IT Outsourcing – Facts & Fantasies

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Information Technology (IT) Outsourcing has become a multbillion industry worldwide in the last ten years. Almost every organisation either has outsourced its IT or is looking at the possibility. It appears however that outsourcing may not be the panacea that many organisations had been promised. Over the last few years there have been numerous reports in the media about the problems that organisations have found when they did pass control of their IT to a third party.

This paper explores the concept of IT outsourcing and identifies just what are the major problems, issues and concerns that organisations face when they outsource all or part of their IT.

Introduction

There has been a lot of hype surrounding outsourcing over the last few years as organisations try to control their IT costs, and in fact try to increase productivity throughout the organisation. There are regular reports in the media every week about the many benefits of outsourcing. Various state and federal governments have announced that they are going into wholesale outsourcing in the hopes of reducing costs and increasing quality. IT vendors continually claim that outsourcing is good for business, the IT industry and Australia generally.

But is outsourcing the panacea it is claimed to be? Or is it really the threat to their careers that many people, particularly IT staff, claim - a threat to careers, to job choices, to independence, and the ability to leverage strategic advantage for the organisation through individual uses of technology? What *are* the real facts about outsourcing?

This paper examines the IT outsourcing phenomenon, reviews the available research that has been carried out into IT outsourcing. It identifies the key problems and issues that organisations face as they contemplate whether or not to outsource any or all of their IT.

What is outsourcing?

Outsourcing is defined as “the transfer of a part or all of an organisation’s existing data processing hardware, software, communications network and system personnel to a third party.” Due (1992). This concept is not new. In the 1960s and 1970s data processing bureaus filled the role. As IT became more affordable to organisations they moved their IT in-house. In the 1980s as technology became more diverse and complex, organisations experienced rising costs, continual staff shortages and problems with managing large IT projects. The concept of facilities management came into being as a way of circumventing this.

The present surge of IT outsourcing began as a result of the sudden and rapid rises in oil prices in the US in the late 1980s, coupled with the fall in real estate prices. Organisations in Texas faced significant and unplanned increases in their costs along with pressure from the banks who were facing the prospect of a large number of bad debts from land owners whose mortgages were higher than their land was worth. To overcome this problem some organisations began to examine the possibility of selling their IT assets to provide the cash necessary to reduce their debts to the bank. They found that by “selling off” not just the assets but all of their IT including the staff they could obtain an even better deal with the vendor. This concept spread quickly during 1988 and 1989, with the main vendor, EDS growing rapidly. It was this rapid growth which lead to the critical mass that it needed to successfully take on the outsourcing of Eastman Kodak’s entire IT operation in 1989, and thus begin the IT outsourcing phenomenon.

At the same time there was another catalyst fuelling the IT outsourcing phenomenon. In the 1990s Business Process Reengineering (BPR) became the preferred methodology for organisations trying to become more cost-effective in their respecttive markets. (Similar to outsourcing this ”new” concept was practiced in the 1950s and 1960s - except then it was called Time & Motion study or Organisation & Methods). The basic concept of BPR was to “. . . use the power of modern information technology to radically design . . business processes” Hammer (1990). In adopting BPR however most organisations have selectively used its concepts focusing more on the “Obliterate” part than the “Automate” part. In addressing this latter concept many organisations have considered the problem of automating their business, or even just trying to manage their IT to be too hard. In this way BPR has fostered the idea of obliterating IT by passing the problem on to someone else.

Many organisations have used outsourcing as a universal purgative in an attempt to rid themselves of all their technological evils and woes. In many organisations wholesale outsourcing has been the norm - handing over the entire range of technology problems to someone else. Unfortunately they have found after about six to nine months that the problems haven’t gone away - but what little control they had over them certainly has. This is supported by numerous research which has shown that outsourcing has not been successful in almost all cases where the organisation has completely outsourced its IT operations (Willcocks, Fitzgerald & Lacity 1996), (Grover, Cheon & Teng, 1994), (Gordon, 1994).

The Problems with IT Outsourcing

A review of the available literature and research into IT outsourcing that has been published over the last seven years indicates a variety of problems associated with this activity. An in-depth review of the available literature was carried out and each research article or paper analysed to ascertain what problems if any were being highlighted. The problems, concerns and issues were then collated and then prioritised to identify the number of mentions and the depth of the problems being discussed.

Of the literature reviewed ten dealt specifically with IT outsourcing and its problems. The table below summarises the problems and their frequency of occurrence. The problems have been ranked in order of priority or importance according to the researchers. It is interesting to note that the top four items refer to promises made by the potential vendor which failed to materialise. Items 5 through 8 refer to concerns by the organisations regarding outsourcing, while the rest refer to actual problems identified after the outsourcing contract had been signed.

	Research Article									
Concern, Problem, Issue	**1**	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**	**10**
1. Cost Savings	†	†		†	†	†	†	†	†	†
2. Cheaper Technology	†				†	†	†			
3. Access to the Latest Technology	†				†	†	†			†
4. Access to Skilled Resources	†				†	†	†			
5. Service Quality	†	†		†	†	†			†	
6. Sharing organisation's IT knowledge with competitors	†						†		†	†
7. Loss of Control by the organisation over its IT		†		†	†		†		†	†
8. Loss of Expertise				†			†			
9. Performance of the Outsourcing vendor			†			†	†	†		†
10. Inadequate Measurement of in-house Service Levels – Service Level Agreements			†					†		†
11. Inadequate definition of in-house services			†					†		†
12. Inadequate or No Service Costing			†					†		†
13. Poor Outsourcing Contract			†					†		
13. Interpretation by Vendor of "Change of Character" clauses in Outsourcing contract			†			†				†

Table 1. Ranking and Occurrence of IT Outsourcing Problems, Concerns and Issues

Each of the problems, concerns and issues identified above is analysed in depth in this paper. It examines the key facts surrounding each item and where possible tries to identify underlying causes for them. In some cases the author's own research and experience of the last thirty years in the field of IT and IT outsourcing is provided to add support and additional background to the research findings.

The Key Problem - Cost Savings

As can be seen from the table the single most common problem with outsourcing concerns the promise of cost savings which don't materialise. Almost every outsourcer quotes significant cost savings as one of the main benefits for using their outsourcing services. One of the main reasons that Australian Federal & State Governments are so keen to outsource is that they have been told by outsourcing organisations that they can save hundreds of millions of dollars.

But as Australian federal government departments have found, (as have many other organisations) outsourcing hasn't saved them the promised millions. In fact all the research that is now available shows that very few outsourcing projects actually save money (Willcocks, Lacity & Fitzgerald 1995, 1996; Due 1992; Lacity, Hirschheim & Willcocks 1994; Benko 1992). Those that do are typically in areas where there are services which require a high capital cost for equipment to deliver the services and/or high cost of service availability, but the frequency and/or cost of service delivery is relatively low eg. weekly garbage collection, hardware maintenance & support (Hodge 1996).

This problem of non-existent cost savings however is more a symptom than a cause – it actually reflects much deeper problems in the organisation. These problems are mainly concerned with the organisation having taken for granted many of the services previously provided by it in-house staff. These services, along with other activities are not costed and are therefore hidden as far as the organisation is concerned. For example Willcocks, Lacity & Fitzgerald (1995) in their extensive survey of outsourcing found that "As well as inadequate measurement systems, there seem to be five additional root causes of such hidden costs. These are:

- Failure to fully define present IT requirements;
- Failure to define fully future requirements, or failure to create mechanisms for protecting price in the face of contingencies;
- Loopholes or ambiguities in the contract;
- Not allowing the vendor a reasonable profit; and
- Unforseen, rising, in-house contract management costs as a result of weak contracting practice."

A particular aspect of these "root causes", the "loopholes or ambiguities in the contract" was mentioned specifically in several papers. It was referred to as "change of character clauses" (problem 13 identified above). In essence this refers to the fact that if there is any change by

the organisation regarding any aspect of any IT software, hardware or service, then the outsourcer is within his rights to demand an additional fee or to vary an existing fee. Several examples of such activity are ". . . if a participant changed from one spreadsheet to another the vendor charged them an excess fee to support the new package (Lacity, Hirschheim, Willcocks 1994). In an extreme case Lacity, Hirschheim & Willcocks (1995) found ". . . one petroleum company being charged almost £500,000 in 'excess fees in their first month into a new contract.".

The fees charged by the outsourcer are another source of concern with regards the non-existence of cost savings. For example the outsourcer will quote fixed fees in the contract, but what do the fees cover ? More importantly what don't the fees cover? Several researchers indicated that organisations go through contract negotiation sessions without adequately ensuring that the services to be provided are properly defined. Lacity, Hirschheim and Willcocks (1994) found that these cost increases were due to " . . . loose contracts that merely stipulated that vendors performed the same services provided by the internal IT department. Consequently, the vendor billed for services the participants assumed were in the contract.". This loose definition post-contract led to the situation where ". . .a participant was charged $500,000 for 'extra' services.".

Another aspect of the failure to realise cost savings lies within the organisation itself. In many cases researchers found that outdated policies, poor management and in one case "politics . . .had previously prevented internal IT departments from implementing cost controls." (Lacity, Hirschheim and Willcocks 1994). The poor buying practices of many IT departments along with a lack of IT standards has contributed to a significant percentage of the rising costs of IT departments. The costs arise primarily from having to support a wide variety of hardware and software, and then requiring IT staff to spend a large amount of time working out how different items of IT equipment interface with each other. There are also significant support costs. In their study Friedberg & Yarberry (1991) found that most large data centres have an inefficiency level anywhere from 10% to 30% which could be eliminated with the proper management. In addition, Benko (1992) states that an estimated 90% of all IT departments do not have any measure of productivity.

Organisations also fail to realise that even though it may outsource much or even all of its IT, they cannot outsource many of the management functions associated with that IT or with the outsourcing contract. For example, an organisation still requires staff to manage the outsourcing vendor to ensure that he is providing the services contracted at the levels stipulated in the contract. In addition core activities such as identification and development of strategic applications, cannot be outsourced effectively. In their research Willcocks, Lacity & Fitzgerald (1995) recommend that a minimum key management capabilities need to be retained in-house. These include:

?? “Strategic thinking on IT in relation to the business;

?? Systems integration;

?? Eliciting business demand for IT;

?? Spotting business opportunities for the use of IT;

?? An ‘informed buyer’ role;

?? Contract monitoring; and

?? The ability to lever vendor relations to an advantage.”

Many of these activities are typically not taken into account when calculating the anticipated cost savings. In fact activities such as “eliciting business demand for IT” and “spotting business opportunities for the use of IT” if placed in the hands of the vendor are akin to giving him a blank cheque.

Cheaper Technology

Outsourcing vendors also promise organisations that they can reduce costs due to the fact that they can buy IT hardware and software at much lower costs because of the large volumes they buy. The fact is however that IT hardware margins are typically 4 – 7% and most organisations have found that they can enjoy the same discounts as the outsourcing vendors. This is supported by Lacity & Hirschheim who quote the IT manager of a petroleum company saying that “As long as we stay on the trailing edge of technology . . . we have an opportunity to capitalise on cheaper computing costs.”.

Outsourcing vendors are also aware of the fact that over the long term – 12 months or more – the cost of hardware will always drop, sometimes dramatically. Take for example the following graph which shows the fall in Pentium Chip prices over an 8 month period. The most dramatic was the fall in the price of the Pentium 200 chip which fell by over 70%. With this knowledge vendors typically lock organisations into 3 to 5 year contracts, sometimes with annual reviews. The prices initially are attractive but within 12 months the real price of the IT has dropped while the organisation is locked into the same prices, which can be substantially higher.

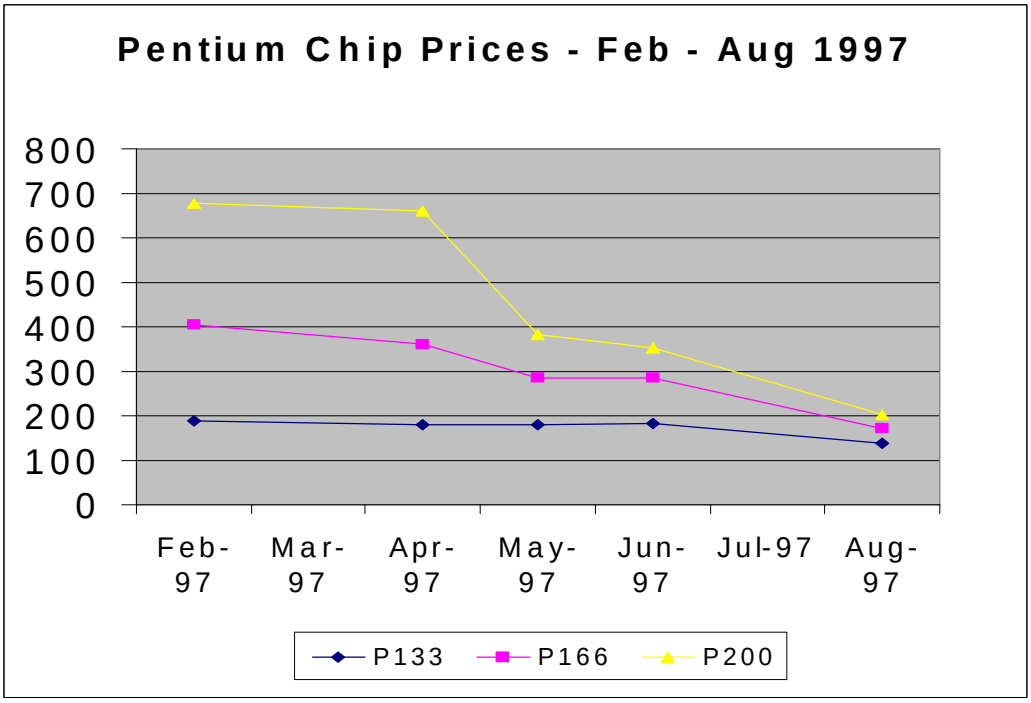

Table 2. Pentium Chip prices January – August 1997

There is an additional problem with this emphasis on economies of scale and staying with older technologies. Wagner (1994) states that it ". . . may result in the use of inappropriate technologies for a particular organisation." The disastrous fire at Bankstown City Council was a case in point. Their IT department had stayed with older IT equipment as a cost saving measure. They had disaster recovery procedures in place and practiced regular backup and restore of their data. When the fire destroyed all their IT equipment they found that there were only 2 other tape backup and restore devices in the world which could read their backup tapes – one was in Texas and one was in France. Fortunately they were able to purchase one of them and restore their data after several weeks.

The price of software is also changing in response to the outsourcing phenomenon. Software vendors typically sell software on a per customer or per site basis. As more outsourcing vendors absorb the different licenses of their clients the return to the software vendors with regards annual maintenance, as well as additional sales of software has been dropping dramatically. In response the software vendors have been introducing new forms of software pricing which circumvents the price advantage enjoyed by the outsourcing vendors. Some software houses now for example charge for their software on the basis of the size of the hardware. The bigger the hardware the higher the fee to be paid.

Many software vendors also do not allow the software licence to be transferred, which means that if the outsourcing vendor takes over all the organisation's IT assets new licences must be purchased by the outsourcer and therefore paid by the organisation. In effect the organisation pays twice for the same software. Other software houses will allow the licence to

be transferred, but will have to pay a transfer fee, which can be up to $500,000 or more in the case of large mainframe software.

Access to the latest technology

Many organisations feel that by outsourcing their IT they will instantly get access to the latest technology. This perception has been found to be very common as Lacity, Willcocks and Hirschheim (1994) found in their research: “Some participants were disappointed that outsourcing did not automatically provide access to new technologies”. The main problem with this requirement is that it is almost always mutually exclusive of one of the main reasons for outsourcing – cost savings. Just as the organisations makes significant investments in technology so too do the outsourcing vendors. If they then can lock organisations into using that technology for 3, 5 or even 7 years, the their investment can be reaped many times over.

If the organisation does want the latest technology it must realise that the latest technology will always cost considerably more than older technology. Similar to the purchasing behaviour described above, the organisation could just as easily purchase the new technology for the same discounts that the outsourcing vendor enjoys.

This misconception regarding the outsourcer’s ability to magically produce the latest technology when the organisation’s staff supposedly couldn’t, can also lead to the organisation being locked in to the wrong “latest technology”. As Due (1992) pointed out “The appearance of industry-specific vendors could result in the spread of systems mediocrity throughout the industry because of the lack of new ideas and product differentiation. “. An important aspect of this is that when the organisation effectively hands over control of this function to the outsourcer, he then becomes subject to the whims of the outsourcer as to what areas of new technology he will advance to in the future. Certainly if the organisation tries to dictate the new technology the outsourcer can immediately invoke the “change of character” clauses that are prevalent in outsourcer’s contracts.

One question that seems to be forgotten in this is whether or not the organisation really needs to have access to the latest technology? Do all their staff really need the latest hardware, software, multimedia, etc? Many IT Managers agree that 90% of their organisational functions don’t require a Pentium 200 MMX with 32Mb of Memory 2.1Gb of HDD and a 20 speed CD-ROM. The main functions that occur in organisations today are word processing, spreadsheet capabilities, and staff access to corporate information as needed.

This attitude is reflected in the PC purchasing trends during the second half of 1997 and into the first quarter of 1998. As demand continues to exceed supply the price of the average PC continues to fall and the price of components and peripherals falls with them. The rule of thumb used to be that you could depreciate PCs over a three to five year timeframe. Today

that period is now 2 years, to 3 years at a maximum. In effect a one year old PC is only worth today 50% of what the organisation paid for it.

Access to Skilled Resources

Another of the significant concerns that organisations express is the lack of suitable skilled resources. Organisations find that they cannot hire the necessary people they need and have to either pay very high salaries for employees or high rates for contractors. Organisations look to outsourcers who say they have all the skilled resources the organisation needs.

But that doesn't mean that the outsourcer has them either. The truth is that behind the scenes there is a large sub-industry between the outsourcers and contracting agencies. The outsourcers don't want it to be publicly known that they don't really have all the inhouse skills and resources that they proclaim to have. They can't advertise so they use contracting agencies as intermediaries. This means that there are two sets of overheads for the contracted person - the contracting agency and the outsourcer, which then raises other problems. For example one large outsourcer who won several significant government outsourcing tenders in late 1997 and early 1998 began looking for top level project managers in this way. The rate for these types of people was quoted at a maximum of $750 per day, while the standard rate was between $1,200 and $1500 per day. At the time this paper was written the results of the personnel search were not known but the result of this will no doubt be contractors who are be prepared to work for this lower rate, and most likely not have the necessary and sufficient skills to carry out the roles effectively.

One other aspect of outsourcing with regards staffing is that the vendor usually undertakes to assume responsibility of all the organisation's IT staff. This certainly solves a major "problem" for the organisation, but many organisations have found when they outsourced to take advantage of the outsourcer's skilled staff " . . . only to find they are supported by their previous staff and additional vendor expertise is expensive." Lacity & Hirschheim (1993).

Many organisations try to look after their staff in an outsourcing situation. They try to include provisos that the outsourcer will look after the organisation's staff etc. They try to alleviate the staff's concern about their future role as the organisation transitions from in-house to outsourced operations. Research has shown however that staff are worried - and with good cause. A recent report by the Australian Industry Commission (1995) into 17 cases of outsourcing in Australia found that just over 50% of the staff originally involved in providing the services were actually retained by the outsourcer. Where the services were to be provided by the outsourcer 29% of staff were made redundant, 4% were terminated and a further 8% reassigned to other areas. Anecdotal evidence also suggests that up to two-thirds of staff who do move to an outsourcer are gone within twelve months.

In many outsourcing projects the human factor is not taken into account - except as an after-thought. They are treated with even less attention and care than the technology that is also

being outsourced, possibly because there is at least a value on the books for the technology. Staff typically join an organisation because of its culture. They like to be in that area of business, whether it be banking, insurance, public service, primary industry, police or whatever. They stay there for 5, 10, 20 years and longer because of this. To be suddenly told by the organisation for whom they have devoted many years of effort and loyalty that they are effectively no longer wanted comes as an enormous shock.

As far as the outsourcer is concerned once the staff are transferred to his domain they are his to do with as he pleases. The specialist skills and knowledge that those staff gained about the organisation over many years now belong to the outsourcer. Any competitive advantage that the organisation had in respect of that knowledge has effectively been passed to the outsourcer and the outsourcer takes full advantage of it. Many organisations have found that although they assumed they would still have essentially the same staff post-outsourcing in fact the outsourcer in many situations has taken the best talent to other potential outsourcing organisations to demonstrate their depth and breadth of talent. As one IS manager quoted to Lacity & Hirschheim (1993) “You pay for them to learn your business, they move those people to court other companies in your industry. They transfer skills to get new business: now the learning curve is yours to pay for again.”.

Service Quality

One of the attractions to using outsourcing vendors for the supply of IT services is that they can provide them at a far higher quality than inhouse staff. These statements are usually made by the vendors in the same sentences as those about skilled staff, lower costs, etc. Unfortunately the research over the last seven years has shown this not to be true, and thus to be a significant concern to organisations who thought they would obtain an increase in service levels by outsourcing. In the literature surveyed 6 of the ten research articles specifically mentioned the drop in service quality as a concern with outsourcing. In particular Lacity Hirschheim and Willcocks (1994) found that “Companies that engaged in total outsourcing often suffered service degradation and, in some cases, increased costs. Indeed some companies have threatened to sue their outsourcing vendors for non-performance.”.

The Gartner Group survey in Europe (1996) also disputes the claim by vendors of higher quality. This survey found that 80% of organisations who had outsourced their IT tried to renegotiate their contracts within twelve months. Three main reasons were given: quality, price, and changing ideas about required services. The study by Graeme Hodge (1996) into 129 research papers on outsourcing also disputes the claim that outsourcing provides high quality. In fact Hodge’s study found that organisations have achieved similar quality improvements by in-sourcing their operations.

There is also an interesting anomaly - if the outsourcer can save all the money they promise, provide higher quality using the organisation’s staff when they move over to the outsourcer

and make an estimated 20 - 30% profit, then why can't the organisation do the same and save all the hassle. Certainly the Defence Computing Bureau demonstrated its ability to do so when they won the outsourcing bid against all the outsourcers in 1997. Naturally this has caused a large amount of angst amongst the outsourcers who are still protesting the decision saying that it brings uncertainty into the industry.

Sharing Organisation's IT Knowledge with Competitors

Organisations have typically built up a wealth of knowledge over many years regarding the use of IT in their organisations. It includes not only the broad technical knowledge about all facets of IT such as hardware, software, networks, etc. but also the specific knowledge about the unique ways in which IT is used in the organisation. Some organisations have very sophisticated IT operations, using IT as a competitive weapon. In the 1980s and early 1990s certain US airlines were using their computerised reservations systems to such great competitive advantage that the US Anti-Trust authorities forced the airlines to open their systems so that other airlines could also use them.

On the other hand many organisations consider that IT is not a core competence – that it can and should be carried out by those who are the experts, and leave the organisation to get on with those activities that it knows best. Unfortunately many organisations consider IT to be essentially one word – they do not consider the *Information* and the *Technology* separately.

Certainly the technology may not be core, all organisations use similar hardware and software, and operate over similar local and wide area networks. But that's where the similarity ends. The uniqueness lies in how that technology is used and the specific corporate information the organisation processes and stores in that technology. These two area are where the advanced organisation can gain significant and sustainable competitive advantage. Its also these two areas over which the outsourcing vendor tries to gain control. Once that control has been won the vendor can then sell that capability to other organisations who have a similar requirement.

Loss of Control by the Organisation over its IT

Many organisations expressed concern over losing control of their IT once it was outsourced to the vendor. Similar to the concerns expressed above they felt that having spent many years and millions of dollars building up that expertise, they would no longer have control over its future focus and direction. One area of concern was that while the IT was in-house and the staff were employees or in some cases individual contractors, IT management were able to control the day to day duties of and to direct their staff in the formulation of specific IT related projects. Any additional tasks that may be required could be requested knowing that they would be carried out with a reasonable level of certainty.

This would not be the case however once the functions and staff were outsourced. Any request for work would be firstly reviewed by the outsourcer in terms of what he had contracted to provide, and at what cost. The organisation could no longer necessarily dictate the way in which the work was to be carried out nor who was to carry it out unless the contract expressly allowed – a very rare occurrence.

Another aspect of this is that once the ownership of IT is transferred to the outsourcer, unless the contract expressly stipulates, he is relatively free to do with it as he sees fit provided he continues to provide the required services. In some cases this has meant the IT is transferred to the vendor's premises which can be several hundred kilometres away, or the hardware is sold and the applications are transferred to the vendor's own hardware to be run in conjunction with other organisations' applications.

This also brings into the discussion the question of security. The unique information that each organisation has is now potentially available to other organisations as well as the vendor's staff who may be working with other organisations. Although assurances may be given as to the confidentiality and security of the organisation's IT, in practice it is much harder to implement.

Loss of Expertise

Only two research articles mentioned loss of expertise as a concern in an outsourcing situation. This is most likely due to the fact that most organisations do not have a sufficient understanding of the large body of knowledge their IT staff have, and the value of that expertise. What was found by researchers however was that once the organisation had outsourced its functions to the vendor, in many cases the staff that had transferred to the vendor were no longer available to the organisation. In addition whereas previously certain functions such as password reset and security access were carried out within hours whilst in-house, they now took many days once outsourced.

What is obviously not appreciated by many organisational managers who consider outsourcing is the enormous amount of knowledge about organisational processes built up by IT staff over many years. As Wagner (1994) found in her research "A new opportunity perceived as urgent by the organization may not be solved (or even worked on) in a timely fashion. Even though there are now many specialists, few, if any, of them may have expertise in the organization's particular industry.". It is this knowledge that disappears and can take many years to rebuild if it is outsourced.

Performance of the Outsourcing Vendor

A concern expressed by organisations who had outsourced was in the performance of the outsourcing vendor. This was noted as a concern or problem in half of the research articles reviewed. In defence of the outsourcing vendors, it is not all their fault that they have not been able to meet expected service levels for their customers. In many cases it is the fault of the organisations who did not have adequate, or in some cases, any way of measuring service levels when the services were being provided in-house. According to Benko (1992) " . . . an estimated 90% of all data processing operations do not employ any measures of productivity.". Although this finding was in the early 1990s, it appears that IT departments have not learnt a great deal during over the years since. Recent research indicates that many IT managers don't know what services their department provides, how much they cost, nor how those services are provided. One of the four main areas of weakness by organisations with regards their IT operations cited by Willcocks, Lacity and Fitzgerald (1995) in their research was a "failure to establish adequate measurement of the pre-existing in-house performance". Although there may well be some justification for berating the outsourcing vendor it is difficult to blame him for non-performance when the organisation did not have a pre-outsourcing benchmark against which to compare them.

Inadequate Measurement of In-House Service levels – Service Level Agreements

Service Level Agreements (SLA) are a necessary tool for establishing and measuring IT service performance for the organisation. Yet there appears to be a great deal of misunderstanding about them, not only within organisations but even with the vendors themselves. A Service Level Agreement formalises the commitment of a service provider to provide services of a stated quality at a stated level of response to the customers who will be paying for the services, and the consumers who will be the recipient of services detailed within the agreement. By developing and negotiating an SLA with its customers, the IT department can effectively plan to provide a range of services which covers the core services required by corporate management and the optional ones which may be needed periodically by individual customers.

It appears from the research that many organisations have tried to cover their inadequacies in this area by passing the blame on to the outsourcing vendor. The previous concern about Vendor Performance is a reflection of this. After all it was he who said he could provide all the services previously provided by the in-house staff, and at the same level. He must have known therefore what services, service levels, etc were being provided. Unfortunately for the organisations, they assumed that the vendor was working in the organisation's interest and not their own.

The concept of "vendor partnering" was prevalent in the research literature. This concept is one actively promoted by the vendors (eg "we're in this together"). Equally prevalent was the

comment by researchers that it was a false assumption. The organisation typically allows the vendor to draw up the contract, only looking at the superficial benefits (cost savings, reduction of headaches, access to new technology, etc.). No monitoring systems are put in place, after all "we are partners – we should be able to trust each other". Its only after the contract is signed and the honeymoon period over that the realisation hits home. As Willcocks, Lacity & Fitzgerald (1995) reported in their research "We also found parties all too frequently relying on 'partnering' notions to offset any difficulties arsing from loose contracting. These rarely provided a sufficient base in themselves from which to run effective outsourcing arrangements.".

Inadequate Definition of In-House Services

Inadequate or No Service Costing

Although these problems were identified in only 3 research articles they were heavily emphasised as major problems in outsourcing. The most probable reason for this is that the underlying reasons for these problems is due to inadequate management controls and disciplines in the IT department. More than likely this is why outsourcing was considered – a way of overcoming deficiencies such as these. Lacity, Willcocks, Hirschheim and Fitzgerald in several of their articles identified areas where the IT department had not gotten its own house in order before venturing anywhere near an outsourcing vendor. These included the failure to establish Service Level Agreements, fully define and cost all IT services and the inability to monitor performance of the IT department against the service levels established in the SLA.

Poor Outsourcing Contract

Change of Character Clauses

These two areas of concern were only mentioned in 3 of the research articles reviewed, yet the financial affect they can have on the organisation concerned is significant. In one case reported in the research one organisation found that due to a "change of character" in the IT operations they were faced with an additional monthly bill of over $500,000 (Willcocks, Lacity & Fitzgerald 1995). In another case the organisation found that when it switched from one type of spreadsheet to another, the vendor invoked the "change of character" clause to charge extra fees, even though the level of service would not change (the other spreadsheet was to be dropped from the organisation).

With regards poor outsourcing contracts organisations are in many cases at the mercy of the outsourcing vendors whose job it is to ensure they obtain the maximum return for their shareholders. With one vendor for example the largest single item of expense is not the technology or the people, but the legal costs. Organisations will typically be negotiating an

outsourcing contract for the first time. Even the organisation's legal representatives will most likely not have the same level of expertise in this area as the vendor's legal counsel. As Willcocks, Lacity & Fitzgerald (1995) found in their research "In practice it is all too easy for all parties to a contract to agree broadly on what is required from a vendor.". The assumption is in many cases that the vendor will do the right thing by the organisation. Practice unfortunately has shown the opposite. Several researchers reported cases where the vendor interpreted the terms of the contract strictly, and always in his favour.

The poor contract aspect also had a flow-on effect in terms of vendor performance. Whereas it was a simple job to get a particular service carried out whilst IT was in-house now it required examination of the contract by the vendor, does he have to provide the service, if so can he charge extra, if not how can he get around the contract so he can? All this causes delays in what the organisation is trying to achieve – cost-effective use of IT. In some cases the organisation gives up in despair (Glass 1994) and becomes even more frustrated with IT than when it was in-house. At least then the organisation had some measure of control over its IT.

The "Unintended" Consequences of Outsourcing

In addition to the problems, concerns and issues identified in the research above, there are also unintended consequences of outsourcing that are not reported widely but have been observed by the author. On radio recently it was stated that due to the Australian Federal Government's stated approach to outsourcing, the biggest growth industry in Canberra today was removaling. Small businesses, locked out of government contracts by the outsourcers, are shutting down. People previously employed in government departments are moving out of Canberra trying to find work.

The evidence from numerous studies including the Australian Industry Commission study (1996) shows that there is a significant (at least one-third) reduction in employment as a result of outsourcing. In addition many of these jobs are typically migrated from the organisation's premises to the outsourcer's premises, which may be several hundred kilometres away or interstate. To force staff to move in this manner is onerous to say the least.

Another important aspect in this area is that almost all the outsourcers are foreign owned multi-nationals - their profits go overseas. If the demand for the services is really there why put a foreign-owned multinational in between the service provider and the organisation - all it does is add an extra layer of management, greater potential for problems to arise and additional overheads (typically 20 - 30% of the costs and greater if there is more than one contracting agency involved).

Conclusion

There are numerous problems, concerns and issues that organisations face when they consider the possibilities of outsourcing their IT to a third party. They could be in the form of claims made by the outsourcing vendor which don't eventuate, they could be concerns over the lessening of competitive advantage, control or expertise if their IT is outsourced, or it could be concerned with the vendor, his performance or interpretation of the contract.

The biggest single concern of all organisations however is in the area of cost savings – also the single most common reason why organisations look at outsourcing. The research has shown that there is no one main reason why organisations fail to save money by outsourcing – there are many. They range from unrealistic expectations about what the outsourcing vendor will provide, through a poor understanding of exactly what it is that the IT department provides in the way of services to the rest of the organisation, to inadequate in-house practices, controls and disciplines that management were either unaware of or were hoping to alleviate by outsourcing.

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