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ITB11456

This chapter appears in the book, *Managing Successful IT OUtsourcing Relationships,* by Petter Gottschalk and Hans Solli-Saether. © 2006, Idea Group Inc.

Chapter IX

Governance Structures

The overall objective of this chapter is to concentrate on the important issues of strategy, structure, and management of IT outsourcing arrangements. Using well-known theoretical perspectives described earlier in this book and experience earned from several business case studies in this book, we present a governance model for successful management of IT outsourcing relationships.

Perspectives on Governance

IT governance can be defined as a firm's overall process for sharing decision rights about IT and monitoring the performance of IT investments. Weill and Ross (2004) define IT governance as specifying the decision rights and accountability framework to encourage desirable behavior in using IT. IT governance is not about making specific IT decisions—management does that—but rather determines who systematically makes and contributes to those decisions. IT governance reflects broader corporate governance principles while focusing on the management and use of IT to achieve corporate performance goals. Effective IT governance encourages and leverages the ingenuity of the enterprise's people in IT usage and ensures compliance with the enterprise's overall vision and values.

All enterprises have IT governance. Those with effective governance have actively designed a set of IT governance mechanisms (committees, budgeting processes, approvals, etc.) that encourage behavior consistent with the organization's mission, strategy, values, norms, and culture. In these enterprises, IT can factor significantly into competitive strategy. In contrast, enterprises that govern IT by default more often find that IT can sabotage business strategy.

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Before we dive into IT outsourcing governance, we must look at the broader issue of corporate governance in enterprises. Corporate governance is concerned with governing key assets, such as (Weill & Ross, 2004):

- *Human assets*: People, skills, career paths, training, reporting, mentoring, competencies, and so on.
- *Financial assets*: Cash, investments, liabilities, cash flow, receivables, and so on.
- *Physical assets*: Buildings, plant, equipment, maintenance, security, utilization, and so on.
- *Intellectual Property (IP) assets*: IP, including product, services, and process know-how formally patented, copyrighted, or embedded in the enterprise's people and systems.
- *Information and IT assets*: Digitized data, information, and knowledge about customers, processes performance, finances, IS, and so on.
- *Relationship assets*: Relationships within the enterprise as well as relationships, brand, and reputation with customers, suppliers, business units, regulators, competitors, channel partners, and so on.

As we can see from this list, IT outsourcing governance includes not only information and IT assets. IT outsourcing governance is concerned with several of these assets, sometimes even all of these assets. From this perspective, IT outsourcing governance may be as comprehensive in scope as corporate governance.

In governing IT outsourcing, we can learn from good financial and corporate governance. For example, the chief financial officer (CFO) does not sign every check or authorize every payment. Instead, he or she sets up financial governance specifying who can make the decisions and how. The CFO then oversees the enterprise's portfolio of investments and manages the required cash flow and risk exposure. The CFO tracks a series of financial metrics to manage the enterprise's financial assets, intervening only if there are problems or unforeseen opportunities. Similar principles apply to who can commit the enterprise to a contract or a partnership. Exactly the same approach should be applied to IT governance (Weill & Ross, 2004).

The dichotomy market or hierarchy has exercised a dominant influence on the study of forms of governance and their operation for some time. However, in the past two decades, there have been large numbers of investigations of intermediate forms of governance. Subsequently it has been recognized that the behavior that occurs within exchanges is not necessarily determined by the forms of governance used, and this points to a need to understand behavior within a variety of exchanges. Blois (2002) defines governance as the institutional framework in which contracts are initiated, monitored, adapted, and terminated. An exchange occurs between two organizations when resources are transferred from one party to the other in return for resources controlled by the other party.

The organization of interfirm exchanges has become of critical importance in today's business environment. Many scholars have criticized the inadequacies of legal contracts as mechanisms for governing exchange, especially in the face of uncertainty and

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