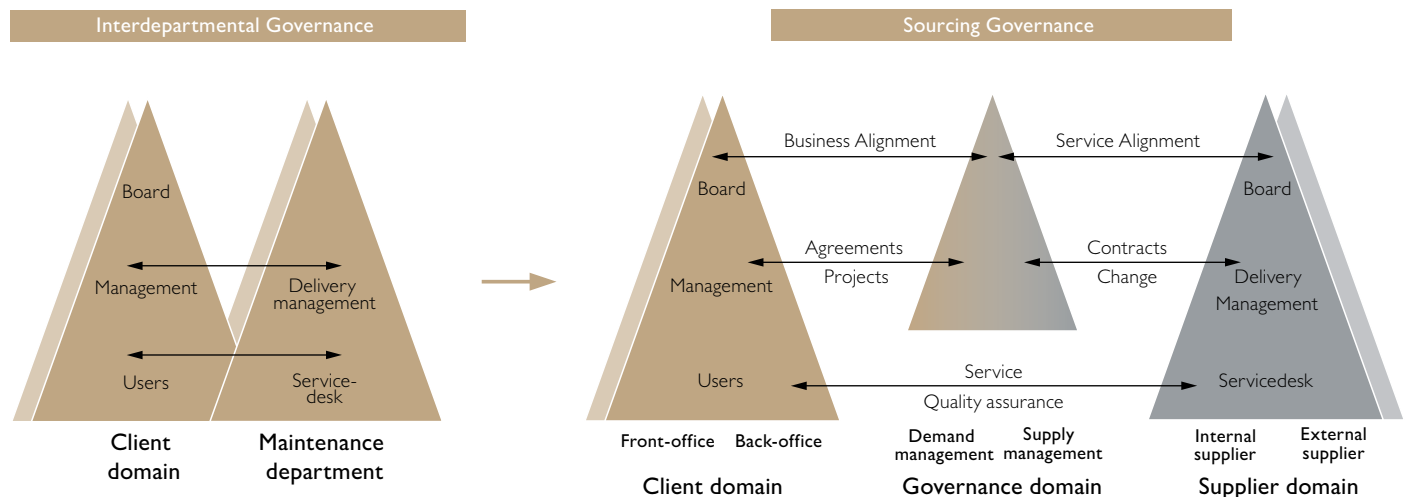


FIGURE 1. The organizational transformation from interdepartmental governance to sourcing governance.

TABLE 1. Key responsibilities within the governance domain.

KEY RESPONSIBILITIES WITHIN THE GOVERNANCE DOMAIN	
Demand management on strategic level <ul style="list-style-type: none"> Developing a strategic vision on sourcing Continuous dialogue with the internal customer about long-term needs 	Supply management on strategic level <ul style="list-style-type: none"> Managing the sourcing strategy Keeping strategic vision on the market
Demand management on tactical level <ul style="list-style-type: none"> Managing the product and service portfolio Managing the SLA's with the client organization Safeguarding customer satisfaction 	Supply management on tactical level <ul style="list-style-type: none"> Selecting and contracting suppliers Managing the contracts and relationships with suppliers Managing the product and service portfolio Evaluating supplier driven innovation
Demand management on operational level <ul style="list-style-type: none"> Managing operational requests from the internal client organization Measuring client satisfaction Reporting services levels to client Registering incidents regarding service delivery 	Supply management on operational level <ul style="list-style-type: none"> Giving orders to suppliers Controlling execution Supervising and delivery monitoring

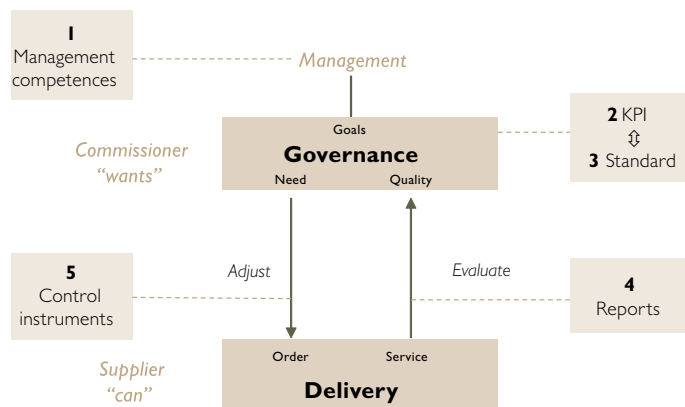


FIGURE 2. Five elements of effective governance.

the maintenance supplier. At the start of the outsourcing relationship a governance organization has to be implemented with clear roles and responsibilities on a strategic, tactical and operational level in order to effectively govern the relation with the supplier and assure the delivery of the desired services.

So what should an effective maintenance organization look like and how do these principles work in the daily operation?

In **FIGURE 1**, the organizational transformation is illustrated. The left side represents the old situation in which maintenance activities are carried out

by the internal maintenance department. In this situation the internal maintenance organization operates as a service provider to operations.

The right side illustrates an example of a governance organization in an outsourcing relationship. In this model, the triangle on the left represents operations, or in other words, the client domain. On the right, the external supplier is drawn. The middle, rather smaller triangle represents the governance domain. This domain symbolizes the modern maintenance organization which now acts as a governance organization be-

tween the internal client and the supplier.

The governance domain consists of two different sides: demand management and supply management. Demand management focuses on the (internal) client and translates maintenance needs into service requirements which are requested from the maintenance supplier. Supply management consists of reliability engineering, contracting required services and monitoring and evaluating the performance of the suppliers and their delivery. The governance function is responsible for both demand management and supply management. A number of key responsibilities within the governance domain on both sides are described in **TABLE 1**.

The responsibilities mentioned in **TABLE 1** provide you with a general high level overview of what activities are performed within the internal governance domain. However, to be able to effectively govern your outsourcing relationship with your maintenance suppliers, instruments to monitor and steer the suppliers have to be put in place.

The next chapter introduces a framework with five basic elements for effective governance which are the keys for successful maintenance outsourcing.

The Five Elements of Effective Governance

To effectively govern your outsourcing relationship it is key that the five elements depicted in the framework, which is build on past research by De Leeuw (1974), are covered within your governance organisation, **FIGURE 2**.

The model represents the interaction between the governance organization (demand) and the supplier (delivery) and the elements that form the preconditions for effective governance

and professional commissioning. We see that Management (1) sets objectives which have to be translated into needs and desired quality. To make sure a client can assess the Quality of the service, key performance indicators (KPI) and standards are set (2&3).

With reports (4), the supplier is able to show what service he has delivered which the client uses to monitor the service. The Need results in an Order. With the control instruments (5) the client can steer towards getting the desired service. How professional commissioning can be realized with the above competencies will be explained in more detail below.

Management Competencies

The element 'management competences' reflects the ability of management to create a thorough vision. This vision can include general questions such as; "Where should the organization be in five years?", "Should I outsource some functions? And what do I want achieve with this decision?"

The decision between different forms of outsourcing is also an example of a management competence. For example, the business strategy of a pharmaceutical organization states that it plans to purely focus on its core competences: making a specific kind of medicine. This implies that maintenance is not a core competence and therefore can be considered to be outsourced.

Management for example decides that output sourcing is the right sourcing strategy so that the organization is no longer responsible for planning and carrying out maintenance tasks. Such a decision will influence the way governance needs to be done. The goals, needs and

quality that are put forward by the governance domain are highly dependable on management's ability to translate the business strategy to an outsourcing strategy.

Key Performance Indicators (KPI's) And Standards

Being a professional governance organization suggests that as a customer you have to develop the skills to translate your demand into clear and unambiguous requests to the supplier. Once the requirements have been determined, an organization needs to think about the level of performance that is required.

This level of performance should contribute to the overall goals of the organization and the specific needs of its users / clients. The required level of performance should be made explicit by making use of Key Performance Indicators (KPI). These KPI's are clear indicators for the performance that is expected from the supplier.

It is essential that the service levels defined for a supplier and the KPI's to measure the performance on the requested service levels match with the level of responsibility that is given to the supplier. This is dependent on your sourcing strategy.

There is a great difference between sourcing the capacity to execute certain maintenance activities and sourcing their output. If you source on capacity it is important to clearly define to the supplier how he should perform the requested activities, on the other hand if you source on output only the end result has to be communicated to the supplier.

Service levels and KPI's should be in line with the sourcing strategy and have to be defined according to exact require-

ments. It is useless to hold a supplier accountable for a 99,8 % availability of an electrical system, if the supplier is requested to perform certain inspections and preventive maintenance activities according to the maintenance plans designed by the client organization.

Many organizations struggle with defining clear KPI's that only measure the performance that the supplier can be held accountable for.

The most important rules for the design of Key Performance Indicators are:

- KPI's should measure what is important to an organization on an operational level. Ultimately, this should contribute to the goals set on tactical and strategic level.
- KPI's should measure the performance of specific activities for which the supplier can be held accountable for.
- KPI's need a clear definition and can not be interpreted in different ways (for example, if the number of disruptions in a system is measured, a clear definition of the term disruption is required).
- KPI's must be measurable. For example, if a KPI states that the supplier has to decrease the NOX-emission by 5 %, then the client organization has to have the means in place to measure this.

Reports

It is the responsibility of a client organization to evaluate the delivery of a supplier. Many organizations procure services from suppliers without being able to evaluate whether the delivery of the supplier meets the original demands and performance agreed in the contract.

TABLE 2. Examples of governance control instruments.

Termination	<ul style="list-style-type: none"> ■ Termination of the contract already before the expiration date ■ The service is sourced to the organization or transferred to another supplier
Replace key players	■ Replacing key players of the Contractor
Penalty	■ Paying less than billed in case of underperformance
Improvement plan	■ In an improvement plan the Contractor clearly states how they will improve performance and when the improvement will be realized
Escalation	■ Putting issues on the agenda of a higher organizational level
Legal notification	■ An official notification that the agreed service level is not met by the Contractor
Replace sub-contractors	■ Replacing subcontractors when unsatisfied with service delivery
Adapting contract	<ul style="list-style-type: none"> ■ Expanding the scope of the contract if supplier performs well ■ Diminish the scope of the contract if supplier performs poorly
Mediation	■ Using an independent third party to mediate between the client organization and the Contractor in order to find a solution
Damage retrieval	■ The retrieval of damage if there is a clear link between underperformance of the supplier and the damage caused to the client organization

Many outsourcing deals do not attain the original goals because the suppliers' delivery and performance cannot be sufficiently evaluated. Our experience is that organizations think about the desired service levels and KPI's when setting up the contract with the supplier, but once delivery starts, they forget to gather sufficient information to evaluate the actual performance of the supplier.

Being a professional client implies that you are able to define the information that is needed to objectively evaluate whether the supplier delivers the performance that you agreed on. This information is presented by the supplier in reports. In these reports the supplier shows the performance of his service on the agreed Key Performance Indicators.

The content of the various reports requested from the supplier at the strategic, tactical, and operational level of the organization and the frequency of reporting should be explicated in the Service Level Agreement (SLA) or other addendum to the contract. For example, if one of the KPI's states that only 1% of the maintenance tasks may ex-

ceed the planning, then the supplier is requested to monthly report the number of maintenance tasks that were planned to be done, and the number that is overdue.

Similarly, on a tactical and strategical level, the client organization has to define the specific information that is requested from the supplier.

Reporting on performance is always linked to the designed KPI's. If there's no information that explains the performance of the supplier on the various KPI's, then it is of no use to define KPI's at all.

Control Instruments

As discussed, evaluation by KPI's and Standards can show whether a supplier does or does not deliver the agreed performance and service level. A professional client has the responsibility and, with the five basic elements, the means to make adjustments in the relationship. It is difficult to directly influence the performance of the supplier.

However, with the right control instruments in place, the relationship with the supplier can be steered which will indirectly result in a positive impact on



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THE GOVERNANCE ORGANIZATION ACTS AS A LINKING PIN BETWEEN DEMAND AND SUPPLY.

performance. Control instruments can adjust the relationship in two ways; they can either reward, or penalize the supplier.

If the delivery meets the agreed service level, thus the reports show that the standards and KPI's are met, there are various ways to reward the supplier. A traditional and commonly used rewarding method is to award a bonus. Besides rewarding the supplier by means of direct financial incentives, you can also reward your supplier by granting other contracts or by adding additional activities to the current contract. Giving permission to use your company as a reference case can also be a valuable way to reward good supplier performance.

If the delivery by the supplier proves to be insufficient or is not in compliance with the agreements in the contract, a professional client has the responsibility to make the necessary adjustments. A variety of instruments can be used to penalize the supplier for underperforming. The goal of using these instruments is to make sure that future service delivery meets the client's requirements.

Since the performance of the supplier is measured by using KPI's, it is strongly recommended to identify for every KPI which instrument is in place in case the supplier fails to meet the agreed performance. **TABLE 2** presents examples of instruments that one of our clients has in place to govern its relation with a main contractor.

Conclusion

Due to an increase in outsourced maintenance activities the role of the traditional maintenance organization has changed from being an internal service provider into a governance organization. The governance organization has the task to translate the business needs into clearly defined service requirements and has to evaluate and accept service delivery. The governance organization acts as a linking pin between demand and supply creating a smooth and well defined process in the outsourcing relationship.

Implementing the five elements for effective governance in your organization and at the same time assigning clear roles and responsibilities within the governance domain, will help you to become a professional commissioner. Working with these principles and embedding them in your organization will significantly contribute to long-term outsourcing success. ■

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12 – 14 October 2010

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