



Warranty Processes: Strategic Gain through Global Sourcing

Executive Summary

Historically, there was a feeling that critical business systems could not be moved out of the corporate data center. However, the truth is that there are many business-critical functions that have very successfully been entrusted to global services providers, including financial applications, HR, ERP and functions within warranty service. As global sourcing has gained more traction and generated more success stories, this historical thinking has changed. In fact, in their book *Multi-sourcing*,¹ Linda Cohen and Allie Young write:

"Outsourcing worked. Using external service providers to cut costs and improve performance has become truly commonplace. As much as the popular press has focused on the debate over the benefits of outsourcing, no executive leader team, board of directors or government agency of any size would deny that outsourcing is a vital, even integral, part of successful operations today."

Done right, transformational managed business services can enable operational improvements that advance business objectives and drive competitive differentiation, while delivering a superior experience for a client's end users.

In this paper, we will investigate two related items relative to the warranty business and global sourcing. First, we will investigate best practices in global sourcing, what it takes to manage a complex global service provider relation-

ship, how these apply to the warranty business and where these practices are working well in the warranty arena. Second, through a representative study, we will see how combining these practices can result in substantial savings.

In business process outsourcing (BPO), the era of simple solutions is over. Indeed, the market's evolution calls for service providers to do much more than trim a client's operating costs. In fact, Young and Cohen go on to write:

"... And, of course, outsourcing to cut costs no longer provides significant competitive advantage – all your competitors are using outsourcing as well and reaping the same cost advantages."

The focus of BPO, "also called managed business services," has traditionally been on cost savings and other tactical objectives. However, this emphasis is giving way to a more strategic and customized approach that goes beyond merely replicating inefficient business processes at lower price points. Done right, transformational managed business services can enable operational improvements that advance business objectives and drive competitive differentiation, while delivering a superior experience for a client's end users. Young and Cohen write:

"But precisely due to this success, new challenges are emerging. The high expectations associated with outsourcing are increasing."



Companies spend vast sums on warranty and after-market service, estimated at nearly \$30 billion in the U.S. alone, according to estimates by *Warranty Week*. On top of that, these are large and complex processes. However, in these continued times of economic uncertainty, there is relentless pressure on organizations to reduce costs while also improving customer service.

Consequently, our first question is whether companies should consider managed services for some or all of their warranty operations. Given that warranty administration is rarely a core function in the business, the answer is clearly yes, as long as the company can find a partner that can reduce its costs, meet its goals and improve service to its customers. Finding the right partner is a significant challenge, but when achieved, it can provide fantastic results.

Figure 1 lists five best practices relative to warranty global sourcing. In this section, we will review each of these practices and discuss specifically how they apply in a warranty and after-market sales environment.

Five Best Practices in Warranty Global Sourcing

- 1. Customized Solutions:** Ensure you have a dedicated solution from a company you can trust.
- 2. Clear SLAs and Metrics:** Strive for clarity in writing SLAs and metrics.
- 3. Aligned Economic Incentives:** Business incentives need to be based upon a shared set of risk/reward controls.
- 4. Cross-Industry Best Practices:** Make full use of all the global services provider's expertise and resources.
- 5. Looking Beyond Tactical Benefits:** Use the global services provider strategically.

1. Customized Solution

Conventional cookie-cutter managed business services and global sourcing may help improve the bottom line, but it often fails to add the value of newer, more strategic approaches. To get there, work with a global services provider that has a dedicated but customizable solution for the problems you are trying to solve and can tightly align with your strategic business objectives. In this still-emerging market, companies must seek out a partner that can serve as a trusted advisor. Capabilities can be replicated from one managed business services provider to another, but in a services-based business, relationships are of the utmost importance.

Corporate cultures are important, and over the years, companies build up processes and procedures that help define the brand. Because it is important to preserve many of these, it is essential to select a global services partner capable of customizing its solution to include these processes and procedures. On the other hand, companies need to select a partner that can also provide consulting and re-engineering support, where appropriate, so you can enjoy continuous improvements in both customer service and cost. The ideal global services partner will have the depth to allow you to compare your processes with others both inside and outside of your industry so that best-in-class warranty service can be ensured.

Specifically for warranty global sourcing, ensure that you have a managed business services partner that specializes in warranty- and after-market-related services. Areas in warranty and after-market services that lend themselves to global sourcing include:

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Warranty Outsourcing for Strategic Gain



Figure 1

- Customer Interaction and Support
- Extended Warranty
- Field Service Support
- Service Parts Optimization
- Warranty Claims Management
- Financial Management

We've seen this practice successfully used by a number of organizations. One large consumer electronics manufacturer, for instance, uses a global services provider for all of its call center operations. The company has nearly 200 associates who are actually employees of its global services partner. This provides the company with complete flexibility in adding and subtracting people and allows it to concentrate on warranty service and not on HR and hiring. This has led to a successful long-term relationship, with benefits for both organizations.

2. Clear SLAs and Metrics

Service level agreements, or SLAs, serve as the basis of global sourcing and other vendor/client relationships. Particularly for a major engagement, companies should use the SLA writing process as a means to establish what they expect from the services provider and vice versa. Use simple, relevant terms and performance-based language, and make the performance parameters as specific as possible. Identify milestones to be achieved along the way, as well as timelines for achieving those milestones. Determine – and put in writing – not just what will be accomplished but who will do the work. And if issues do arise, as they inevitably will, spell out exactly how the global services partner is organized to deal with, and resolve, those issues.

The old adage, “You can’t measure what you don’t manage” is particularly true when it comes to global sourcing engagements. Both the warranty administrator and the global services partner need to agree on – and again, put in writing – what measures they will use to gauge the progress and success of the project they are embarking on. Wherever possible, attach specific numbers to such metrics, e.g., “Improve external query response time by 10%,” “Bring new claims processing platform live by June 15, 2011,” “Decrease parts out-of-stocks by two percentage points nationwide,” etc.

It is important that SLAs are linked to the business metrics and provide controls not only

on specific items but also on end-to-end controls across the entire warranty spectrum. These items need to reflect the impact on the entire business. For example, an end-to-end control could be a measurement of the effectiveness on warranty reserve for changes imposed by the global sourcing process.

Even when performance metrics have been agreed upon and put into writing in SLAs, that doesn't mean they will necessarily be achieved. Strong SLAs need to build in penalties if tasks are not accomplished on time or are performed inadequately. If the global services provider understands that there is a real price to be paid for failure to live up to the SLA, its management will be motivated to keep a sharp eye on the project's progress and will devote the necessary resources to meet the stated goals.

Companies will want to use a carrot as well as a stick to motivate the global services partner, its management and its employees. If the services provider exceeds the expectations spelled out in the SLA that lead to measurable improvements in performance for the retailer – for example, achieving a faster-than-expected ROI or a larger customer satisfaction increase than had been projected – then both parties should build in mechanisms for sharing the benefits.

For warranty global sourcing, these mechanisms would specifically be tied to the services being globally sourced. For example, a typical global sourcing engagement might include SLAs and metrics for claims processing time, net promoter score, parts availability and warranty processing costs. In each case, detailed goals should be established and associated metrics tracked.

A good example of where this is done today is the service agreements between many manufacturers, especially those in the computer industry and their network of service providers. Using a network of independent service providers is a type of global sourcing that has the added complication of being performed by hundreds or thousands of different organizations. A key element of this program is the pay-for-performance model. These SLAs and metrics allow the manufacturer to reward organizations that provide good or even outstanding performance and penalize those that do not. In well-run programs, the metrics are clearly defined

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and well-known by both organizations. In addition, they help to align efforts between the two organizations, the importance of which we will see in the next section. Well-structured metrics are geared toward measuring the results more than the methods.

3. Aligned Economic Incentives

Warranty managed services arrangements will work best, especially over the long run, when the economic incentives of both organizations are aligned. Business incentives need to be based upon a shared set of risk/reward controls, with the organization that controls the feature responsible for a larger part of the impact, should that control not perform to the plan. A partnership based upon the precept of “your pain is my gain” rarely works for long. In service arrangements, this means trying to avoid direct fee-for-service relationships unless both partners have a financial incentive to reduce the number of service events.

In well-run programs, the metrics are clearly defined and well-known by both organizations.

It is also important to align economic incentives with the appropriate party that can best control the cost. For example, a provider of managed business services that has been contracted for customer interaction and support should not be held accountable for an increase in calls due to manufacturing defects. However, contracts should be structured so that in areas where the provider can make a difference, there is financial incentive to do so. Again, in the global sourcing of customer interaction and support, if the provider is also supplying technology, its contract should be structured so that it benefits if it reduces calls by providing more self-service options or through programs that reduce the number of actual service events.

In the global sourcing of warranty services, this can be especially important, as there tends to be cost requirements from a number of areas. For example, we have seen instances in which the service group of a large retailer worked with one of its existing global services partners to develop new processes and technology for the management and submission of warranty claims. The companies worked together to ensure success of the program would benefit both organizations. The resulting changes reduced the submission time for claims from over a week to just over a day and allowed the retailer to gather millions of dollars in additional claims that it previously was not able to submit.

4. Cross-Industry Best Practices

By deconstructing and documenting key business activities and working closely with clients to ensure effective knowledge transfer, managed business services can deliver quality improvement and accelerated time to value. The ultimate goal is to identify and deploy business process improvements that can fit an individual client's business requirements and, when possible, boost the performance of associated IT systems, as well.

A service provider must offer more than labor arbitrage and cookie-cutter solutions to help clients reap the strategic benefits of managed business services. What is required is a highly tailored set of solutions necessary to support the client's unique business requirements.

To accomplish this, the global services partner must be willing to invest in a dedicated solution design and transition team for every engagement. The team's role is to obtain a detailed understanding of a client's process. This heightened level of process understanding increases the client's comfort level with managed business services. As such, the provider is seen not only as a business partner but as a true extension of the customer's organization. For example, for global sourcing of warranty services, call center agents must come across as knowledgeable and as plugged in as the company's own employees. They must have an appropriate understanding of products, warranty periods and service options. The successful managed business services provider will interact with customers and business partners as if it were “one of them.”

Another key way to help customers feel more at ease with managed business services is to utilize some of the client's key resources as part of the on-site team. Many companies view global sourcing simply as a means to cut costs or achieve goals without adding to their in-house staff. While these are both valid reasons, many global services partners offer value-adds and higher-level services that companies can take advantage of.

For example, some providers have developed considerable expertise in the warranty business, through their own research and their experience with providing global sourcing services for a number of different companies. These global services providers can help companies benchmark their own warranty operations against those of others in the industry, and they can teach clients best practices

they may not be aware of. Global services providers can also be an objective source of information and judgment, both about a company's own IT systems, as well as those of competitors or companies being considered for acquisition.

Many global services partners have developed not just IT, domain and industry expertise but also other functionalities and expertise from other industries. Leading providers that prize innovation, for example, have developed in-house tools that encourage innovative thinking among their own employees and manage the processes by which these ideas are turned into practical, tangible business benefits. Global services providers that are willing to share these types of solutions can help companies address a wider range of business challenges. The best possible solutions will often incorporate expertise from other industries and engagements to apply best practices. This broad focus generally results in the best possible solutions.

When companies have a recall, this can put a huge strain on the organization. All of the day-to-day operations have to continue, but there are now huge additional requirements imposed by the government that must be met in very short order. When a large appliance manufacturer went through two million unit recalls in less than six months, it was able to successfully pull both off by working with its global services partners. One partner helped with additional call volume, as well as supported additional in-home service calls. Another partner helped with managing the list of consumers and tracking when the repairs were complete. By successfully leveraging its partners' experience, the company was able to successfully navigate this potentially disastrous time and close out the recalls in considerably shorter time than originally estimated.

5. Looking Beyond Tactical Benefits

Warranty is a fast-changing, rapidly globalizing industry. While many companies moved into survival mode during the economic slowdown, the industry's leaders are now looking at new ways to achieve their business goals. In the warranty space, this generally involves trying to improve customer satisfaction scores while also trying to lower costs. The ability to achieve both is a crucial element of the business.

Some companies will choose to use global services providers simply to maintain their current systems

while they focus on new opportunities. But it's also possible to use the global services provider as a "lab partner," experimenting with new functionalities in ways that leverage both the company's and the provider's expertise while minimizing the risks for both parties.

Tactical changes are generally measured and monitored through core metrics and SLAs. Strategic changes can be measured through industry benchmarks, best-in-class analysis and comparisons with other industries. In addition, introduction of best practices from other disciplines, such as Six Sigma and lean manufacturing, can lead to a shift from just improving efficiencies, to significant improvements in effectiveness, predictability and breakthrough achievements. In the warranty industry, there is a significant opportunity for these game-changing improvements that can be driven by finding the proper partner.

A global appliance manufacturer was looking to connect and provide better service to its customers. The company used a network of independent service providers but wanted to be able to schedule service appointments with its customers on the original call. The manufacturer got together with one of its global services partners, and together they were able to develop a system that provided connectivity to a huge portion of the manufacturer's service network and allowed it to provide this real-time scheduling. Today, this manufacturer schedules over one million warranty calls each year and has significantly improved its customer satisfaction ratings.

In the second half of the paper, we'll look at how a global sourcing engagement might benefit the company that contracts with the global services partner. In fact, we'll see that each of the best practice areas can result in direct savings. In our example, we'll assume a manufacturer with about \$10 billion in annual sales that is spending about \$300 million per year in warranty cost.

1. Customized Solution

The initial savings comes from core benefits from global sourcing. Using lower cost resources provides a direct savings. In addition, the economies of scale from multiple engagements

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Managing Warranty Costs: Dissecting the Costs and Analyzing the Benefit

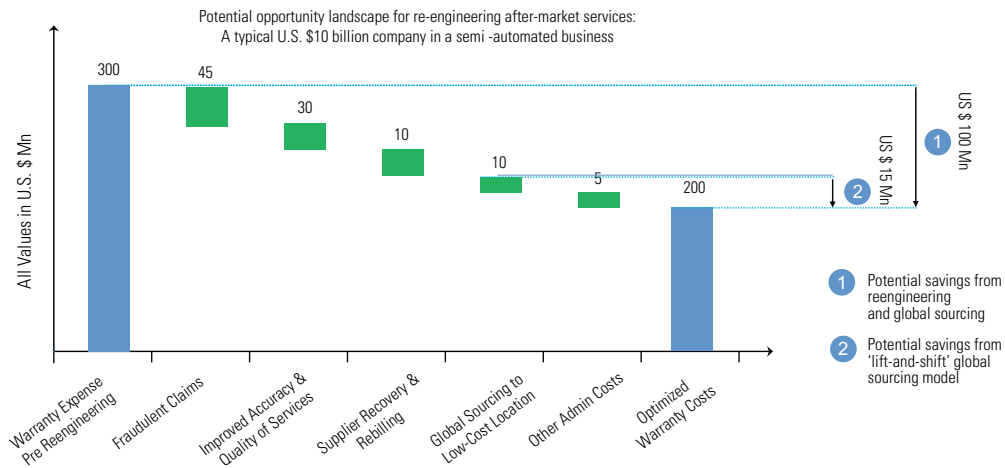


Figure 1

can provide efficiencies across the entire global sourcing solution.

Our estimated cost savings from this one area is \$10 million annually.

2. Clear SLAs and Metrics

Additional savings can come from properly written SLAs and metrics. When well established, these provide incentives to the global services provider to continue to improve processes and lower costs. By properly structuring the relationship, these savings can be enjoyed by both organizations.

Our estimated cost savings from this area is \$5 million annually.

3. Aligned Economic Incentives

Our next area of savings was from improved accuracy and quality of service. Since the economic interests of both parties were effectively aligned, the global services provider had the necessary incentives to invest in a continuous improvement program for a number of its warranty solutions (such as claims processing and financial management). This program allowed the organization to improve accuracy and quality of service. This would include improved parts management systems to ensure that the necessary parts were available when needed without an increase in inventory. This would reduce not only the cost of parts but also the volume of buyouts and returns.

Further system improvements included more stringent automated warranty checks that reduced claim payments for products covered

until alternative warranties were available (such as a workmanship guarantee from the service provider).

Our estimated cost savings from this area is \$10 million annually.

4. Cross-Industry Best Practices

The best global services providers will be able to incorporate expertise from other industries and engagements to allow companies to be able to provide best-in-class warranty service. For example, a global services firm might have experience with other types of claims such as healthcare claims. Expertise developed in this industry through areas of concentration such as fraud reduction can be applied to warranty.

There are many similarities between warranty claims and healthcare claims. Both involve a customer, services provided by a third-party and a finite set of service offerings. By leveraging best practices in the use of analytics for uncovering and detecting fraudulent claims, huge savings can be generated in a warranty claim process.

Our estimated cost savings from this one area is \$45 million annually.

5. Looking Beyond Tactical Benefits

Strategic use of a global services provider can involve the introduction of new processes not

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currently implemented by the company's warranty department. A good example here is supplier recovery. While many organizations in heavy industries employ a supplier recovery process, most manufacturers do not. This is potentially an area with significant short-term savings potential, as well as a way to measure suppliers to improve product reliability in the long term.

Our estimated cost savings from this one area is \$10 million annually.

Conclusion

In our example, the company is able to reduce expenditures on warranty by about one-third and drop an extra \$100 million to the bottom line. Clearly, this combination of global sourcing and reengineering can make a tremendous difference not only to the warranty department but also to the entire organization.

Footnote

¹ Linda Cohen and Allie Young, *Multi-sourcing*, Harvard Business Press (November, 2005).

About the Author

Imran Masood leads the Manufacturing, Logistics and Technology BPO practice at Cognizant, with responsibility for all engagements within North America. Prior to joining Cognizant, Imran worked in the BPO industry in various leadership roles, in Six Sigma, operations and client management, helping Fortune 500 companies in the areas of shared services, offshoring strategy and process innovation, with a special focus on multi-location global environments. Imran is an electrical engineer with a post graduate in Management. He can be reached at Imran.Masood@Cognizant.com.

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