

The Risks of Outsourcing Services at Selected Facility Management Companies in Cape Town

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Abstract: The outsourcing of facility management services has become increasingly competitive and success now depends on companies' ability to assess and manage risks of low employee morale, intellectual property right, legal, increased costs, unrealistic savings projections and reputational damage successfully. This paper examined outsourcing risks at selected facility management companies in Cape Town. Previous study identifies loss of control, cost and life cycle impact and time inefficiency as anecdotal evidence of outsourcing risks. In the facility management sector, the identification and management of risks have begun to shift progressively from external to internal – like resource and capability management and the strengthening of internal control mechanism. This quantitative study utilised self-administered questionnaire to collect data from 142 randomly selected respondents; employees of participating facility management companies in Cape Town. The paper found that top 6 risks ranked from the highest are information security, legal, ethics/compliance, contractual, financial and economic. The higher end of the mean scoring indicates a greater emphasis on controllable (internal) risks, with 4 out of the top 6 ranked items identified within the internal risks category. This research provides insight to understand outsourcing, risks of outsourcing and risk assessment techniques with emphasis on internal risk management. The examination of outsourcing risks enables companies to understand risk assessment, evaluation and mitigation requirements and categorisation for successful management of risks associated with the outsourcing of facility management services.

Keywords: Risk Management; Controllable and Uncontrollable Risk; Strategic Facilities Planning

JEL Classification: M11

1. Introduction

In a competitive real estate market, companies need to assess and manage facilities management related services to ensure that the company operates optimally whilst

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ensuring minimal risk. The outsourcing of services comes with risks, such as reduced employee morale, IP, legal, increased costs, unrealistic savings projections and reputational damage. The examination of identified risks enable a company to manage outsourcing of facility management services. Outsourcing, according to Ikediashi, Ogunla and Boateng (2012) is the “contracting out” of business process to a third party. While most facility management services are outsourced, some remain insourced to maintain organisational cohesion and control (Ikediashi, Ogunla & Boateng, 2014, p. 473). In a similar study, Kavcic (2014, p. 9) states that the decision to outsource is one which could be of long term and strategically important for a company overall cohesion and control. For the facilities management company to be successful, improved organisational cohesion and control should be regarded as essential part of organisational activities and functions.

2. Literature Review

Increasing complexity in the real estate sector along with shifting paradigm progressively from external to internal – enhances resource and management capability (Krumm, 1998, p. 95). This paradigm shift provides impetus for robust acquisitions, mergers and strategic alliances decision to improve organisational resources and capabilities for success and growth. This is done with the objective of risks identification, mitigation and management. In addition to risk mitigation and management, the growth and success of outsourcing would benefit from the application of four principal components; (1) strategic facilities planning, (2) strategic asset management, (3) asset maintenance service and (4) facilities service management.

Strategic facility planning: The formation of strategic facilities planning commences in the boardroom and requires the input and support from major divisions within the company. Whilst strategic facilities planning is a key component in long-term planning of assets, success would depend greatly on the identification, management and mitigation outsourcing risks. In this instance, error in risk identification, mitigation and management could lead to financial loss, reputational damage with consequence of adversarial relationship with third parties. It is imperative that strategic facilities planning is conducted in a manner where it has complete stakeholder buy-in compatible with companies’ objectives.

Strategic asset management: provides the guiding principle for procurement, strategic planning use and disposal of assets (Barton, Jones & Gilbert, 2001, p. 70). Jolicoeur and Barrett (2005, p. 52) indicates the success of strategic asset management is determined by the degree of alignment with other resources to support a company’s strategic direction. Also, the alignment allows a facilities manager the time to contemplate on how best to respond to change in requirements.

As competition increases, strategic asset management becomes an important management principle that should be applied for success, growth and competitiveness (Fraser, 2014).

Asset maintenance service: Although maintenance management models exist, risk management in the context of outsourcing is focused on four dominant models. These models according to Fraser, (2014) are: (a) total productive maintenance (TPM), (b) condition-based maintenance (CBM), (c) reliability centred maintenance (RCM) and (d) condition monitoring (CM). The four maintenance models should be used in conjunction with building provision of basic services for human habitation like, clean water and air, waste removal, optimal humidity and thermal control, privacy, security and acoustic comfort (Osborn & Greeno, 2007).

Facility management services: The outsourcing risks here relate in part to user satisfaction of the facility which should be optimised (Mohd et al, 2016, p. 29). Tan, (2016, p. 86) explains that users' satisfaction may be assessed via two perspectives, namely the purposive approach, where the aim is to understand if the property is fit for purpose for a specific user and the aspiration-gap approach. In this instance, users have a set of aspirations for their space and require that the condition of the space meet their aspirations. With the four management principles above, there are other elements of risks exposure that requires mitigation and management. These are:

Exposure to and Elements of Facility Management Risks

Abbasi et al, (2005) define risks as the likelihood of an occurrence of uncertainty, unpredictable and undesirable nature which may alter the probability of investment the success. In outsourcing, other risks include a possible change in companies' ability to achieve both investment success and the failure of a relationship between the principal (client or client's representative) and the outsourcing vendor. In study by JLL (Jones Lang LaSalle Incorporated, 2015) an American professional services and investment management firm which specialises in real estate, have highlighted seven compliance and facilities related risks when considering outsourcing. These risks are: ethics, safety, vendor and financial management, labour management, information security, data governance and contractual risks.

Drivers of Outsourcing and the Effects on Stakeholders

Through vertical integration strategy in facility management, outsourcing plays a role in the transfer ownership and management of processes to a third party (Farncombe & Waller, 2005, p. 259). This transfer allows companies to focus on core contends that the capability benefit can maximised when you focus on those activities that matches companies' capabilities. Woodward-Pu, (2014) extend this notion when he argued that core competencies should never be outsourced so that it can be maximised when directed toward a single activity. In determining a company's key strengths, internal factors should be used to strengthen control and

ownership in the form of strategic asset management. Outsourcing should be complementary providing much needed support services which pertain to a core competency that are external to the company.

Risk Assessment Planning and Implementation

Risk assessments involve the identification of potential losses by means of establishing the extent of these, understanding the likelihood of the potential losses, placing significance to the potential losses whilst appraising overall risk attributed to it (Zsidisin et al, 2004, p. 398). Lee, Yeung and Hong, (2012, p. 544) proposed the failure mode and effect analysis (FMEA) framework to construct a risk map for qualitative risk assessment purposes. A FMEA according to asq.org (2018) can be defined as a step-by-step approach in the identification of possible failures in a design, assembly/manufacturing process, a product or service. A FMEA can be used during the design phase of a product, process or service, when an existing product, process of service is redesigned, prior to the modification of control plans for new or modified processes whilst analysing failures of existing products, processes and services.

Various factors which contribute to risk analysis using FMEA are taken into consideration, which aids in the exploration and diagnoses of problems at progressive stages of a process (Carbone & Tippett, 2009, p. 29). Stage one focuses on the identification, exploration and examination of the outsourced service. Stage two focuses on the quantification of risks, hence accounts for components such as probability, impact and detection factors. Stage three focuses on the understanding of what each risk entails. Consequences understanding is key to strategy formulation in the risk mitigation domain. Stage four focuses on the statistical techniques of outsourcing, with the cost and benefit associated with this being explored. Stage five focuses on the design of an action plan and, finally, stage six the stage where action is taken, leading to mitigation of risks.

3. Research Methodology

Research methodology is derived from the theory of data collection to acquire knowledge on the process, methods or procedures to assembled data. The data provides evidence to construct knowledge about the unit of analysis and serves as the base for the research strategy (Creswell & Clark, 2017).

In this paper a quantitative study using survey method was applied. The quantitative survey combines normative techniques with descriptive research to examine respondents' perception of outsourcing risks. The quantitative survey method was adopted to ensure participation by sufficient numbers of respondents. To this end,

self-administered questionnaires were distributed via email to 142 randomly selected respondents employee of participating facility management companies.

Respondents were requested to return questionnaires within 10 days of delivery. Participants were informed in the email that the questionnaire formed part of an academic study with participation being voluntary and that the information obtained will be used exclusively as part of the study and treated with utmost confidence. Persons inside of companies who have little or no exposure to either facilities management or outsourcing functions were excluded due to concerns that their limited understanding of both key disciplines may lead to these participants completing the questionnaire without fully understanding the contents of the said survey.

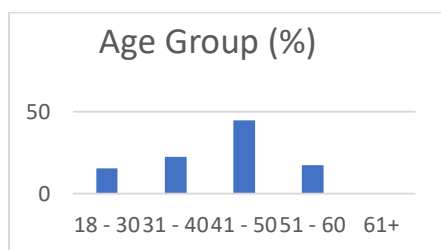


Table 3.1. Age Group (n=58)

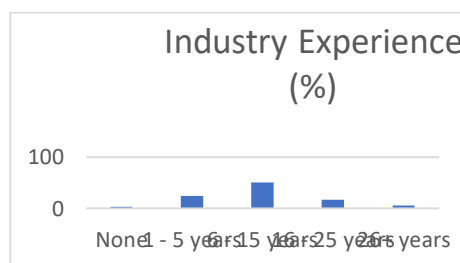


Table 3.2. Industry Experience (n=58)

Of the selected population of 142 persons, 58 participants returned their questionnaires in a completed state with a single participant responding with an indication of their desire not to participate in the survey. This meant that a total of 83 participants did not return any surveys, which equates to a 41% response rate. Although below 50%, several studies concluded that an increase in response rate does not increase survey accuracy.

Visser et al (1996) states that surveys with lower response rates (near 20%) yielded more accurate results than those with higher response rates (70%). Table 3.1 shows that the largest group of respondents (45%) falls within the 41-50 years old age group, followed by those in the 31-40 years age group (23%). A smaller group of respondents (17%) falls within the 51-60-year age group, with the remaining 15% falling within the 18-30-year age group. No participants over the age of 61 years participated. Industry experience specifically pertains to the amount of years participants were employed in or exposed to the facilities and/or outsourcing sectors. Half of the respondents fall within the 6-15-year bracket, with 24% falling into the 1-5-year bracket, 18% the 16-25-year bracket, 5% of respondents falling into the 26+ year bracket and 3% indicating that they have had no exposure.

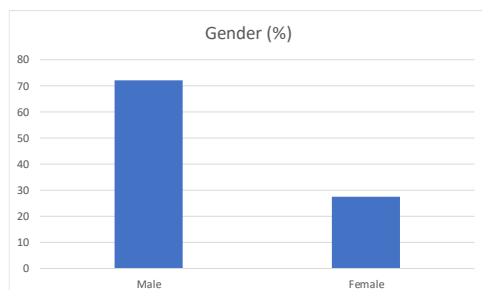


Table 3.3. Gender (n=58)

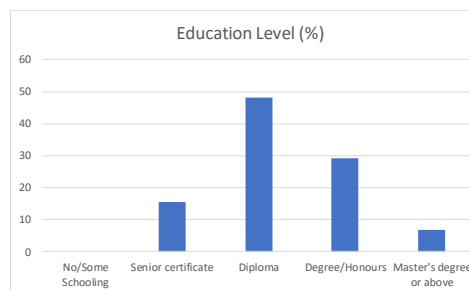


Table 3.4. Education Level (n=58)

As shown in Table 3.3, most of the respondents in this study were male (72%), with female respondents making up the balance thereof (28%). This represents a nearly 3-to-1 male to female ratio. Table 3.4 indicates a large section of respondents having obtained some level of tertiary education, with 84.5% having obtained a diploma or above and the remaining 15.5% of respondents having obtained a senior certificate. None of the respondents who participated have indicated none or only some level of schooling.

Instrumentation

Methods of instrumentation include gathering data on whether outsourcing of FM related services is prevalent in the participant's company, the level of outsourcing, the desired level of outsourcing in the opinion of the participant and the impact which outsourcing of FM related services have had on the company. Next, the reasons for outsourcing was measured. As adapted from the model presented by Burdon and Bhalla, (2005), noted that a Likert scale indicates key reasons as to why companies may choose to outsource FM related services was included.

Following this, questions pertaining to risk factors associated with the outsourcing of FM related functions, both inside (controllable risk) and outside (uncontrollable risk) of a company were considered. To identify the risk associated with the outsourcing of services on the facilities management environment, a survey consisting of variables which has been adopted from previous outsourcing studies (Keegan & Haden, 2000 and adapted by Ikediashi et al, 2012 p. 304) was used as the design approach which pertains to the perceived risks to companies from an outsourcing perspective. A 5-point Likert scale method of 1-strongly disagree to 5-strongly agree was employed.

Data Analysis

The software package used to conduct data analysis is called SPSS. The analysis of data was completed using basic inferential and descriptive statistical tools (Ikediashi & Okwuashi, 2015, p. 67).

4. Results

Nearly 64% of respondents indicated that facilities related services were outsourced within their organisation, with 33% indicating no levels of outsourcing and 3% being unsure. The variance between companies practicing full outsourcing (12.2%) and the desired level (15.5%) as well as companies where no outsourcing is prevalent (20.7%) and the desired level (22.4) is low. This indicates a general satisfaction between existing and desired levels of outsourcing.

Table 4.1. The impact outsourcing of FM services

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Positive	35	60.3	60.3	60.3
	Neutral/no change	10	17.2	17.2	77.6
	Negative	2	3.4	3.4	81.0
	Not applicable	11	19.0	19.0	100.0

When considering reasons why companies choose to outsource FM related services and as illustrated in table 4.2, the desire to focus on core activities, followed by the need to reduce costs are considered as the greatest reasons to do so.

Table 4.2. Descriptive Stats on Reasons Companies Outsource FM Services

Determinant	N	Minimum	Maximum	Mean	Std. Deviation
Q5.5 To focus on core activities	58	1	5	4.45	.921
Q5.1 Reduction of costs	58	1	5	4.43	.840
Q5.3 Access to greater knowledge/skills pool	58	1	5	4.29	.918
Q5.2 Shared risk/accountability	58	1	5	4.21	1.039
Q5.6 Competitive pressure	58	1	5	3.98	1.000
Q5.4 Less staff to manage	58	1	5	3.81	1.115

Table 4.3 takes both controllable as well as uncontrollable risks into consideration, with the risk which is assigned the highest risk being the one(s) with the mean closest to that of the maximum. A benchmark of 3 $(1+2+3+4+5)/5$ was set to determine the significant as well as non-significant factors, which is a model adopted by Ikediashi & Okwuashi (2015, p. 69), who used this method in a study to determine a number of critical success factors (CSFs) for the implementation of risk assessment and management practices within Tanzania's construction industry. Thus, any mean value greater or equal to 3 can be considered as significant.

Table 4.3. Descriptive Statistics for All Risks

Determinant	N	Minimum	Maximum	Mean	Std. Deviation	Rank	Remark
Q6.5 Information Security	58	2	5	4.07	0.876	1	S
Q7.2 Legal	58	2	5	4.07	0.856	1	S
Q6.3 Ethics/Compliance	58	1	5	4.03	0.955	3	S
Q6.2 Contractual	58	2	5	3.97	0.917	4	S
Q6.1 Financial	58	1	5	3.95	1.067	5	S
Q7.3 Economic	58	2	5	3.95	0.804	5	S
Q6.4 Staffing	58	1	5	3.84	0.951	7	S
Q7.5 Technology	58	2	5	3.79	0.913	8	S
Q7.4 Political	58	1	5	3.6	0.917	9	S
Q6.6 Vendor Management	58	2	5	3.59	0.817	10	S
Q7.1 Social	58	2	5	3.33	0.866	11	S

The top 6 risks ranked from the highest are information security, legal, ethics/compliance, contractual, financial and economic. The higher end of the mean scoring indicates a greater emphasis on controllable risks, with 4 out of the top 6 ranked items identified falling within this category. According to Ernst & Young, (2017), preventable or controllable risks present only negative impact, which should be avoided or eliminated. Information security risk was highlighted as the leading risk (mean of 4.07) companies are faced with when choosing to outsource facilities related services.

Many high-profile data breaches were found to occur due to physical security weaknesses, which emphasises the importance of adequate data protection, both at client (principal) and supplier level. Although risks to information systems can be mitigated by implementing items such as proper contract structuring, partnering with the correct service provider and understanding the company's information security objectives (Gonzalez, Gasco & Llopis, 2005) argued that an increase in information security risk will always remain when choosing to outsource facilities related functions. Legal risk was identified as the joint biggest risk (mean of 4.07) faced by companies who choose to outsource facilities related services. Pai and Basu, (2007, p. 29) states that any outsourcing agreement would require proper due diligence and legal planning as to prevent the common legal pitfalls. Thirdly, ethics/compliance risk was listed as a risk to companies when choosing to outsource facilities related services.

Ethical behaviour between the principal and service provider is of utmost importance, as failure to do so may see negative consequences both from a reputational and financial perspective. Following this, contractual risk was identified as the next biggest risk. According to JLL (2015), a breach in contract has both legal

and financial implications, with even minor infractions having serious ramifications. Financial and economic risks make up items number 5 and 6 considered as the biggest risks to companies conducting outsourcing functions. Whilst both items pertain to items of a monetary nature, financial risk specifically refers to controllable risk, with economic as uncontrollable.

5. Conclusion and Recommendations

5.1. What are the Risks of Outsourcing Facilities Management Services?

By considering the descriptive statistics, both controllable and uncontrollable risks appeared at the upper end of the combined table when ranked from the highest to lowest and using the mean as a benchmark. There is however an inclination towards controllable risks as the ones considered as greater risk to an organisation. Items such as information security, ethics/compliance, contractual and financial risk features prominently when considering controllable risks, with legal and economic factors featuring as such when considering uncontrollable risks. Information security and legal risk were deemed as the greatest risks facing companies who choose to outsource facilities management services. Gasco and Llopis, (2005, p. 299) study support this finding from an information security perspective while similar study by Platz and Temponi, (2007) found the legal risk to be greater.

5.2. Why do Companies Outsource Facility Management Services?

By considering descriptive statistics and using the mean as the benchmark, it was found that outsourcing allows a company to focus on its core activities (mean of 4.45 out of 5) was highlighted as a key determinant when considering outsourcing services. Another key determinant when considering reasons to outsource is a reduction in costs, with a mean score of 4.43 out of 5 reflected in this regard. Outsourcing, according to Embleton and Wright (1998, p. 96) stemmed from economic climate which places an emphasis on cost cutting and profit maximisation.

On the basis of the above discussion, this paper recommends as follow:

- (1) Conducting capability management exercises to prioritise in-sourcing of facility management services;
- (2) Consider drivers of outsourcing determine those which may resonate with the said company;
- (3) Apply the Failure Mode and Effect Analysis (FMEA) Where outsource is found to be prefer option for qualitative risk assessment, mitigation and management as part of the outsourced contract;

- (4) Develop partnerships with specialised third party and utilise analytical tool to identify, evaluate and mitigate outsource risks between partners and contractors.

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