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IT Outsourcing: 9 Signs It's Time to Fire Your Vendor

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Breaking up is hard to do. And when it comes to IT outsourcing, it can be expensive and risky, too. But issues with an outsourcer—such as deteriorating service levels, lack of investment, excessive turnover, or even fraud—are potentially even more costly than the actual break-up.

Outsourcing relationships don't go south overnight. Customers are more likely to experience a series of subtle changes over time. And sometimes, the partnership itself may be relatively healthy but other changes—a merger or acquisition, for example—may make outsourcing less attractive than it once was. Here are nine signs it might be time to call it quits with your IT service provider—or at least get some counseling.

1. Supersized Growth

In the business world, growth is good. But when it comes to outsourcing, it's more complicated. Most IT outsourcing deals are optimized around the original scope of the deal plus or minus 50 percent, says Adam Strichman of Mechanicsville, Va.-based outsourcing advisory Sanda Partners. You sign a contract to manage 500 servers; when your environment gets to 1000-plus servers it's time to rethink your agreement.

"The deal has lost all its original economies and needs to be totally redone," Strichman says. "When you outgrow your house and need one that is three times bigger, you can't just keep fixing it by nailing a plywood shack to one side and calling it permanent. Totally new architecture and innovation is required."

The same thinking applies if your company grows through a merger or acquisition, and suddenly you're juggling multiple data centers: Your outsourcer will insist that he can take all of it over and lower your costs, says Strichman. But don't buy the pitch.

"Once a client reaches a certain scale, the original value proposition for outsourcing may evaporate," says Strichman. "If the value is gone at this point, you should listen to that little voice that says 'This just doesn't seem to make sense anymore.' That little voice is telling the truth."

2. Turnover of Key Staff

Whether the outsourcer's account managers are leaving voluntarily or the vendor is transferring them to other accounts, when key staff head out the door, "it's time to worry," says Scott Lever, managing consultant with PA Consulting Group. You want your outsourcer's best and brightest, and you want them for as long as possible so knowledge of your environment is not lost.

Lever had one client whose provider kept rotating new people through its account team, leaving the customer's employees spending their time keeping the vendor up to speed, rather than doing their own jobs. "It turned out that the account staff had a significant proportion of their compensation based on new revenue generated and there weren't many new opportunities [at this customer]," says Lever. "Staff turnover is another signal that the service provider is not giving priority to your account or giving people incentive to stay. They're looking to greener pastures." So should you.

Look out for staff migration at lower levels, too. If project work, which you pay extra for, is being staffed with operational employees originally intended to do system maintenance or skilled staff are being replaced with less experienced employees, the relationship is headed in the wrong direction, says Scott Feuless, a principal consultant with Compass Management Consulting.

"If your outsourcer feels that meeting their transformational guarantees can be accomplished by replacing their showcase staff with 'B' or 'C' players, they're clearly gold diggers," says Michael Engel, managing partner of outsourcing consultancy Sylvan VI. "Send them packing."

3. SLAs are Green, but You Feel Red

Solid service level agreements are the cornerstone of a successful IT outsourcing arrangement. But SLAs don't measure everything. "When your service provider is meeting all of the contractually obligated SLAs, but the services don't come close to meeting your expectations, you've likely gotten married to the wrong partner," says Engel.

Similarly, you'll want to check into your termination rights if you find your vendor hiding behind SLAs that are based on average performance across your entire deal when service quality within specific business units is suffering, says Compass's Feuless.

On the flip side, if your outsourcer repeatedly misses service levels and opts to pay the penalties rather than fix the underlying problems, "you're probably already divorced and you just don't know it," says Engel.

4. The HP-EDS, Dell-Perot (DELL) Factor

The last year has seen some interesting mergers between IT hardware makers and IT service providers. "If your service provider was acquired by a large hardware company that isn't your corporate standard," says Sylvan VI's Engel, "you may be in for a rocky relationship."

5. Extreme Profiteering

If your vendor rep is parking his Ferrari next to your Kia, jokes Randy Wiele, managing director of EquaTerra's IT practice, something is rotten in the state of IT services. "Outsourcing pricing is very dynamic and has a steep downward curve for some functions," Wiele says. "A dated contract can provide a very lucrative profit margin for the outsourcer."

If your prices are more than 20 percent the market rate, head back to the negotiating table or walk out the door.

6. The Transformation That Never Comes

For many outsourcing customers, "your mess for less" is not enough of a selling point; their outsourcing deals were predicated on some kind of transformation of the IT environment—whether that be server consolidation, the move to a virtual environment, or the retirement of legacy platforms or systems.

"I have seen deals that by year three still only have 25 percent of the transformation done, even though it was supposed to be complete," says Strichman. In such situations, parties tend to point fingers at each other, and "they are usually both correct to some extent," Strichman says. Unforeseen investments necessary for the transformation crop up, grinding change to a halt.

"By year three, if the transformation is 50 percent or more behind schedule, termination is a real option," says Strichman. But, he adds, such moves can get nasty.

7. Everything Costs Extra

If every time you ask for something, the vendor refers you to the letter of the agreement and says anything else will cost more, it's a bad sign, says Feuless. Chances are the provider is not getting the profit margin it needs on your deal, and you can expect to pay one way or another.

"If your outsourcing relationship was forged at a country club between two executives and the delivery team utters any of the following phrases: 'We are not making any profit on this deal,' 'This deal is a loss leader,' 'The executives underbid this deal,' or 'We bought this business,'" says Engel, "it's time to find a good divorce attorney."

Some other signs to watch for: the service provider drops regularly supporting activities such as disaster recovery testing, cuts back on training and development for staff on your account, delays upgrades to equipment and software, or stops regularly documenting and updating processes.

"These are signals that the service provider is trying to squeeze profitability and that they are taking a short term perspective," says PA Consulting's Lever. "Chances are that if they are changing the things you can see, they are certainly cutting the things you can't see."

8. The Project-Hours Fight (Again)

Every outsourcing customer and provider argues back and forth about project hours every month—what can be billed as extra and what's included in the contract, says Strichman. "It's a healthy check and balance for every relationship."

However, when these monthly discussions become heated fights that paralyze the deal, or the project hours being charged create significant budget or ROI problems on either side, "it's the best indicator, in my book, that expectations are clearly out of alignment and have been so for quite some time," says Strichman.

It's like a couple arguing about the toilet seat. Plenty of partners go back and forth on the issue repeatedly, but when the weekly fight leads to tears, name-calling and insults to the in-laws, it's not just about the up or down position anymore. Something more fundamental is wrong with the relationship.

9. The Satyam Scenario

If you discover your vendor doing anything shady that violates your contract, like altering metrics reports, it's time to call it quits. "They are not in it for the relationship," says Engel. "They are in it to survive."

And, adds Engel, if you just happen to have "tens of millions of dollars in business with a provider accused of systematically falsifying financial records and the outsourcer's CEO responds by saying, 'I am now prepared to subject myself to the laws of the land and face consequences thereof,' it's probably time to consider finding a new partner."