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ORDER-TO-CASH OUTSOURCING

Finance and Accounting BPO Buyers Moving Toward Process-Based OTC Outsourcing

ISG

ISG WHITE PAPER

INTRODUCTION

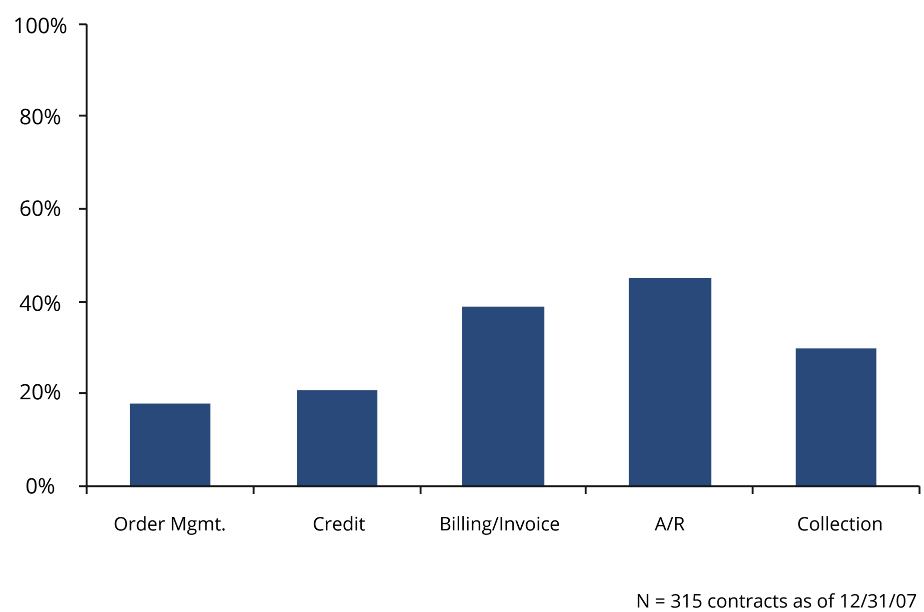
To date, the majority of order-to-cash (OTC) outsourcing has been focused on outsourcing two or three functions, such as invoicing, cash applications, and collections. This has traditionally occurred in the “invoice-to-cash” (ITC) segment (see graphic below that captures OTC functions outsourced among larger companies where the total contract value is more than US $25 million).

Service providers are beginning to see a return on their investment in OTC.

This trend is shifting. In our view, the development of service providers’ capabilities to provide end-to-end OTC outsourcing solutions is the key trend in the OTC arena over the past five years and will likely continue as companies (buyers) are moving toward outsourcing their entire OTC process instead of just outsourcing selected functions. In other words, service providers are beginning to see a return on their investment in OTC.

This paper discusses the reasons for the market’s shift from function-based to process-based (i.e., end-to-end) OTC outsourcing, including observations on other emerging trends affecting OTC solutions.

Order-to-Cash Processes in Outsourcing Contracts

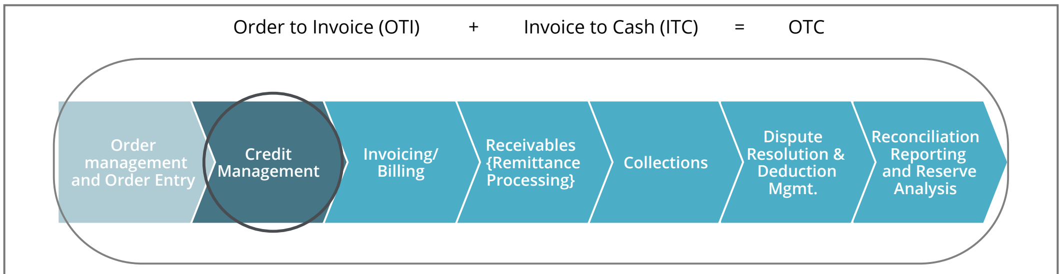


Source: TPI Prevalence Database™

ISG defines "OTC" as the end-to-end cycle starting with order management, credit, invoicing, cash applications, collections and dispute management, and proceeding to reporting and analysis.

OTC OUTSOURCING SHIFT

There are multiple definitions of the OTC process that include all or part of the OTC equation. As illustrated below, ISG defines "OTC" as the end-to-end cycle starting with order management, credit, invoicing, cash applications, collections and dispute management, and proceeding to reporting and analysis. The definition is important because each component or sub-process has varying levels of adoption in the marketplace, and it is helpful in understanding trends that we see evolving in OTC outsourcing.



Credit Management can be part of an OTI scope or part of ITC scope

SHIFT FROM FUNCTION-BASED TO PROCESS-BASED OUTSOURCING

One of the most significant challenges in outsourcing OTC is working cross-functionally with the multiple departments involved with the various OTC functions. This is particularly true when addressing customer order, shipping, billing, collection, and dispute-resolution problems that occur across the OTC process. Traditionally, order management resides in the sales organization, with billing, receivables, and collections in the accounting group and operations in the supply chain organization. Depending on the company, credit management may be part of the sales or the accounting organizations, and in some cases, may actually be split between these two groups. Not surprisingly, undefined boundaries can cause process disconnects, errors, and friction within a company along with a lack of transparency in problem solving. Consequently, once a problem is known, it cannot be solved in a vacuum and thus takes the teamwork of various organizations to piece together the solution.

The more integrated the OTC process, the more efficient the solution.

From an outsourcing perspective, the more integrated the OTC process, the more efficient the solution. In fact, including "order management" activities in the outsourcing scope — instead of just invoice-to-cash — is an even better solution because both the company outsourcing the processes and the service provider are now tapped into the upstream activities that impact the problems and issues found in the downstream functions like remittance processing and dispute resolution.

To help mitigate these issues in OTC processing, companies must implement visibility into the data and communication process. Readily available quantitative and qualitative information is a requirement for successful processing and issue resolution in OTC. This comes with highly integrated processes that are typically supported with integrated ERP platforms. Today, most companies are in various stages of implementing ERP solutions, and most continue to rely upon internal legacy applications to some extent. Many companies have sought to use overlay tools that give visibility into different data across differing systems. Service providers in the OTC space bring these tools to the table, enabling companies to integrate their OTC functions.

Transformation and the ability for the service provider to bring full process redesign and technology solutions have become key drivers of the OTC process approach.

Automating and tracking the cycle of cash flow from order management through to cash application is becoming increasingly attractive as a transformational opportunity with companies. Transformation and the ability for the service provider to bring full process redesign and technology solutions have become key drivers of the OTC process approach. Functional OTC solutions tend to result in piecemeal and less integrated solutions.

The focus on cash flow coupled with the realization by buyers that OTC outsourcing can provide more than just cost-reduction benefits have also supported the shift to a process-based versus functional approach. Service providers can offer significant value by improving the company's financial position through increased cash and working capital levels, which in turn provide benefits of increased funds for investment and/or decreased debt levels to the company. Decreased receivable DSO ("day's sales outstanding") is best achieved through managing the end-to-end OTC process, where processing errors and snags are minimized.

The turf and politics of "who owns what" is shifting in today's OTC scope discussions as the benefits of end-to-end OTC solutions are creating a climate where the various domain owners, such as finance, sales, and operations, are working together to develop the best solution for the company. And service providers are anxious to deliver these end-to-end solutions to capitalize on their increasing investment in and development of end–to-end OTC tools and processes.

SHIFTING BUYER INTEREST FROM OFFSHORING TO COMPANY TRANSFORMATION

Providing offshore capability has been the price of admission for playing in the large-company business process outsourcing (BPO) segment.

Service provider solutions have traditionally focused on the wholesale "lift and shift" method of migrating existing company processes to offshore centers. Today, however, most of the major service providers have established offshore capabilities with multiple global service centers linked by technology and telecommunications infrastructures that provide low-cost, workload balancing, and disaster recovery/business continuity capacity. In effect, providing offshore capability has been the price of admission for playing in the large-company business process outsourcing (BPO) segment.

OTC transformational solutions have been evolving, and some service providers have taken aggressive steps to quickly build their OTC capabilities, as evidenced by the acquisitions of niche receivable and collection management companies (examples are IBM's purchase of Equitant in 2004 and the Genpact acquisition of Creditek in 2005). Other providers have focused on building their own tools and processes to enhance their OTC abilities. As discussions increasingly center on process transformation, service provider investments in OTC capabilities are likely to speed up as larger players continue to acquire niche players to gain or develop OTC proprietary tools and processes.

As buyers recognize the benefits of OTC process transformation, their finance and accounting (F&A) optimization interest continues to shift from the service providers' offshore capabilities to their transformational capabilities to drive the cost, efficiency, and service quality requirements for the future.

WEIGHING CUSTOMER SERVICE VERSUS THE COST-REDUCTION TRADEOFF

Buyers of OTC services have become much more sensitive to service provider call center capabilities as companies react to increased levels of customer complaints — both internal and external — that come with offshore outsourcing. Customer complaints are most often attributed to language barriers and delays in getting issues resolved, which result in frustrated and dissatisfied customers.

OTC buyers have come to value customer language and time zone compatibility so highly that, in some cases, they are willing to trade off some of the cost-saving benefits from offshore solutions for better service and higher customer satisfaction that comes with onshore or near-shore alternatives. For OTC, where customer satisfaction is critical, we expect to see the interest in onshore and near-shore customer call centers increase. This includes solutions designed with separate, but highly integrated front-office (same or near-shore) and back-office (offshore) arrangements that provide seamless communication and processing capabilities. We would not be surprised to see a reversal of some existing contracts whereby current offshore activities switch to onshore and near-shore solutions.

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ANALYZING WHERE STANDARDIZED IS BETTER THAN CUSTOMIZED

As discussed, service provider investment in end-to-end OTC solutions will continue. On top of the many other benefits of this trend, the push for less labor-intensive solutions will drive investments toward integrated technology and processes. Functions will be redesigned to minimize processing activities, such as reducing reconciliations, and eliminate the errors and disconnects that result in time-consuming investigation and correction processing.

The push for less labor-intensive solutions will drive investments towards integrated technology and processes.

As part of the technology push, ERP platforms will be implemented with less emphasis on customized applications. The benefits of standard ERP solutions with lower cost, less maintenance, and less complexity will outweigh the benefits of customized applications especially in transaction-based functions that add little value.

Most ERP standardization will likely occur in the ITC segment as many companies continue to demand custom processes in upstream order-management and order-processing functions to meet their customer-specific requirements as well as their own complex product/service/term requirements.

F&A "CORE" BECOMING "NON-CORE"— IMPACT ON OTC

BPO F&A outsourcing (FAO) is moving up the F&A process curve as increased service provider capabilities in analytics and decision support are creating the market for higher-end functions. This is consistent with the push by some of the larger multifunction service providers and India-based service providers to expand their resources in business performance analysis, forecasting, and analytics.

This capability is particularly important in OTC because it enables service providers to move beyond just invoicing and collections into bundled processes that span company divisions to provide dispute resolution, analytics, and report capabilities. It is also consistent with providing full OTC process services.

OTC MARKETPLACE ACTIVITY

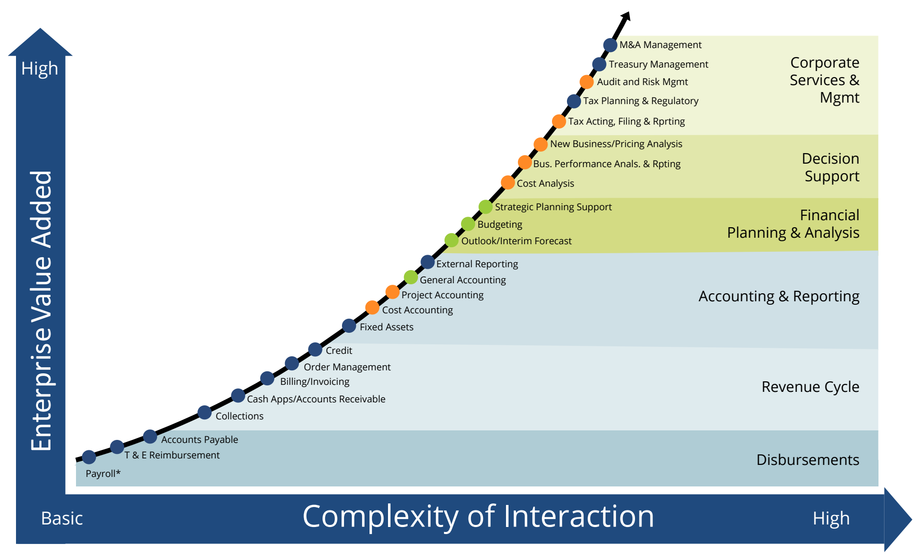
In the past 12 months, our observations of F&A activities within BPO indicate a marked increase in the level of interest and activity occuring in the OTC segment.

In the past 12 months, our observations of F&A activities within BPO indicate a marked increase in the level of interest and activity occurring in the OTC segment. We believe this upswing is based on a convergence of interest in OTC activities by these BPO F&A stakeholder groups:

1. **Buyers:** Increased interest in exploring service provider OTC capabilities through the RFP and proposal process together with an increase in contracting for OTC services.

FAO SERVICES

Transactional and general accounting activities continue to be the core base of F&A contracts. However, FP&A and decision support services are emerging.



*Payroll may report to CFO or HR

2. **Service providers:** Increased investments in OTC capabilities and solutions, including strategic acquisitions of niche receivable management/collection companies in order to expand end-to-end OTC service capabilities.
3. **Outsourcing research and journal organizations:** Increased amount of articles surveying, analyzing, and discussing the OTC segment.

The increase in OTC activity is certainly not unanticipated, as it reflects the evolution and expansion of services occurring in F&A outsourcing. The difference is that OTC seems to be taking the spotlight, especially as buyers seek the benefits of end-to-end process solutions. It's the direction the activity is moving that is changing — and full-process OTC outsourcing is where buyers and sellers are headed.

CONCLUSION

With businesses more cognizant than ever about the bottom line and customer satisfaction, F&A BPO users want exactly what the acronym implies — business process optimization. To meet their objective and please their shareholders, buyers are moving away from outsourcing parts of a function to obtain modest savings or process improvements. Instead, they are taking a more holistic approach by looking at the entirety of their F&A processes to gain larger savings and process improvement opportunities.

Service providers recognize the opportunities and are no longer simply “lifting and shifting” a client’s operations. They are building their OTC capabilities in order to provide complete OTC solutions that will continue to be demanded of them.

ABOUT ISG

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