Financial Services Authority

Offshore Operations:

Industry Feedback

April 2005

Contents

Overview

This report sets out the main findings of our recent review of offshoring operations to India.

Context of the feedback

For the purposes of this review we have taken 'outsourcing' to mean contracting another legal entity to do some of the firm's work. This entity may be part of the firm's group or a third party supplier. 'Offshoring' is moving some of the work to another country; whether to a 'captive'[1], third party supplier or a joint venture.

The FSA's Principles for Business state that a firm must take reasonable care to control its affairs responsibly and effectively, with adequate risk management systems. In line with this, firms' directors and senior managers are responsible for assessing and managing risks, including those related to outsourcing and offshoring. Offshoring is not inherently more risky than outsourcing domestically provided that there is suitable risk monitoring. Our existing policy for outsourcing can be found in Senior Management Arrangements, Systems and Controls (SYSC) and for banks and insurers in the Interim Prudential Sourcebook for Banks (IPRU(Bank)) and the Integrated Prudential Sourcebook (PRU) respectively. A firm, which must also notify us of any material outsourcing arrangements, cannot contract out of its regulatory obligations and should take reasonable care to supervise the discharge of outsourced functions.

This report does not constitute formal guidance from the FSA given under section 157 of the Financial Services and Markets Act. We hope that the findings of our review will help senior managers and staff involved in outsourcing and offshoring in the financial services industry. It aims to help them compare the nature of their risks and risk management practices with those of their peers. While any regulated firm – whether big or small – can offshore activities, we would want all regulated firms to identify, assess, monitor and manage operational risks arising from offshoring. This report sets out some examples of practice implemented by a cross section of firms to monitor and manage risks arising from offshoring which, in the context of the operations of those firms, we found to be consistent with our policy. These are practices that could be considered by other firms already offshoring activities or intending to in the future, although of course whether any firm's systems and controls are adequate to meet our regulatory requirements will depend on the circumstances of that particular firm.

1 Retaining the business in-house; e.g. by setting up a wholly-owned subsidiary company in India.

Methodology and scope

A number of firms we regulate have set up operations offshore to support operations in the UK. The largest retail groups we supervise most frequently set up in India and, hence, we chose it for this review.

We visited ten operations (some captives and some external suppliers) in India. Most of these provide services for the UK operations of retail banks and insurance companies, with one wholesale group included in the review.

In addition to this, we had input to the project from another five firms – 15 firms in total (including the ten we visited in India) returned a questionnaire with information on their current operations in India. We also visited firms in the UK both before visiting India and when we returned to gain an insight into the governance and control functions operating here.

We would like to thank the management and staff of the firms and their suppliers who participated in the review for the information they supplied and for meeting us.

Main conclusions

Our overall conclusion is that offshoring can contribute a material risk to the FSA objectives of:

- market confidence;
- reduction of financial crime; and
- consumer protection.

The main risk identified is the complexity of achieving suitable management oversight and control from a distance. However, appropriate governance frameworks, risk management systems and controls can identify and mitigate operational risks from offshoring.

Our review shows that the cross-section of firms we covered are aware of these and their own firm-specific risks and are taking appropriate actions. Currently, all have formal oversight structures and it is important that, even as this mode of operation becomes more common, the risks remain under such scrutiny. Not least since the impact of offshoring greater volumes and more complex functions will affect the firm's risk profile, particularly in relation to its operational risks.

However, it should be noted that the firms in this exercise were, by definition, major groups and so we would expect them to have appropriate risk management control frameworks in place. More generally, any firm undertaking this sort of activity would need to be able to demonstrate appropriate oversight from the UK.

We provide more detailed analysis within the body of this report but two main observations about offshoring to India relate to attrition and business continuity planning.

Staff Attrition

The industry in India is experiencing a high level of staff attrition[2], largely because it is quite a young industry. The level of attrition depends on the method of entry chosen (captive or third party supplier), the processes offshored (call centre or back office) and the length of time that the operation has been in India (pilot as compared to an operation that has been in India for a number of years). For some activities, however, the rates are comparable to those in the UK.

While attrition is a risk it was stated in all cases that this risk is being monitored and that there are strategies in place to combat it. These include programmes to motivate staff to stay within a company and industry-wide initiatives pioneered by an Indian trade body, the National Association of Software and Service Companies (NASSCOM). We were concerned that high attrition could adversely impact service provision but found that firms had factored it into their recruitment and training capabilities.

Business Continuity Planning (BCP)

The market for warm sites[3] in India is non-existent at present as the cost of such facilities is comparatively high. Therefore firms have had to develop alternative strategies for BCP. Options that have been pursued include repatriation to the UK (which is the most popular option given that very few companies offshore 100% of any process), development of a joint site with other companies/suppliers, and, if the operation is large enough, spreading processes across more than one site or city within India. At least one group has a worldwide BCP strategy so their presence in more than one continent provides reciprocal back-up capability.

As processes ramp up and new processes are migrated, firms increasingly need to monitor the potential for business disruption and its likely impact, and assess the most appropriate countermeasures for the group.

2 Staff turnover

3 A warm site is an alternate facility that is electronically prepared, equipped and furnished for operation. It can be fully operational within several hours.

Introduction

Objectives

1. Offshoring to India has increased markedly over the years due to stated benefits such as the growth of low-cost, well-educated labour pools and the development of low-cost data transmission capabilities.

2. Our objective in reviewing operations in India was to investigate:

   a. how financial services firms manage risks arising from offshoring;

   b. how the risks identified are evolving; and

   c. the risks they pose to our objectives.

3. In some cases, we were already familiar with how the UK firms exercise control over these operations, as we have undertaken visits and engaged in regular contact with supervised firms. By visiting the operations in India we were able to review the process and risks from the overseas service providers' perspective.

Scope

4. Our review covered industry practices and standards in outsourcing and offshoring by major financial groups trading in the UK.

5. Some of these groups are UK firms and others are foreign-owned, with head offices that are themselves overseas. In the case of the latter, some depend on the provision of some services from their mother countries. We did not cover this aspect during the review, although we would naturally expect the UK management to have a clear understanding of the risks of such a dependency and processes for monitoring the adequacy of the provision of such services.

Methodology

6. We devised a standard questionnaire which, during October 2004, we sent to all the largest retail groups with operations in India. Once the questionnaires were returned we examined where in India the operations were based. We found that the majority of operations were based in Mumbai and Bangalore. It should be noted that some firms have operations in more than one location.

	Bangalore	Mumbai	Pune	Other
Companies	8	6	4	3

7. During November 2004, we visited firms in the UK to gain an insight into the operations we would be visiting in India and to appreciate how these relationships are governed.

8. In the week beginning 13 December we visited five firms in Mumbai. Between December 16 and December 22, we visited another five firms in Bangalore. The firms were third party suppliers, captives and a joint venture operation.

9. In January 2005 we conducted more meetings in the UK with those groups that we had not seen overseas because they were in a different location to those we visited in India or that we did not have the opportunity to see before going to India.

10. We have also studied generally published material on offshore operations and on India.

Queries

11. Rachelle Wilson and Frances Allen conducted this review and wrote this report.

This report is published for information but should you wish to provide us with comments please address them to:

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Findings

Strategy

12. Most companies had a documented strategy for outsourcing/offshoring and the decision to move operations offshore was mostly ratified or taken by the Board in response to a formal proposal. A number of firms had a clear idea on a finite size limit, in relation to their overall activity, on offshore operations.

13. Where a third party supplier is used, most companies adopted a flexible model for the arrangements in India using the build-operate-transfer (BOT) approach. This gives companies access to third party expertise at the outset and, once they have attained confidence and experience, they then convert these operations into captives. This is a faster way to get into the market and some firms noted that this was also a less risky way to get started. Some of the larger operations in India, which have been using third parties for a couple of years, are now at the stage where they are considering switching to captives.

14. While cost advantages were the initial impetus for offshoring, many financial services firms now note that they will continue offshoring to India, almost regardless of the economic environment, due to other benefits. Firms stated that as most of the staff were graduates the quality of work is extremely high. In addition, increased flexibility was seen as a benefit.

15. Flexibility of operation is achieved through operating services around the clock. This is partly due to time difference (GMT +5.5) and the use of night/shift-work to meet the needs for call centre activity in UK-acceptable hours. The time difference works particularly well for back office functions. The UK ends the day and closes operations (and, if appropriate, runs batch processing); India then picks up reconciliation and investigation activity a few hours later in their morning and can discuss problems with the UK during their afternoon (the UK's morning).

16. A variety of processes are sent offshore, including call centre (e.g. personal banking telephony, inbound and outbound collections, non-FSA regulated sales) and back office processes (e.g. servicing of accounts, claims first response and verification, insurance renewals). All groups start with simpler processes but, as they gain confidence, they expand the range of activities undertaken offshore. Many have been so happy with the quality of service that they are starting to bring over end-to-end processes and/or offshore more complex processes, e.g. financial research and underwriting.

17. Similarly, while in the early days much time is spent convincing business to consider moving part of their operations, now many firms have reported an excess of demand. As a result, some have taken a conscious decision to cap the amount of work that can be sent offshore. This was primarily due to business continuity requirements and the capacity of the offshore location to handle more business. Most also have improved the rigour with which proposals are assessed to more clearly identify processes that are suitable to be moved offshore and those that are not. In addition there is, typically, an

overarching strategic body to prioritise projects to ensure that not too much is moved in too quickly.

18. It should be noted that to date most companies still have the majority of operations in the UK so that critical functions can be repatriated if needed.

Due diligence

19. Most companies treat any decision to move offshore in much the same way as they would a major change programme, the setting up of a new office or a significant outsourcing initiative. They set up a formal governance framework and the associated authorisation processes. The due diligence required is similar to that of a major initiative but includes the consideration of country-specific risks and those related to providing and managing operations from a long distance.

20. Companies conduct due diligence to ensure all associated risks are mitigated. Moving too quickly to achieve the cost reductions and other benefits may not result in effective assessment of all of the risks. Most companies visited documented all of the processes to be migrated, which not only enhanced their understanding of the processes for the Indian operations but also improved their understanding of processes used in the UK.

Contract/service level agreements

21. All firms with offshore operations have contracts and have established service level agreements (SLAs), relevant to the nature and scale of operations. All have formal governance structures and escalation processes in place so performance, future workloads and new initiatives can be discussed. There is usually a person on the ground in India who ensures that the processes are meeting the required operational performance levels and that they comply with policies and regulatory requirements. Resource levels are planned in advance.

22. As with any outsourcing arrangement or the relocation of a process within the UK, firms have learnt that they need to make allowance for stabilising the process and training. So a number are setting performance targets to reflect this but which ramp up over time to at least meet those of the donor locations.

23. Targets are monitored in much the same way as they are in the UK. As well as direct measures (e.g. call waiting time and duration, number of claims processed, critical time deadlines met, etc.), this includes quality checks and customer satisfaction surveys. Most firms noted that performance to date either meets that achieved in the UK or exceeds it.

Change management

Transition and migration

24. As should happen with any new process in the UK, new functions are migrated using formal project management techniques. Staff that assist with one migration/transition

are often moved onto the next ones, as otherwise it was found that new areas had difficulty in implementing new processes.

25. Once a process has been migrated, it is usually subject to a period of parallel running (the length of time depends on the complexity of the process). Initially, the level of oversight by and assistance from the donor locations is quite significant but this diminishes once the offshore staff gain experience. Nonetheless, even once the process is mature a predetermined level of performance monitoring by the donor location continues.

Quality and continuous improvement

26. Most of the third party suppliers firms choose to use in India are ISO9001 (quality standard) and CMM (Capability Maturity Model standard) Level 5 certified. Some suppliers are focused on quality management and use Six Sigma to institute projects for change and continuous improvement. Some firms with captive operations are also adopting these techniques and hiring staff with the necessary qualifications. These teams re-engineer processes to make them more efficient and effective. Process improvement is a cyclical model.

27. Most of the UK businesses using the Indian services have a formal change process which requires the UK to authorise changes. This is particularly important if the same process is still undertaken in the UK, especially when this is a deliberate policy to enable cross-country business continuity planning. Nonetheless, some things can be improved locally without affecting UK operations. At present, most third party suppliers do not do any end-to-end process in India. By having only one part of the process, they have been able to identify problems and rectify them. Smaller processes are easier to re-engineer.

28. Firms that have been offshoring to India for a while, in particular, are now in a position where some changes initiated in India have subsequently been successfully adopted in the UK. A number encourage their Indian operations to suggest changes via existing staff suggestion schemes and we observed that this was something that the staff were eager to do.

Recruitment

29. Most companies recruit graduates, all of whom speak English. Some require no business experience while others require experience in addition to degrees. Recruitment is done via consultants, directly ('walk-ins', whereby people come in off the street, seem to be a common practice in India), advertisements or through a referral process from existing staff.

30. Staff undergo a thorough vetting process, at least in line with the parent company's standards. Some firms commented that certain checks were different (e.g. credit referencing could not be done in the same way, as much of the population do not hold bank accounts). However, one firm reported that some aspects of the vetting process in

India were rated as superior to that elsewhere in the region, and this good practice was now being adopted elsewhere.

Training

31. As would happen in the UK, all staff undergo induction training to give them an understanding of the company, its culture and policies. Where the firm uses a third party supplier, this will typically cover an understanding of both the supplier and the client firm.

32. Specialist language training is typically required for call centre work but not for back office functions; although a few firms provided it for all staff. Some firms use external specialists but supplement them with their own training. Some also play English films and television programmes in the canteen so that the staff can hear a variety of accents on an ongoing basis.

33. Process training takes six to ten weeks depending on the complexity of the process. Once a process is mature, training is repeatable and done locally. There are three ways in which training can be conducted initially and most firms used a mixture of these.

- The whole team goes to the UK to train.
- Part of the team goes to the UK and then comes back to India to train the rest of the team.
- UK trainers come to India and then leave when the process is stabilised.

Relationship management and oversight

34. We require regulated firms to be responsible for effectively managing the risks of outsourcing arrangements and this requires effective oversight. Most firms developed a governing body that is charged with the oversight of the offshore operations and also the strategic decisions involved with deciding which processes should be migrated. It typically consists of the Heads of the Operational areas involved and key advisers, e.g. Risk, Compliance, IT and HR.

35. In most cases where a third party was used, there was an Offshoring Manager who had oversight of and specific day-to-day liaison with the operation in India. This role involved both oversight from the UK and frequent visits to India. In two cases we felt that this key contact posed a key person risk but the firms have assessed the situation and have plans to address it. Some firms using third party suppliers had a team of people on the ground which strengthened the oversight function and mitigated key person risk. Most encourage staff at all levels to feel part of the firms' operations as well as the supplier's.

36. Captive operations were structured in a similar way to the UK. Some firms have a few expatriate managers employed at the Indian locations. Service levels and performance are monitored as they are for the same operations undertaken elsewhere in the group.

The Indian operations, particularly at management level, participate in the same meetings where possible (e.g. by use of conference calls, video links, visits to the UK, etc.). This concept cascades down and most firms also have some level of formal and informal interaction between managers, team leaders and staff with their counterparts in other countries.

37. All firms have mechanisms whereby changes in UK regulations are advised to and implemented in India, typically via the relevant business unit. In most cases, compliance is monitored both locally and from the UK, with overall oversight responsibility being vested in the UK.

38. A number of firms have also implemented their risk assessment practices (e.g. Control Self Assessment) in India. In some cases, the Indian operations were considered during an assessment of the overall business process (UK and India) but with India also taking responsibility for identifying and addressing its own country/operation-specific risks and controls.

39. Depending on the group structure, the group, region or UK Internal Audit functions are responsible for assessing the risk of the Indian migrations and operations and incorporating them in their audit plans, accordingly. A number of captive operations, having reached a viable size, have set up a local audit presence, typically reporting to group or UK audit functions.

Contingency planning

40. All of the operations visited had contingency plans in the event of a serious problem. The size of operation examined influenced the Business Continuity Planning/Disaster Recovery Planning (BCP/DRP) arrangements. Companies with larger operations have already been able to spread to multiple locations.

41. Some suppliers have a policy not to employ more than 3,500/4,000 in any one city. Some firms already have offices located in more than one city (either as captives or via their suppliers) and others are considering this. This enables them to attract different skill sets as the nature of the work undertaken in India broadens, but also gives them some local business continuity opportunities. This minimises risk through multiple delivery locations.

42. Others are experiencing significant problems organising local BCP options. There is no external market for warm sites (such as Sungard in the UK) as the cost of buildings is prohibitively high in comparison to the cost of labour. (Conversely, in the UK, labour cost is higher so companies want full utilisation of staff, which is one of the reasons for having a warm site.) Propositions to resolve this include having a joint site with other companies. Others are considering developing their own warm site once their operations get to a critical size.

43. In most cases building evacuations are tested regularly. Most test their BCP at least annually and BCP forms part of the initial migration project planning. As ramp-ups

occur BCP requirements generally change in line with the business needs. The priority of most processes are defined along with their time criticality. Of those suppliers and subsidiaries that have a warm site option, at least one felt that the warm site is the last resort as resource is flexed between India and UK first, where appropriate.

44. Most companies still have the capacity in other parts of the world to pick up critical workloads from India should the need arise. The fact that the data storage and main systems are outside India, with data only passed there as necessary for processing, makes this easier. However, firms do have to ensure that staff remain suitably familiar with the processes to be able to fill in. At least one firm has a deliberate bi-polar BCP strategy. As several other firms do, they conduct tests at least annually to ensure that the UK can undertake work on behalf of India and vice versa (i.e. the UK also tests its BCP in reverse with India taking the calls, etc.). This highlights an added benefit from offshoring, which is to maximise business continuity between the UK and India.

Exit strategies

45. Most companies still have the capacity in the UK to repatriate if need be, which is particularly important for smaller operations.

46. Some companies had multiple strands to their exit strategy depending on whether the requirement to exit was due to the operation or supplier failing and therefore another option offshore needing to be pursued. Exit requirements (e.g. transition support and penalties) are generally built into the contracts with third party suppliers. The speed with which processes can be transferred to another supplier or repatriated back will depend on the type of process and amount of work offshore.

Country specific risks

Staffing

Availability and quality

47. With approximately 2.5 million English-speaking graduates a year in India, there is no shortage of suitable recruits. As discussed, careful choice of which functions to offshore, where offices are located and, indeed, a multi-location strategy should ensure a suitable availability of people with the appropriate skills.

48. It was noted, however, that in some cases during the early stages of offshoring it was difficult to find acceptable candidates for managerial / senior posts and that where they are available, their salary expectations are on a par with those of their UK counterparts. However, as the business tenure increases more and more people are being promoted from within. This reduces the cost, satisfies the requirement to have skilled people in management positions and also motivates staff to stay with the firm and to strive even harder, as they can see a career path.

Call handling

49. We listened to calls at most locations and were impressed by the calibre of staff handling the calls. Not only were they clear in speaking, they also possessed the necessary skills and technical expertise to handle enquiries quickly and efficiently. This, in part, also served to demonstrate the benefits of well designed processes and training. There are team leaders available to refer calls to if the agent cannot handle the enquiry. Staff are also encouraged to get help from other staff around them if the enquiry is particularly difficult.

50. Call monitoring is usually done by both Indian and UK management. They do this either by logging onto a call monitoring system through the third party supplier or directly through the UK call monitoring system.

Back office processing

51. In most situations, the back office processing was exceeding the SLAs set for similar operations in the UK. Some SLAs have been revised upward to account for the favourable experience in India.

Staff Attrition

52. In India, attrition could be regarded as a symptom of concentration risk as more firms move into the same locations offering job opportunities. However it is mainly symptomatic of the relatively young age of the people working in the business process outsourcing (BPO) and Information Technology (IT) sectors. All companies consider attrition a risk and its impact is continuously assessed. In financial services many of the headline rates reflect operations supporting the US, where the working hours are very anti-social.

53. On the whole, attrition was stated to be either the same or better than the UK experience. It is generally higher in the third party suppliers; however, this again depends on the arrangement established. We did see companies that have quite low attrition. Management and knowledge-based jobs have so far not experienced any significant attrition. Non-voice processes (e.g. back office and administration tasks) generally have lower attrition than voice; rates are typically 10% and 30% respectively. Attrition for some companies' voice operations is lower than in the UK. Newer/pilot operations generally have higher attrition until the operation settles down.

54. Firms are analysing reasons for attrition. The main reasons staff leave are to pursue higher full time education and/or marriage, with women either not permitted to work after they marry or moving to where their husband is located.

55. There is no shortage of suitably qualified candidates (one firm stated that it hires only 10% of applicants) and, indeed, the reason for choosing a specific location includes the proximity of good universities. To deal with attrition and the consequent need to constantly hire new recruits, companies ensure that they have well-documented

processes and standard, repeatable training modules. As they grow to a reasonable size, firms are able to cross-train existing staff and back-fill vacancies.

56. Nonetheless there are efficiencies to be gained by lowering attrition rates and some companies are developing retention programmes. Some are offering exchanges to the UK; others use training trips as a reward. Other programs to combat attrition include multi-skilling staff in other processes, swapping between voice and non-voice so that they do not get bored with either, or even moving across companies (where permitted) within a third party supplier. A great deal of recruitment is done through a referral process so existing staff work with friends. Together with initiatives such as involving staff in more social activities together, this aims to make the firm an attractive place to work. Some companies also offer concierge services to staff – such as paying bills for them, purchasing movie/theatre and transport tickets, etc. – as the staff do not have the time to do these things while at work. Other initiatives include making the remuneration package more competitive (based on an annual survey of the industry) and developing career opportunities through internal promotion programmes.

57. Some firms are entering 'no poaching' agreements with each other. NASSCOM (India's trade body active in the software and the BPO arena) is also developing a database of workers who have served their notice period (one month) and that have been granted a 'leaving certificate' from their previous employer. Companies are abiding by a NASSCOM-promoted Code of Conduct/Ethics whereby they will not employ people who do not serve their full notice period or are persistently 'job-hopping'. The database will be made accessible to companies so they can make such checks. Third party suppliers and captives are involved in this initiative.

58. We also noted that the risk of attrition is agreed in some contracts. The onus is on third party suppliers to manage attrition levels to keep costs down.

Tax and legal

59. Local regulation and legislation has to be taken into account and most firms use local external experts to keep them advised. Once they have gained a critical mass, some firms find it beneficial to hire the expertise in-house. We comment on some of the India-specific considerations below.

Software Technology Parks of India (STPI)

60. All IT and BPO work that is for export comes under the STPI, which is effectively the IT industry regulator. The STPI Scheme was intended to encourage this industry and so, as well as favourable tax concessions, STPI also set up TV radars on buildings for satellite links for the firms. The industry has now matured to the point where a lot of the companies operating in Bangalore have more advanced technologies than this; however other cities might still benefit.

61. Although there is no obligation to do so, companies need to be ‘registered’ to get benefits, such as a tax break on profits and duty free imports on equipment and so on. It was stated by some that the tax break only made a difference of 3-5% of costs. The scheme was originally meant to last for the first ten years of a company’s operation but is now expected to end in 2009. However, all firms have taken this impact into account.

62. To gain these benefits the company must meet basic criteria, such as the requirement that a company has to export five times the value of imports over a five-year period. The company also needs to meet specific obligations, such as filing ‘softex returns’ annually (details of monies received). There are also quarterly and monthly returns which monitor how much a company imports and exports.

63. All overseas equipment bought under the duty free scheme is ‘bonded’ to the building that the company is in. We were advised that this does not create any problems, as equipment can be sold via a ‘debonding’ process and that it always makes commercial sense to use this benefit. At the time of sale the duty has to be paid on the written down value of the piece of equipment.

Value Added Tax (VAT)[4]

64. At the time of the visits there were proposals under discussion relating to the introduction of VAT in India in 2005. However, most companies stated that VAT will replace the current sales tax and therefore the net effect is minimal. Recently the decision to implement VAT has been taken in 21 of 28 Indian states.

Staff Transport

65. A national law states that companies requiring female staff to work late hours have to provide transport for them to get to and from work. Some firms have decided to apply this to all (male and female) staff that have to be at work before 9am and after 6pm. Some suppliers offer a door-to-door service, while others offer point-to-point and some do a combination of both, depending on the hour.

Security

66. We observed a high level of security in operation and some firms stated that security is far more controlled than in the UK. For suppliers, controls over people, processes and access swipes are client-specific; for firms it is line with their own policies. Some have used their own or external security experts and internal auditors to define and review arrangements.

67. Most companies had swipe entry clearances to enter the premises; one supplier had an airport-style detector. Individual floor or office entry was further restricted by swipe card access to specific client areas (for relevant supplier staff) or particularly confidential areas

4 On 3 March the European Court of Justice issued a final ruling on the Andersen Case (Arthur Andersen) that outsourced back office activities provided to insurers in the EU are not VAT exempt. Initial discussions with the sector indicate that some may be considering moving their outsourced operations offshore. The actual implications of the ruling are currently under discussion between the relevant authorities and the industry; but are expected to be addressed in the next couple of years so it is premature to consider this aspect in our report.

(for relevant firm staff), such as offices where company research activity is undertaken. Some companies had CCTV and/or security guards walking the floors.

68. Generally speaking, a firm's staff working in call centres and all supplier staff are not permitted to take mobile phones, bags, cameras, etc. in to their work station. There are lockers provided. If bags are permitted on the floor, they are checked for confidential information, computer discs, etc. At some companies staff are given numbered paper to write notes on during the day and this has to be handed in to verify that all the paper is accounted for before they can leave; others ensure all written material is shredded in the room. Computers do not have hard drives, floppy drive access, access to email/internet or printers. Where printers are required, access is controlled and restricted to relatively senior people.

69. Most of the third party suppliers firms choose to use in India are BS7799 (British Standard for Information Security) certified. Companies have also installed systems to automatically lock out staff access to computers and buildings if they resign. In all companies reviewed, data is stored onshore in the UK and transferred to India as necessary where it is accessed via 'green screens'. Some firms recorded a percentage of calls in India for quality assurance and training purposes. Where this occurs access to the calls is restricted to specific individuals, there are adequate control procedures around the system and the calls are deleted after a suitable time period.

70. In conclusion, companies have implemented systems to monitor phone conversations, protect data and monitor staff. There is no evidence to suggest consumer data is at greater risk in India than in the UK.

Concentration risk

Location in India

71. Firms do consider country risks (e.g. political, legislative, security, cultural, etc.) when deciding which country to move to. Most did assess – and some continue to assess – the suitability of other countries. It was noted that India has several advantages as a leading offshore destination:

- low cost – although staff costs are rising, firms commented that this has been compensated by decreases elsewhere (e.g. telecommunications);
- established destination for outsourcing;
- large pool of English-speaking graduates;
- low-cost data transmission capabilities;
- Indian suppliers offer near-shore services (i.e. have a UK presence);
- Indian vendors are expanding organically and inorganically to establish a multi-location presence in India, to de-risk their business; and

- Indian government backing and encouragement, e.g. to improve the technical infrastructure and education systems to meet the demand.

72. India is such a large country that, of itself, it does not pose a concentration risk. In the context of the influx of a number of firms, however, we did want to know how firms were assessing the risks relating to the concentration of activities in specific locations.

73. We asked a number of groups why they selected the location they did in India. Most rated the different locations against a balanced scorecard comprising aspects such as: people available (numbers with the required skill sets), competition, attrition, infrastructure (IT and physical, e.g. buildings, transport and security aspects). There were a number of cities which featured in most firms' shortlists. Aside from Mumbai and Bangalore (which are the two most used at present), these were Pune, Chennai, Delhi, Kolkata, Hyderabad, Mangalore and Goa.

74. We noted no real differences between Bangalore and Mumbai, apart from some infrastructure issues. Bangalore frequently experiences blackouts, but each company has its own generator so little or no time out is experienced. The industry installs multiple back-up options as firms cannot afford downtime. Bangalore has better streets and infrastructure and less traffic; however, it does not yet have direct flights from the UK (this will apparently change in 2005 with the development of a new international airport).

Availability of suppliers

75. The same few suppliers appeared on everyone's shortlists and there was an observable difference between the two or three established suppliers and the newer and smaller ones. However, firms assured us that there were still plenty of suitable suppliers to choose from.

76. The decision to develop a captive or use a third party stemmed from the current international experience of the firm offshoring; rather than from lack of supplier choice. If the firm already had experience in overseas markets then they were more likely to pursue the captive option. The speed with which the firm wanted to implement also influenced which method was pursued. Firms that required a faster entry to the market opted for third party suppliers who had the experience in the functions being outsourced.

Other issues

77. As a result of offshoring there is some political risk in the UK. There has been backlash in the media about workers' job security in relation to the practice of moving work offshore; although some report that overall the UK is a net gainer of overseas jobs. More recent coverage of US-based analysis suggests that both donor and recipient countries of offshoring arrangements are net beneficiaries in GDP terms. Most organisations offshoring note that job losses in the UK are met through redeployment and natural turnover.

78. Job security fears could lead to poor performance and disaffection in the UK. Most firms recognise this risk and have an active communications strategy from the outset, ensuring that UK staff and, where relevant, unions are kept informed throughout. A number of UK staff have had the opportunity to visit India (e.g. to deliver training) and have found the experience positive. A number of firms commented that as all or part of their existing jobs move offshore, often UK staff are freed up to undertake other fulfilling roles.

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