

Chapter 1

Outsourcing Opportunities

In this chapter on outsourcing opportunities, a common conceptual understanding of important issues of the business practice of our interest is established. First, we take a look at how researchers have defined the term outsourcing. An updated outsourcing definition will serve as a common platform for understanding the sourcing universe presented in the following section. Next, we describe in more detail the building blocks of the sourcing universe – insourcing, information technology (IT) and information systems (IS) outsourcing, business process outsourcing, transformational outsourcing, and global outsourcing. At the end of the chapter, we discuss some key aspects of the important outsourcing decision.

OUTSOURCING DEFINITIONS

If a firm does not want to use its internal resources to build or operate information systems, it can hire an external organization that specializes in providing these services to do the work. The *process of turning over an organization's computer center operations, telecommunications networks, and/or applications development to external vendors is called outsourcing* (Laudon & Laudon, 2005).

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Loh and Venkatraman (1992a) define IT outsourcing as *the significant contribution by external vendors in the physical and/or human resources associated with the entire or specific components of the IT infrastructure in the user organization*. Vendors may contribute computer assets for the user from outside the organization. Alternatively, the ownership of certain computer assets of the user may be transferred to the vendor. Similarly, vendors may utilize their personnel to provide the required services, or the vendor may employ existing staff of the user. In their research, they attempted to explain the degree of IT outsourcing by using cost structures and economic performance. They found that the degree of IT outsourcing is positively related to both business and IT cost structures, and negatively related to IT performance. IT outsourcing was framed as a make-versus-buy decision, where contractual modes differ in the domain of influence within the corporation (Loh & Venkatraman, 1992a, 1992b).

Lacity, Willcocks, and Feeny (1996) define outsourcing to *dismantle internal IT departments by transferring IT employees, facilities, hardware leases, and software licenses to third-party vendors*. Hirschheim and Lacity (2000) define information technology outsourcing as the practice of *transferring IT assets, leases, staff, and management responsibility for delivery of services from internal IT function to third-party vendors*.

In research by Grover, Teng, and Cheon (1998), they define outsourcing of IS functions as *the organizational decision to turn over part or all of an organization's IS functions to external service provider(s) in order for an organization to be able to achieve its goals*. This decision-making approach is interesting because it focuses on an early stage of a long process. Resource-based theory and resource-dependence theory from the field of strategic management and transaction cost theory and agency theory from economics are used in order to describe its implications for outsourcing research and practice. The definition includes decisions about how to arrange external IT services. Using several theoretical perspectives of outsourcing, they presume that organizations attempt to make these decisions in their best interests. Similarly, Grover, Cheon, and Teng (1996) define outsourcing as involving *a significant use of resources – either technological and/or human resources – external to the organizational hierarchy in the management of information technology*.

Hu, Saunders, and Gebelt (1997) define information systems outsourcing as *a business practice in which a company contracts out all or part of its information systems operations to one or more outside suppliers*. Here we find that outsourcing is a practical issue that also has a significant impact on business organization. Even though outsourcing is a business practice, for IS executives acquiring outside services is an important strategic issue confronting their organizations. Thus, their theoretical perspective is strategic decision-making. In their research they have identified sources of influence in the adoption decision. One significant influence is the combined effects of external media, vendor pressure, and internal communications at the personal level among managers.

Outsourcing can be defined as *turning over all or part of an organizational activity to an outside vendor* (Barthélemy, 2003). Here outsourcing is the purchasing, from outside the organization, of IT services needed to perform business functions. According to Langfield-Smith and Smith (2003), outsourcing is *the contracting of any service or activity to a third party*. Both definitions are concerned with the inter-firm relationship, and the authors pay attention to how to deal with uncertainty and risk encompassed in outsourcing. Where Barthélemy is concerned with management expertise as a predictor of success or failure, Langfield-Smith and Smith are concerned with the design of management control systems.

Outsourcing is *a phenomenon in which a user organization (client) transfers property or decision rights over information technology infrastructure to an external (vendor) organization* (Levina & Ross, 2003). By using this definition, Levina and Ross direct their research at how vendors can deliver financial

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