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COLLEGE OF MANAGEMENT AND TECHNOLOGY

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2009

ABSTRACT

Using a Framework of Responsible Risk Management Strategies to  
Mitigate Risks Inherited in Outsourcing

by

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B.S. California State University, 1986  
M.B.A. National University, 1988

Dissertation Submitted in Partial Fulfillment  
of the Requirements for the Degree of  
Doctor of Philosophy  
Applied Management and Decision Sciences

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## ABSTRACT

While outsourcing is widely used by U.S. organizations, the practice is laden with risks related to contracts, process management and loss of confidential information. If left unmitigated, these risks expose outsourcing organizations to unnecessary resource waste and knowledge and expertise loss, which can reduce competitiveness and profitability. Based on an outsourcing value proposition (OVP) theoretical framework, the research focus of the explanatory descriptive study was to define how frequently 20 risk-mitigation (RM) best practices (OVP-BP) defined by researchers in this field were employed by U.S. companies using either domestic or off-shore outsourcing. OVP-BP use data from surveys completed by 37 senior risk management officers were explored via descriptive and time series analyses. Results revealed that OVP-BP related to contract RM were more commonly employed than OVP-BP addressing process management RM. No consistent trends over time were observed for domestic OVP-BP, whereas OVP-BP increased over time for overseas outsourcing, but still remained well below domestic OVP-BP deployment. These results suggest that public policy interventions are needed to enforce the use of best practices that can reduce wasted knowledge and expertise. From a social implication perspective, knowledge of the specific gaps in practice identified in this study can be used to remedy the current weaknesses in outsourcing risk management practices and contribute to increased competitiveness and profitability among U.S. organizations.



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## CHAPTER 1:

### INTRODUCTION TO THE STUDY

To meet the contingencies of a globally competitive marketplace, organizations must constantly improve their abilities to produce goods and services at reduced prices, increase the speed-to-market or speed-of-delivery of products and services respectively, and offer the highest quality products and services at a competitive price. This requires organizations to continuously evaluate and improve their internal processes (Dean, 2006). According to Bhagwati (2004), during the last 2 decades, organizations have tried various restructuring business models such as reengineering, downsizing, and strategic sourcing to achieve these objectives.

Reengineering methods allow organizations to optimize their operations by streamlining the organizations' processes and reducing waste of resources (Rossetti, 2005). Along with streamlined processes, organizations have used various downsizing methods to further reduce operating costs and increase their earnings and stock prices (Cascio, 2005). In addition, and especially since 2000, organizations have started to achieve parts of their operations goals by hiring services of specialized third-

party sellers or providers (Lee, 2004), a practice called outsourcing. Outsourcing is one strategy organizations can use to obtain services from other organizations more economically than can be obtained from their own facilities.

Obtaining outsourcing services from organizations that have skilled resources improves the effectiveness and efficiency of the organizations other internal processes (Sheng, 2006). Acquisition of skilled resources at lower costs allows organizations to improve the organization's overall performance (Farrell, 2006) and reduces their overall cost of operations (Weiss, 2007). Cascio (2006) stated that when organizations in high-wage economies use providers in low-wage countries, it further reduces the cost of outsourcing. Outsourcing to other countries is called offshore-outsourcing and sometimes off-shoring.

When organizations' support activities, such as information technology (IT), human resources (HR), legal, and financial services are outsourced the organizations can better concentrate on their core business activities. According to Willcocks (2006), organizations' first priority should be to concentrate on their core activities or value-adding activities rather than support activities.

Several research-based studies have indicated that outsourcing is a very good method of obtaining support functions, and organizations should pursue this method to become competitive. According to Cascio (2005), when non-core activities of an organization are outsourced to specialized providers, an organization's ability to perform its own core or niche activities can be greatly enhanced. Most research-based studies have indicated that using off-shoring greatly enhances an organization's ability to obtain these support functions at reduced cost.

Despite these claimed benefits, outsourcing organizations have failed to achieve their intended outsourcing outcomes or goals. This is because outsourcing introduces various risks for an organization. First, outsourcing requires an organization to disintegrate its vertically integrated internal processes and horizontally integrate other processes external to the organization (Willcocks, 2006). Second, outsourcing creates a dependency on others to achieve one's own objectives (Sheng, 2006). Third, when an organization's processes and activities are performed by other organizations, control over some of the organization's critical decision-making is lost (Barthelemy, 2006). Fourth, an organization loses internal

knowledge and expertise of the outsourced processes and activities (Willcocks, 2006). Fifth, cultural, linguistic, legal, political, and economic differences, especially in offshore outsourcing, leaves outsourcing organizations vulnerable to incomplete contracts, imperfect information, incoherent business processes, and other extrinsic risks such as loss over control of service quality and confidentiality and privacy of information (Kakabadse, 2003). These risk factors mentioned are the causes of various outsourcing risks that have prevented organizations from gaining the benefits from outsourcing and have led to unnecessary resource waste. Outsourcing risks have caused other negative outcomes for outsourcing companies such as failure to operate as a coherent, effective, and efficient organization.

Failure to control these outsourcing risks can prevent outsourcing organizations from providing their core value functions and reduce their competitiveness. Loss of profit, reduced overall quality of products and services, and ineffective and inefficient processes are commonly experienced losses for organizations that use offshore outsourcing (Barthelemy, 2003). These losses have caused loss of valuable resources and reduced competitiveness of

U.S. businesses (Willcocks, 2006). Modarress (2007) indicated that uncontrolled outsourcing risks can contribute to unnecessary business interruptions that can lead to customer dissatisfaction. Loss of competitiveness whether caused by inefficient use of scarce resources or dissatisfied customers can be counterproductive in a highly competitive global marketplace.

In addition to loss of competitiveness for the outsourcing companies, when organizations use offshore-outsourcing this exposes countries to labor market shifts and job dislocation (Farrell, 2006). Offshore-outsourcing relocates jobs that were once performed in the outsourcing organization's country to another nation (Harrison, 2006). According to Harrison, despite claims that outsourcing countries create other jobs in place of outsourced jobs, research has validated that outsourcing has led to a net job loss for the U.S. labor market. He demonstrated through various data analysis that outsourcing creates permanent job relocation.

According to Chopra (2004), operational alliances such as outsourcing relationships are important to become competitive, but research was needed to demonstrate the strategies that can effectively control the inherited

outsourcing risks. This research study was an attempt to (a) determine what theoretically and research validated strategies were needed to effectively control these inherited problems in outsourcing, (b) explore to what extent outsourcing organizations were using these strategies, and (c) explain the exposures that were most and least controlled by U.S. organizations that use outsourcing and offshore-outsourcing.

#### Problem Statement

The problem this study addresses is that while the use of outsourcing by U.S. organizations has introduced various risks that expose these organizations and the U.S. economy to unnecessary resource waste, it is not clear whether organizations use the necessary strategies that effectively reduce the negative exposures of these risks. As indicated by Chopra (2004) operational alliance such as outsourcing is required to become competitive, but research was required to determine the strategies or best practices (BP) organizations need to mitigate the risks in outsourcing.

Research based studies since 2004 have demonstrated that U.S. organizations that outsource have experienced resource waste, faced with uncertainties in terms of their ability to obtain value from outsourcing, and vulnerable to



future economic losses. Some studies suggested that a means to reduce problems such as economic losses is to use responsible risk management strategies. Barthelemey (2004) indicated that exposures of unmitigated risks can take time to manifest and the failure to recognize risks and take mitigating steps in a timely manner increases the likelihood that these organizations will incur losses. In another study, Weiss (2007) confirmed that outsourcing organizations that failed to use risk management strategies increased the costs of operations significantly higher than their pre-outsourcing levels. In yet another report, Modarress (2007) indicated that outsourcing organizations that do not mitigate risks inherited in outsourcing suffer customer dissatisfaction, unnecessary business interruptions, and resource waste in the end.

The problem with wasting resource is that it exposes outsourcing organizations to competitive disadvantages and threatens the success of industries and even the ability of a nation to become an effective player in a globally charged economy. In 2002, the U.S. Congress also passed a mandate for organizations to reduce risks in order to improve the value to the organizations' shareholders, and prevent unnecessary resource waste. This problem is

relevant and needs to be studied because (a) the U.S. Congress passed a mandate in 2002 for organizations to reduce the risks they inherit, (b) U.S. economy suffers when U.S. organizations fail to use irresponsible risk management practices, and (c) because the problems inherited in outsourcing can be prevented by responsible risk management strategies.

#### Background of the Problem

Research-based findings during the past ten years demonstrated that outsourcing strategies of many U.S. organizations lack concern for long-term risks in terms of shareholder's values, business continuity, or the long-term economic consequences. Rossetti (2005) demonstrated that one common problem with organizations' outsourcing strategy is the use of low-bid or low-cost method to select outsourcing partners. Rossetti also mentioned that while outsourcing can help organizations improve their internal processes, instead, most U.S. companies engage in outsourcing practices to improve financial ratios. Bielski (2006) indicated that instead of using outsourcing to form a meaningful sourcing alliance, U.S. organizations use outsourcing as a quick fix for long-standing problems. These studies indicated that the problem with these

strategies is that in the end these organizations inherit various risks.

Cost-driven strategies or low-bid methods have led to unsuccessful outsourcing relationships (Rossetti, 2005). According to Rossetti, in an effort to make up for their own errors in estimating cost of providing outsource services, and due to a continuous need to further reduce their cost of operations, outsourcing buyers use contractual pressures to demand low costs of operations from suppliers. Weiss (2007) further suggested that the buyers demands for low cost bids increases pressures for outsourcing suppliers especially offshore-outsourcing suppliers to engage in low-cost bidding practice just to win outsourcing businesses. In the end, however, the vendors are not able to offer the services at the low costs specified in the bid. According to Rossetti (2005), when faced with their own investor demands to improve shareholder values these vendor organizations have to take various cost-cutting steps, such as hiring of unskilled resources, and buying lower quality materials. These low-cost bid methods and practices in the end lead to poor quality of services, increased risk of unsatisfied

customers, and reduced profits for the outsourcing organization.

The use of outsourcing simply to inflate a financial indicator or performance matrix is another example of a use of a strategy without concern for long-term risks. The study by Rossetti (2005) demonstrated that management in U.S. based companies use outsourcing as a means to improve many of the financial metrics that stock analysts use as a performance indicator. Reducing return on assets (ROA) is an example of this practice. When organizations outsource their entire IT department, this reduces their investments in various hardware, software, furniture, and buildings. In the short run, this practice boosts the organization's performance matrix. However, in the end inherits risks such as loss of core-competencies in the area of outsourced services makes it difficult to evaluate vendor performances and changing needs of the organizations.

Organizations also used outsourcing as a strategy to quickly fix long-standing problems without understanding the root causes of problems (Barthlemey, 2003). Some organizations outsource out-of-control or difficult-to-manage processes and either fail to calculate or do not have the ability to calculate the outsource exposures to

the other processes of the organization (Willcocks, 2006). When organizations outsource processes that they do not understand, it becomes difficult for them to determine what the outsource vendor should be charging and what they should be receiving in terms of quantity and quality of services.

Kakabadse (2003) mentioned that when organizations fail to maintain any control or in-house capability and knowledge, they become incapable of managing the outsourcing relationships in terms of planned transitions to alternative and more profitable sources. In his study, Kakabadse indicated that failure to mitigate the inherited risks in outsourcing would lead to knowledge, industry expertise, and U.S. job losses. In a later study, Harrison (2006) reported that since U.S. organizations started using outsourcing, the U.S. Labor Bureau has reported a net loss of jobs in the United States of America. Because of these unmitigated risks, outsourcing U.S. organizations expose themselves and the U.S. economy to loss of competitiveness.

According to Barthelemy (2003), during the first decade of outsourcing, organizations made the decision to outsource based on short-term gains and with little concern for risks and risk management. Friedman (2006) suggested

that given the current knowledge about the negative consequences of using short-term outsourcing strategies, organizations have no choice but to use responsible risk management strategies to mitigate those risks inherited as a result. In a case study of the application of risk management strategies at Dupont Corporation, Willcocks (2006) demonstrated that the use of responsible risk management strategies were the only means to reduce risks inherited by outsourcing organizations. According to Liebesman (2008), the U.S. Congress created a mandate called Sarbanes Oxley Act (SOX) in 2002 that requires all U.S. companies, including nonprofit organizations, to understand and mitigate risks with strategies that can prevent resource waste and prevent intentional and unintentional errors within an organization.

#### Research Objectives and the Research Questions

One research objective for the study was to determine the extent to which U.S. organizations used the necessary risk management strategies to reduce the outsourcing risks inherited from their outsourcing practices. The other research objective was to determine the extent to which organizations that used offshore-outsourcing and for longer than five years used the risk management strategies.

### *Research Questions and Hypotheses*

The research questions that guided this study were (a) Which risk management strategies or BP were being used most and least by outsourcing organizations, and (b) Which risk management strategies or BP were most and least used by organizations that used offshore-outsourcing and for longer than five years? The answer to these research questions might explain whether the current strategies used by outsourcing organizations can prevent future economic losses.

The following null hypotheses were tested.

Null Hypothesis 1 -  $H_{01}$ : The framework of risk management strategies used by outsourcing companies can prevent future economic losses.

Null Hypothesis 2 -  $H_{02}$ : The framework of risk management strategies used by organizations that use offshore-outsourcing and for longer than five years can prevent future economic losses.

A two-step process was used to verify or reject the null hypotheses. The first step was to determine what constituted a baseline or a framework of risk management strategies needed to prevent the outsourcing risks

inherited in outsourcing. Theory and research-based studies were used in this step to ensure all known outsourcing risks were included in this study. During the second step, an exploratory study using descriptive statistical analysis was used to explain whether the risk management strategies used by U.S. organizations that (a) outsourced and (b) used offshore-outsourcing for over five years could prevent unnecessary resource waste.

#### Purpose of the Study

The purpose of the study was to determine whether outsourcing organizations used responsible risk management strategies to prevent unnecessary resource waste that expose the U.S. economy to competitive disadvantage. According to Enlow (2006), despite the fact that outsourcing is laden with risks, the use of responsible risk management strategies can reduce the impact of these risks and allow organizations to meet their outsourcing objectives and prevent resource wastes. Dean (2006) indicated that carefully selected risk management strategies or BP can help organizations achieve their outsourcing goals and ensure that resource waste are prevented.



Given the widespread use of outsourcing and the magnitude of financial losses already experienced by outsourcing organizations, it was important to conduct this study. Finding the answers to the two research questions in this study is a means to achieve the purpose of the study.

#### Significance of the Study

Outsourcing has been reported as, "a business imperative to succeed in a global marketplace" (Tompkins 2005, p. 9), "an inevitable next step to globalization" (Farrell, 2006, p. 32), and an opportunity for organizations to create value (Dean, 2006). Researchers and management experts including Barthelemy (2006), Casio (2006), Hart, (2005), Kakabadse and Kakabadse (2002), Lei (2006), Sheng (2006), and Willcocks (2006) have concluded that an organization's ability to compete in a today's global marketplace will be determined by its ability to use outsourcing as a business model to become effective, efficient, and thereby improve performance.

Outsourcing practices are growing at a rapid rate. Since the 1990s, 50% of U.S. manufacturing jobs have been sent out of the country (Harrison, 2006). According to Barthelemy (2003), various studies indicated that 58% of all IT services of U.S. organizations will be outsourced by

2010. Studies by Gartner group (2002) suggested that non-IT related service outsourcing will double between 2000 and 2005 and will grow exponentially during the remaining of the decade. Other studies by Aron (2005) and Weiss (2007) indicated that organizations continue to pursue outsourcing at a rate higher than even what outsourcing providers were anticipating. These studies indicated that during the first half of 2007, outsourcing service providers were experiencing an increase in demand for all types of outsourcing services including IT, business processes, human resources, legal, accounting, manufacturing, and even very critical research and development services.

According to Modaressi (2007), because the demand for outsourcing is higher than the supply, not changing irresponsible outsourcing practices will consequently increase the impact of failed outsourcing projects. If outsourcing failures are not controlled, he suggested that nations can become vulnerable to significant exposures such as reduced competitiveness, loss of wealth, and more direly, inability to support the welfare of its citizens. Given the exponential growth, potential imbalance in supply and demand trend, and the magnitude of exposures, it becomes an imperative to determine if organizations are

using responsible strategies to control outsourcing failures.

#### Evolution of Theoretical Framework

As a business restructuring initiative, organizations outsource because of a make-or-buy strategy that organizations have to adopt. The Coase theory provides the basis of understanding the make-or-buy justifications, benefits, and associated risks. Two extensions of this theory, the transaction cost theory and the resource dependency theory, have established the framework for understanding the risks inherent in a contract-based relationship. The dynamic risk management theory and the control principles have further established the framework for applying risk management strategies in order to control the exposures of the risks inherited when organizations form contract-based relationships.

According to the Coase theory, an organization reasons their make-or-buy decisions based on the relative costs associated with performing the activities internally or going to the market for better alternatives. When organizations decide to go to the market to buy their activities, this creates a contract-based relationship (Coase, 1937). According to Coase, contract-based

relationships are affected by imperfect information risks and market uncertainties and in order to achieve their goals, organizations should understand, monitor and reduce these risks.

According to the transaction cost theory (TCE) market uncertainties and lack of perfect information leads to the risk of less than optimal buying decisions and can increase the transaction costs related to the purchased good or services (Williamson, 1999). The resource dependency theory (RDT) informed that when organizations depend on other organizations for their resources, they lose full control over their activities and may not be able to control their own destiny (Pfeffer, 1978). These two theories served as the framework for describing the risks inherited when organizations form contract-based relationships to achieve their own goals and objectives.

Aulack (1996), explained that not having control over all activities can lead to delays in receiving inputs to an organization's processes and even reduce the quality of their products and services. According to Aulack, these problems can lead to business interruptions and potential shutdowns. The control management principles developed by Aulack indicated that these risks can be controlled by

establishing expectations, monitoring changes, and taking actions to correct these problems. According to Fehle (2005) because market conditions are constantly changing, organizations should manage risks dynamically or as new changes become apparent. The control management principle provides the formula for monitoring, governing, and managing a relationship, whereas a dynamic risk management theory demonstrates the need for buyers to be-aware of changing conditions.

The theories and principles discussed in this section provided the various lenses through which a study should examine concepts related to contract-based relationship risks and risk management strategies. The RDT and the TCE theories demonstrated inherent risks in a contract-based relationship. The dynamic risk management and the control principles suggested the risk management strategies needed to reduce the risks and the negative exposures of the risks.

#### Scope of the Study

The study concentrated on contract-based service outsourcing relationships created between two organizations by a written contract. The types of services that were included in the study including business process

outsourcing, IT services outsourcing, call center outsourcing, HR and other legal outsourcing, financial services outsourcing, and other services outsourcing. Outsourcing relationships formed between two U.S. companies or a U.S. company and a vendor in a foreign country or offshore outsourcing were both included in this study.

The distinction between a contract-based outsourcing and other forms of outsourcing is important to note. There are two other ways to form an outsourcing. First, organizations can run their entire operations, or relocate parts of their business operations in a foreign country (Farrell, 2006). Second, a buyer can relocate their outsourced services closer to the outsource provider or vis-à-vis (Bhagwati, 2004). Those forms of outsourcing can have similar risk factors but will not be the focus of this study.

In short, the scope of this study was limited to studying the outsourcing risks related to what Bhagwati (2004) explained as long-distance contract based relationship or alliances formed with another organization to obtain an organization's own activities and services.

### Limitations

The most significant limitation of this study was that only currently known and applicable outsourcing risks and risk management strategies were studied. The nature of outsourcing practice is always changing and evolving. The strategies that reduce the outsourcing risks today may not be applicable to mitigate the new outsourcing risks of tomorrow. Outsourcing as a practice emerged a decade ago as a business tool to reduce an organization's operation cost. As the practice matured, outsourcing became a business tool to meet other goals and objectives such as a means to obtain an organization's non-value-adding activities so that organizations can concentrate on their core-competency or value-adding functions. Recently organizations have started outsourcing their entire business processes. As the goals of outsourcing changed, the risks changed. Given the original goals of cost reductions, only contract management risk were applicable. As the goals of outsourcing changed, along with contract management risk, organizations inherited process management and even information security, privacy, and confidentiality risks.

Another limitation in this study was scarceness of studies that demonstrated the effectiveness of controls using a multiple criteria risk management strategy. For example, a study by Bielski (2006) explained how governance and contract monitoring strategies significantly reduce contract management risks inherited in outsourcing. Punj (2006) and Tompkins (2005) explained the strategies that controlled the process integration risks. Allied studies by Koh, Ang, and Straub (2004) explained how good exit and transition plans, and performance evaluations allowed buying flexibility. Weiss (2007) offered detailed explanations of exposures related to information management, security, and privacy and confidentiality risks. Willcocks (2007) offered risks management strategies for these types of risks. In this study, data from these studies was combined to create a comprehensive list of outsourcing risks and a framework of related risk management strategies without consideration to the different aspects of each of those studies.

Another limitation is that, success of any risk management framework is contingent upon various market driven factors such as technology capabilities, maturity of the organization, knowledge management capabilities of



the organization, nation maturity such as adopting and enforcing various rules and regulations, changing economic, social, and the political landscape of both the outsourcing buyer and the outsourcing seller. These contingencies change the effect of the application of the risk management framework from organization to organization. In other words, given that two organizations implement the same risk management framework both may not be able to mitigate the risks equally.

Rapidly changing business and environmental factors in a global marketplace and limited research in the field of a multiple criteria for responsible strategies and their combined effects on outsourcing success therefore are the limitation considerations for this study.

#### Delimitations

Despite the limitations indicated, multiple sources including theoretical frameworks, case studies, industry experts, government agencies, and other research-based studies ensured the quality of this inquiry. This study used time-tested theories and principles from various management disciplines to establish the list of variables used to answer the research questions. The list of variables used in this study came from the available

theoretical frameworks and were validated against findings in current research based studies. This process increased the validity of the study and reduced the chance of testing for variables that were contingent upon factors such as the size of the organization, type of outsourcing relationship, or other contingencies specific to a type of outsourcing practice.

Concepts of creating sustainable value from the economics discipline, and principles of strategic and organizational management requirements for competitive advantage from the organizational management and strategic management disciplines were used to validate the responsible risk management strategies used as the variable in this study. Applicable theories were used to determine the universal risk variables and responsible strategies that were not impacted by the changing environmental contingencies. A thorough review of all literature during the last five years, and a thorough investigation of studies conducted by various independent groups such as Government Accounting Office (GAO), Gartner, Forrester, Meta Group, and The Outsourcing Institute helped reduce the risk of not identifying any significant variable. Experts from outsourcing companies

were consulted to ensure the inclusion of industry knowledge about these risk management strategies.

#### Definition of Terms

*Business imperative:* A necessity created by the environment in which a business operates (Tompkins, 2005).

*Exposure:* The amount of risk multiplied by the total impact (Dean, 2005).

*Off-shoring:* when outsourcing involves a purchase of a business activity from an organization abroad or a foreign country (Modarress, 2007).

*Outsourcing:* a practice when a business entity purchases some of their business activities such as inputs and services from other organizations (Enlow, 2006).

*Outsourcing failure:* When outsourcing has a negative impact on an organization's performance or fails to deliver the established outsourcing value, goals, or objectives (Kakumanu, 2006).

*Outsourcing goals and objectives:* The result an organization anticipates from their outsourcing relationship (Enlow, 2006).

*Outsourcing organization:* A buyer or an organization that uses another entity to provide activities that is used to meet their own organizational goals (Dhar, 2006).

*Outsourcing provider:* The organization, which provides outsourcing services for another organization (Dhar, 2006).

*Outsourcing risk exposure:* A negative impact of an uncontrolled outsourcing risk such as resource waste, loss of jobs, business interruption (Kakabadse, 2003).

*Outsourcing value:* The goals and objectives established for an outsourcing practice (Kakumanu, 2006).

*Product or manufacturing outsourcing:* when a firm purchases goods (i.e., cars, parts) from another company (Rossetti, 2005).

*Risk:* A concept that denotes a potential negative impact to an asset or some characteristic of value that may arise from some present process or some future event (Dean, 2006).

*Service outsourcing:* When an organization purchases services from another organization. These can include customer service functions, project management, technology development, maintenance and support, human resource, accounting and finance, legal, and other business processes (BPO) (Punj, 2006).

*Value:* When net benefits are achieved or when the gains are higher than the losses (Willcocks, 2006).

## Summary

While outsourcing and offshore outsourcing enables organizations to become competitive, they can become a vehicle for economic disaster when organizations fail to mitigate and control the outsourcing risks inherited. Outsourcing has become a business imperative in the 21<sup>st</sup> century (Tompkins, 2005), and a necessary restructuring method in today's competitive market place (Gurung, 2006). As a restructuring method, outsourcing can enable organizations to focus on their core-competency or value-adding functions and capitalize on their knowledge, skills, and abilities (Sheng, 2006). According to Barthelemy (2006), the problem with outsourcing is that it is a risk-laden venture, which exposes organizations to negative economic consequences. Research-based studies recommended that outsourcing organizations could reduce the inherited risks by using responsible risk management strategies.

If used correctly, research has indicated that outsourcing partnerships can enable organizations to become competitive. According to Sheng (2006), when outsourcing partners are strategically selected to perform an organization's non-value-adding and difficult-to-perform tasks, outsourcing provides a complementary buffer for

organizations. Obtaining an organization's non-value-adding functions from others improve an organization's ability to focus on their core-competency or value-added functions and improves their overall services. Choosing outsource providers that specialize in an organization's non value-adding services and can offer those services at a lower cost, further enables the outsourcing organization to reduce their cost of operations and improve the overall quality of their processes.

Despite the value propositions mentioned above, studies conducted between the years of 1994 to 2004 found that the use of outsourcing has not allowed U.S. organizations to become competitive. More significantly, research studies have shown that outsourcing practices has wasted valuable organization resources, caused unnecessary business interruptions (Cascio, 2005), and increased customer dissatisfaction over poor quality deliverables (Barthelemy, 2003). The main reason for these negative consequences, as reported in research-bases studies, is that outsourcing organizations did not pay attention to the inherited and did not use responsible strategies to control the exposures of these risks. Consequently, the use of outsourcing has reduced U.S. organizations' revenues,

market share, and shareholder's wealth (Enlow, 2006). If these strategies are not adopted the competitiveness of U.S. businesses in the global marketplace can be reduced.

In short, while outsourcing can allow organizations to become competitive, to achieve this goal organizations have to use responsible risk management strategies. Research-based findings have demonstrated that the use of responsible strategies can help organizations prevent resource waste and achieve their intended outsourcing goals (Enlow, 2006). The goal of this study was to explore to what extent U.S. organizations use responsible risks management strategies and explain whether these findings indicate that outsourcing organizations' actions can prevent future economic losses for outsourcing companies and the U.S. economy.

Chapter 2 of this study presents the current literature and findings on the frameworks that describe the outsourcing value propositions, current experiences of outsourcing organizations, and the risks that become barriers to achieving outsourcing goals. Chapter 2 presents (a) the exposures of uncontrolled risks in terms of negative impacts on the outsourcing organization and the economy, and (b) the proposed responsible strategies or best

practices that research based studies claim organizations should use to reduce their outsourcing risks in order to achieve their intended outsourcing goals.

In chapter 3, a research methodology for this study is proposed. The research methodology section describes the means for collecting and analyzing the data required to answer to the research questions posed in chapter one. Chapter 4 presents the data analysis section of this study. Chapter 5 presents the answers to the research questions and recommendations for future studies.



## CHAPTER 2:

### LITERATURE REVIEW

The purpose of this chapter was to examine the literature relevant to outsourcing practices. This review of the literature included the years 2000 to 2007 and is presented under the five headings (a) overview and outsourcing value proposition framework, (b) current outsourcing experiences, (c) explanations for outsourcing risks and potential exposures for outsourcing organizations, (d) responsible risk management strategies that reduce the negative impacts of outsourcing risks, and (e) summary of the literature review.

The EBSCO and ABI/Inform databases were the primary databases searched for a list of outsourcing related research and findings. Peer-reviewed journal articles were the primary source of information for this literature review. Other sources used for the literature review included various research oriented consulting firms such as the Gartner group, Meta group, and Forrester research group. The literature review included research-based studies including literature reviews on outsourcing trends and risks, empirical studies on organization experiences, case studies on application of methods for achieving

outsourcing objectives, management principles towards creating sustainable values, and grounded theory on criteria towards achieving outsourcing goals. The literature review was not restricted to any method of outsourcing or to any particular industrial sector.

#### Overview and Outsourcing Value Proposition Framework

Since the 1980s, most organizations have undergone major organization restructuring and downsizing efforts and now left so thinned that from the CEO to the entry-level position in the organization most employees have too much on their plates (Caplan, 2004). Research by Enlow (2006) demonstrated that outsourcing enables organizations to address some of the resource constraint problems created due to their previous restructuring efforts. Enlow further suggested that strategic outsourcing enables outsourcing organizations to reduce their cost of operations, and improve the overall organization performance.

Outsourcing is a strategic alliance or partnership between a buying and selling organization where the buying organization uses a contract-based relationship to obtain some of their services from other organizations. Mostly, organizations try to obtain services that they themselves cannot provide as effectively and efficiently

as their outsource partners. Amongst the objectives outsourcing organizations try to achieve are (a) improved ability to focus on their core competency functions by creating a complementary buffer (Sheng, 2006), and (b) ability to reduce an organizations overall costs of operations (Barthelemy, 2006).

When an organization concentrates on their core-competency functions, they are optimizing on their knowledge or specialization (Sheng, 2006). Tompkins (2005) explained that buying organizations could maximize value by concentrating on things that differentiates them in their marketplace, which allows them to maximize the returns on their accumulated learning and knowledge. According to Sheng, complementary buffer is created when an organization buys their non-core activities from other sources to allow them more time to concentrate on their core-competencies. Greater outsourcing value is realized when a buying organization forms a strategic alliance with selling organizations that specialize in the buyer's non-core activities (Willcocks, 2006).

When two organizations can concentrate on their core-competency services, this leads to labor specialization and reduces both organizations' cost of

production due to economies of scale (Kakabadse, 2003). The economies of scale lead to reduced transaction costs for both organizations. This is because both organizations are specializing in their own core-competency areas and this consequently leads to increased degrees of process effectiveness and efficiencies for both organizations (Bartheley, 2003). According to Farrell (2006), achieving an organization's core-competency and non-core-competency services effectively and efficiently reduces the overall cost of operation. Other values realized through this method are increases in the overall quality of services, and improvements in the organization's overall performances. These improvements lead to increased customer satisfaction, increased revenue, and puts an organization in a better position to innovate and grow market shares.

According to Deming (1992), when an organization focuses all of its efforts towards achieving one goal or a common purpose, the quality of the product or services provided increases. Deming indicated that the quality of the product and services leads to higher client satisfaction, which in turn increases the market share for the organizations. These actions further lead to

reductions in cost of the product and increase the organization's financial performance. Deming indicated that when organizations focus on quality this leads to effective and efficient business process, which in turn leads to cost reductions. The goal of an efficient and effective business process and its impact on an organization's performance is described below.

#### *Effective and Efficient Business Processes*

An organization achieves its goals and objectives by designing effective and efficient business processes (Deming 1992). Each business process either receives input from other processes or makes inputs for other processes. According to Deming (1992,) when the cost, quality, and speed of the tasks performed to produce the output is controlled and optimized organizations achieve process efficiencies. Deming indicated that resource availability and congruently integrated processes helped organizations become effective and efficient.

When organizations face resource constraints or an organization's processes are not integrated congruently, process effectiveness and efficiencies are reduced. Lack of skills required to perform complex and difficult tasks, especially when the tasks are not within the organization's

core competencies, reduces the quality of the output of the process (Dean, 2006). Enlow (2005) indicated that when organization's attempt to process complex non-competency task this reduces an organization's ability to concentrate of higher value core-competency tasks. Therefore, resource constraints and the inability to integrate an organization's processes seamlessly reduces the effectiveness and efficiencies of an organization's processes.

Outsourcing offers organizations an opportunity to overcome these constraints by using distant suppliers or other vendors, to meet their entrenched process goals (Barthelemy, 2006). Outsourcing effectiveness studies conducted by Enlow (2006) and Moore (2006) indicated outsourcing allows organizations to reduce the time to process by using distant suppliers in different time zones. Rational behavior in selecting skilled resources at reduced prices can significantly reduce the cost of input, output of the processes, and helps organizations reduce its overall cost of processing and the quality of the overall product and service (Farrell, 2006). According to Farrell, Laboissiere, and Rosenfeld (2006) this goal is

achieved when companies based in high-wage economies pursue vendors in low-wage economies.

Outsourcing effectiveness studies by Cascio (2005) and Enlow (2006) have suggested that this form of restructuring not only enables an organization to reduce their operation's cost and improve the overall quality of products and services but also can improve the speed-to-market, and enable organizations to innovate and enter new markets. According to Gurung (2006), the speed-to-market is improved when third party vendors in different parts of the country or the world are used to develop a company's product or provide their services around the clock.

When organizations specialize in what they do best and are not distracted from difficult non-core-competency processes, they can concentrate on higher value processes and on strategies for innovation and growth (Sheng, 2006). In addition, choosing outsource relationships based on skilled resources at the lowest possible cost reduces the costs of operations (Barthelemy, 2003). Farrell (2006) indicated that the overall performances of organizations are improved when outsourcing allows organizations to realize the above two values. Farrell indicated that

improved performances are required for organizations to meet the globally competitive challenges.

#### Current Outsourcing Experiences

While various research studies discussed above demonstrated that outsourcing could enable organizations to realize values, other research-based studies have indicated that most outsourcing organizations fail to achieve these objectives. A study by Willcocks (2007) indicated that after a decade of using outsourcing, organizations have not only failed to realize their anticipated outsourcing goals but have created unnecessary and complex business processes that have led to resource waste. Gartner Group (2005) found that more than 50% of U.S. outsourcing organizations failed to receive their outsourced services on time and within budget. These studies indicated that organizations that have been using outsourcing have wasted valuable resources, reduced shareholder values, and some have seriously jeopardized their abilities to compete in a globally charged and competitive marketplace.

Other studies have indicated similar results for outsourcing organizations throughout the world. Barthelemy (2003) conducted an empirical study of 91 organizations across the world and found that outsourcing organizations



not only failed to achieve their intended goals but have experienced negative impacts on their organization's performance. For example, a rental company in this study reported that instead of achieving the anticipated value of reducing their operating cost by 3 to 4%, the use of outsourcing actually increased their operating cost to 10%. The sample study included various types of service outsourcing including IT, BPO, HR, telecommunication, and retail during the period 1990-2002. It was demonstrated in this study that negative returns or not being able to create the intended returns was a very common trend across all service outsourcing regardless of the type, nature, and size of the organization.

Another study by Enlow and Ertel (2006) surveyed 200 outsource buyers during a period of 18 months and found similar results. They compared their results with other studies conducted by consulting companies such as Deloitte and Touche, Gartner Group, and Meta Group and found that not realizing established outsourcing objectives was not just a norm but also a growing trend. An independent study of outsourcing buying experience, by Deloitte and Touche Consulting (as reported by Enlow, 2006) found that approximately 80% of all outsourcing relationships during

2005 led to negative returns. In their own study, and their comparison of studies done by various researchers during the period of 2004-2005, Enlow and Ertel (2006) found that failed outsourcing relationship was more common than successful relationships.

Review of various independent research findings by Weiss, (2007) indicated that at least 50% of outsourcing arrangements fail to meet their goals of reducing cost or improving performance and at least 80% of outsourcing projects experience problems such as cost-overruns, non-adherence to buyer's needs, and increased time to deliver services. Data analysis conducted by Modarress, and Ansari (2007) confirmed these results as well. This data analysis included data obtained from the Bureau of Labor Statistics and audit reports from the U.S Government Accounting Office (GAO). The analysis of data from these agencies indicated that during the first decade of use, outsourcing arrangements caused operational ineffectiveness, inefficiencies, and reduced value for the outsourcing organization's stakeholders. Studies by Harrison (2006) demonstrated that outsourcing practices have increased unemployment in the U.S. rather than create the new jobs

as was indicated in a Department of Commerce report in 2004.

Despite these negative experiences, many researchers mentioned above have argued that outsourcing is a good method for organizations to create complementary buffers for their organizations and allow organizations to focus on their core competency functions. It was suggested that using this alliance to obtain one's services is a business imperative in a globally charged economy (Tompkins, 2005). Willcocks (2006) explained that it was not the outsourcing practice but failure for organizations to adopt risk management strategies to mitigate risks inherited when organizations outsource that has had led to these widespread losses.

According to Barthelemy (2003), the failure to achieve an organization's outsourcing goals is due to the ineffective methods organizations have been using to manage the risks inherent in outsourcing. Bielski (2006) explained that governing outsourcing contracts could significantly increase an organization's ability to achieve their intended goals. Dean (2006) indicated that responsible strategies such as hiring qualified outsourcing vendors, communicating an outsourcing

organization's needs to the outsourced companies, and monitoring performances could significantly improve an organization's ability to achieve their outsourcing goals. Enlow and Ertel, (2006), stated that retaining core competencies in-house to manage outsourced vendors was essential to manage outsourcing risks. Punj, (2006) insisted that having a detail plan for what services to outsource and what to retain in-house would reduce the more serious risks in outsourcing such as losing an organization's ability to bring outsourced services in-house. Sheng, (2006) indicated that retaining knowledge of outsourced services in-house can significantly improve an organization's ability to manage most risks inherited in outsourcing. These researchers all argued that the only way to achieve an organization's outsourcing goals is to use responsible strategies to manage the risks organizations inherit when they outsource.

#### Outsourcing Risks and Exposures

Research-based findings have demonstrated that inherent in the practice of outsourcing are various risks. A careful consolidation and synthesis of findings from all recent literature allows us to categorize the major risks in three groups. These three categories or risks include

(a) the contract management risks, (b) the process management risks, and (c) other extrinsic risks.

The first group of risks are directly related to the existence of a contract that is created between the partners in an outsource relationship. The two partners in an outsource relationship are (a) the buyer or the organization that is using the method of outsourcing to obtain some services from others, and (b) the seller or the outsource provider that is providing the services to others. Risks inherent in this contract based partner relationships can be grouped as the contract management risks. Contract management risk arises due to uncertainties inherent in a resource dependent and contract based relationship. These uncertainties lead to various miscommunications between two contracting parties (Willcocks, 2006). According to Weiss (2007) both intentional and unintentional communication gaps risks are very common when two different organizations use written contracts.

The second group of risks are related to the process used to manage the outsource service. These processes include coordination of efforts between two organizations, planning and organizing, making decisions regarding what

knowledge capabilities are needed to monitor, control, and manage changes that occur because of using outsourcing. Risks inherent in the process management aspect of outsourcing will be grouped as the outsourcing process management risks. The process management risks arise due to (a) poor or lack of planning and (b) the complex nature of coordinating the efforts of two distant entities. Without good control over the processes, an organization cannot ensure that the services promised by the buyer will be delivered on time, on budget, or within the organizations quality requirements. Process management risks create disintegrated franchises, leaves an organization vulnerable to reduced in-house knowledge and capabilities to monitor and measure the outsource provider's performance or the overall benefits or exposures of outsourcing.

The third group of risks is related to various extrinsic factors that are inherent when two organizations with their own separate management style, competitive pressures, belief system work together to achieve a goal. Two organizations from different geographical area may not understand the confidentiality and privacy rules and regulations of each other. These extrinsic risks can include the potential loss of intellectual property,

privacy, and confidentiality of client data and information, and even quality of products and services.

To understand these risks, how and why they are created, or what exposures result due to these risks, several researchers offer further explanations. The explanations of the factors that create the contract management, process management, and other extrinsic risks are detailed below. The exposures created by these risks on an organization's ability to realize their outsourcing goals are provided following the discussion of each of the three categories of risk.

#### *Contract Management Risks*

The transaction cost economics (TCE) theory by Williamson (1999) explained that a buyer-seller contract based relationship is laden with incomplete contract and imperfect information risks. Incomplete contract risks exist due to changes that occur in the buyer and seller organizations after the contract is written. Imperfect information risks are created because in outsourcing two organizations acting in their own best interests have to transfer timely knowledge required by each for critical decision-making.

Contract management risks increase (a) buyer uncertainty in terms of their ability to obtain the required outsourced services, (b) cost of outsourcing due to the need to monitor and control changes to contract, and (c) moral hazards such as unfair negotiating and haggling by the seller or the outsource provider (Williamson, 1999). When a buyer is dependent on others to perform their activities various uncertainties are created. Buyer and outsourcing provider's circumstances change with time. Changes in buyer's needs may require significant changes in the requirements or specifications of a contract (Bielski, 2005). Given the new changes to the requirements, the seller may not have the needed resources to meet the buyer's needs. In addition to changes in buyer requirements, outsourcing providers can also experience operational changes during the course of a contract. These can result due to changes to the organization structure, labor market, social, political and other economic circumstances. These changes create uncertainties regarding the buyer's ability to receive the promised services.

Buyer uncertainties leave an organization vulnerable to increased outsourcing costs. Some of these increases in costs are due to the need to closely monitor and manage the



changes in outsourcing contract (Punj, 2006). Outsourcing sellers are often under pressure to create value for their own stakeholders, which can lead to moral hazard practices (Williamson, 1999). A moral hazard commonly present in contract-based relationships is when sellers add unnecessary costs to contracts or negotiates higher prices for their services when they know the buyer's are dependent on them to deliver their own services. These moral hazard problems in outsourcing expose outsourcing organizations to unfair contract negotiations.

Imperfect information increases knowledge transfer uncertainties, which affects the outsourcing organization's ability to make timely decisions. Imperfect information risks arise due to the intentional and unintentional communication gaps inherent in outsourcing. According to Koh (2004), in a partnership relationship, two organizations with different management styles, organizational culture, and stakeholder priorities work together to meet the goals of one organization. Gurung (2006) explained this as a major cause of miscommunication in any partner relationship.

Intentional communication gaps can occur when an outsourcing supplier withholds information from the buyer

to avoid investments and changes that can impact their own revenue and expense goals. For example, an outsourcing provider may withhold information about technology advancements that can improve process efficiencies and improve the delivery times (Gurung, 2006). However, their own revenue or expense goals may prevent them from making the investments required to implement the new technology. Outsourcing suppliers can withhold resource constraint information such as other contract priorities and labor market conditions in order to keep the contract. These conditions however can affect the outsourcing provider's ability to provide sufficient talented workers to adequately meet the buyer's requirements in terms of timely delivery and quality of services. According to Weiss (2007) culture, politics, and linguistics can introduce other unintentional information gaps in outsourcing. Gurung stressed that the difference is culture is inherent in all contract-based relation, but prevalent when a foreign outsourcing provider is used.

Both intentional and unintentional communication problems create imperfect information risks in outsourcing. These communication gaps introduce unfair advantages (Gurung, 2006) for the outsourcing organization and reduce

their ability to plan for delayed services and make critical decisions about reducing quality problems (Willcocks, 2006). Uninformed decisions expose an organization to higher costs of transactions (Williamson, 1996). Bathelemy (2003) noted in his study that lack of information reduced operational efficiencies, and various competitive disadvantages.

#### *Contract Management Exposures*

Contract management risks expose an organization to (a) increased overall operations cost, (b) business interruptions, (c) increased vulnerabilities to customer dissatisfaction, and (d) potential negative image and financial consequences due to problems such as litigation and quality problems. These risks reduce an organization's ability to realize the improved performance goal of outsourcing and can threaten an organization's ability to compete effectively in a globally competitive marketplace.

Incomplete contracts increase buyer uncertainty, costs and complexity of contract monitoring, and the chance of unfair contract negotiation practices. These risks expose an organization to ineffectiveness, inefficiencies, reduced overall quality of services for their customers, complexities in contract management, and increases in

outsourcing costs. The net effect of these exposures reduces the net benefits anticipated from outsourcing.

Imperfect information increases glitches in timely transfer of knowledge. Glitches in timely knowledge transfer can reduce an organizations ability to make timely decisions about changes, process improvements, and market share opportunities. These can negatively affect an organization's ability to increase market share, reduce cost of operation, and increase revenue. In sum, contract management risks seriously jeopardize an organization's ability to survive in a globally competitive advantage.

#### *Process Management Risks*

Outsourcing creates a new process and organizations have to ensure the effectiveness of this process by dedicating knowledgeable staff to manage the new process (Koh, 2004). Like any other process, coherently integrating all activities related to outsourcing is critical to the success of outsource process management. Barthelemy (2003) indicated that outsourcing process is laden with risks inherent in planning required before outsourcing, coordinating required to integrate the outsourced service back in the organization, and change management required to manage the outsourced activities.

Planning success depends on the inputs from various department heads in an organization and objective decision-making (Punj, 2006). However, time constraints and pressures from various stakeholders to use the outsourcing method to improve an organization's performance introduce various poor and uninformed planning risks (Willcocks, 2006). Coordination efforts to integrate two or more organizations activities can be very challenging and complex and can introduce various process gaps (Enlow, 2006). The outsourcing practice creates resources dependence and subject to various contract based relationship risks. Modarress (2007) further stated that uncertainties in the marketplace, future needs of the organization, and the outsource provider circumstances add various change management challenges.

When organizations outsource parts of their activities, they can lose valuable in-house knowledge and capabilities as well. Tompkins (2005) indicated that any loss of in-house knowledge and capabilities related to the outsourced services increases an organization's dependence on others for internal knowledge and can negatively affect the organization's ability manage outsourcing risks and changes. The resource dependency theory indicates that lack

of internal knowledge to manage any aspect of an organization's operation leads to an inability to control an organization's own destiny. These process management challenges can expose the outsourcing organization to (a) a disintegrated franchise (b) loss of expertise and capabilities, and (c) inability to control one's own destiny.

#### *Disintegrated Franchise Risks*

Outsourcing requires an organization to disintegrate its vertically integrated internal processes and horizontally integrate other external processes (Enlow, 2006; Willcocks, 2006). When the processes of two different organizations are integrated to achieve an organization's goals there is always a chance of creating incoherency (Tompkins (2005). Lack of coherent coordination of efforts between two organizations can create process gaps, which can lead to ineffectiveness and inefficiencies in managing inputs and outputs between the buyer and seller organization (Enlow, 2006).

Outsourcing organizations become dependent on other external organizations and their processes, policies, and procedures to achieve their own effectiveness and efficiency goals (Sheng, 2006). Due to these resource

dependency contingencies, an organization loses control over some of their process management (Barthelemy, 2006; Modarress, 2007). These problems can expose an organization to delays in input for critical processes involved in core-competence services and reduce an organization's overall effectiveness in meeting mission critical objectives (Tompkins, 2005, Willcocks, 2006).

#### Loss of In-house Knowledge and Capabilities Risks

When organizations outsource parts of their processes to other organizations, they can lose critical in-house knowledge of the functions or activities. Knowledge about these activities can be critical to effectively monitor the outsourced process, handle required change managements, and successfully transfer knowledge of the buyer's processes to the vendor. These knowledge transfer problems can affect the organization's ability to provide vendor, monitor outsource provider's performance, and measure performance outcomes.

Reduced knowledge within an organization makes an organization incapable of managing changes that occur as a result of outsourcing or changes that occur in the outsourced services. According to Willcocks (2006) loss of expertise leave an organization vulnerable to not being

able to provide leadership with future direction regarding the effectiveness of outsourcing, or change decisions such as pursuit of other more capable vendors, or exit strategies to deal with failed or unprofitable outsource relationship.

#### *Process Management Risk Exposures*

Process management risks in outsourcing can cause process incoherency, loss of in-house knowledge and capabilities, and increased risks of business loss and litigation. Disintegrated processes can expose organizations to inefficiencies in operations (Lee, 2004; Modarress, 2007; Wang, 2006). Loss of in-house knowledge and capabilities can seriously jeopardize and organization's ability to manage contract management changes and risks (Casio, 2006; Dean, 2006; Modarress, 2007). In sum process management risks expose outsourcing organizations to competitive disadvantages and reduces their ability to realize the intended outsource value.

#### *Other Extrinsic Risks*

The process of outsourcing requires the sharing on valuable and often confidential business and customer information. These can include trade secrets, valuable intellectual properties, sensitive client information



(Weiss, 2007). Difference in the laws and regulations of the two partners' countries can introduce various extrinsic risks such as business loss and legal mess (Weiss, 2006). Poor privacy and confidentiality protection policies and procedures of outsource providers and the differences in the data and intellectual properties laws in the seller's country can pose significant contract management risks as well. Data exchanged between two parties over the network can increase these risks due to the prevalent nature of network intrusions.

#### *Extrinsic Risk Exposures*

Misuse of intellectual property or violations of the outsource providers or their customers' confidentiality, privacy, and security rights increases an organizations exposure to financial and image loss problems. Violation and misuse of confidential information can lead to customer dissatisfaction, and potential litigation. These extrinsic risk factors expose an organization to various legal, contractual, and standard incompliance risks.

#### Strategies that Mitigate Outsourcing Risks

Empirical studies by Barthelemy (2003) and Enlow and Ertel (2006), case studies by Willcocks (2006), and various applicable theoretical explanations by Dean (2006), and

Aron (2005) suggested that carefully crafted and responsible outsourcing strategies can allow organizations to minimize their outsourcing risks and increase their ability realize sustainable contract value. Responsible risk management strategies allow organizations to control the risks that prevent them from achieving their outsourcing goals. Principles from contract management (Barthelemy, 2003), relationship and partnership management (Koh, 2004), monitoring and governance (Bielski, 2006), process management (Punj, 2006), and knowledge management (Sheng, 2006) have been used by researchers to show that an organization's outsourcing goals can be met if they systematically manage the risks related to outsourcing.

Good contract management and governance strategies have been shown in literature as adequate controls for various contract management risks. Contract management strategies proposed by various researchers including Barthelemy (2003), Koh, Ang, and Straub (2004), and Willcocks (2006) have suggested that in order to ensure sustainable outsourcing value, buyers should systematically perform and manage various contract management activities. These activities include: (a) define the scope of the project adequately, (b) clearly specify the deliverables

anticipated from the outsourcing provider, (c) choose qualified vendors to provide outsource services, (d) include specific contract terms such as performance measurement rights, change requirements, and termination rights and bases, (e) base contract price on deliverables to be provided, (f) establish performance measurement standards and terms, and (g) monitor and measure outsource provider's performance regularly.

Contract management and governance strategies were shown in literature as good controls to control communication gaps that lead to imperfect information risks. These included (a) define the scope of the project, (b) provide clear specification of the deliverables expected in terms of schedule, quality, and terms, and (c) monitor and measure the performance of the outsource vendor against the detail specifications (Bielski, 2006; Punj, 2006; Willcocks, 2006). These strategies allow the buyer to determine whether the providers are complying with the detail requirements of the projects. The strategies ensure that the seller understands what is expected of them. Close monitoring allows the outsourcing organization obtain valuable information about the outsourced services.

Selecting outsourcing providers based on the technical and skill set requirements of the projects was suggested as an important risk management strategy to ensure outsourcing success (Barthelemy, 2003). In addition, Barthelemy suggested that a seller's financial conditions should be qualified in order to ensure that the provider has the financial strength to deal with changing labor market, and other conditions that may require additional investments to meet the outsource service requirements.

The process management risks inherent in outsourcing include (a) the disintegrated organization, (b) loss of in-house knowledge and capabilities, and (c) other extrinsic risks such as potential disclosure of proprietary information that organizations share with their outsource vendors such as confidential intellectual property and client information.

Studies by Punj (2006), Sheng (2006), and Tompkins (2005) demonstrated that organizations could reduce disintegrated franchise risks by carefully planning which processes should or should not be outsourced. To maximize or even realize outsourcing value it was suggested that organization determine the value to be achieved by the outsourcing practice and outsource only those activities

that create value (Tompkins, 2005). Willcocks (2006) and Punj (2006) suggested that outsourced services should be cohesively integrated with internal processes to ensure timely receipt and delivery of inputs and outputs to and from outsource providers.

One of the most important risk management strategies suggested in literature was retaining knowledge internally to control outsourced processes. Various studies demonstrated that outsourcing organizations must either retain in-house experts or hire outside expertise (Punj, 2006; Tompkins, 2005, Willcocks, 2006). Punj indicated that even when some employees from the outsourced services are retained, it is unlikely that their roles are unchanged. Tompkins (2005) and Willcocks (2006) have recommended that in order to manage outsourcing operations effectively and efficiently organizations must retrain stay-back employees on their new roles and responsibilities.

Retained in-house knowledge and expertise is needed to provide change management direction and help management make informed decisions about their outsourced services (Tompkins, 2005). Willcocks (2006) suggested that ensuring that core activities and knowledge and capabilities related to core activities are retained in house helps monitor

outsource provider's performance and reduce contract management risks.

Researchers suggested various responsible strategies to reduce or mitigate extrinsic risks such as disclosure of confidential information and inability to protect the privacy and security of data. Enlow and Ertel (2006) indicated these strategies should include; train vendor's on buyer's data protection requirements, review policies and procedures of providers, and measure the outsource provider's performance to ensure compliance with contract terms and deliverable specifications. Modarress and Ansari (2007) and Weiss (2007) added that outsourcing organizations should choose qualified vendors, include terms in outsource contract requiring vendor's to comply with buyer's information protection requirements.

A consolidated list of the responsible risk management strategies found in this literature review included: qualify vendors; have "well-defined" project scope; write clear specification of deliverables and requirements; enforce buyer's right to monitor, monitor changes to control destiny; measure vendor performance; train outsource vendors and transfer knowledge; have a general outsource plan; establish measurable outsourcing goals;

integrate outsourced and in-house processes; retain core-competency knowledge of outsourced processes; enforce confidentiality, privacy, and data security requirements; have exit strategies and good change management strategies. A detail explanation of each of these responsible risk management strategies, as explained in this literature review, is provided next.

#### *Vendor Qualification*

Qualifying and choosing outsource service providers based on their skills and abilities, and financial capabilities provides assurance that vendor has (a) the skills needed to perform the services, and (b) financial capabilities to acquire skilled resources and make necessary investments to perform the services effectively and efficiently. According to Willcocks (2006), while vendor financial capabilities may be less significant in short term contracts however, it is a crucial success factor in long-term contracts.

#### *"Well-Defined" Project Scope*

"Well-defined" project scope prevents unnecessary haggling and negotiation from the vendor. According to Punj (2006), when the scope of a project is not well defined, the vendor can demand additional service fees claiming

services requested were outside the scope of the project. A "well-defined" project scope also significantly reduces miscommunications, misunderstanding, and other project complexities that often lead to high project monitoring costs.

#### *Clear Specification of Deliverables and Requirements*

Clear and detailed specification including detail deliverables or requirements of a project eliminates various communication problems (Barthelemy, 2003). Clearly defined requirements of a project (a) allows the buyer to determine exactly what they are paying for, (b) sets expectations for the vendor regarding what they need to be deliver to the buyer (Punj, 2006), and (c) becomes the standard against which a vendor's performance can be monitored and measured. Clear specification should include (a) quality requirements of delivery, (b) schedule of delivery, and (c) payment terms per delivery (Koh, 2004).

#### *Enforcement of Buyer's Right to Monitor, Measure, and Control Destiny*

The buyer's right to monitor must be included in the terms of the contract (Feeney, 2006). When buyers adequately communicate and get an agreement to monitor the performance, this can reduce vendor slack and moral hazard.



According to Koh (2004) enforcing a buyers right to monitor and measure increases the buyer's ability to monitor changes and maintain control of outsourced service.

#### *Performance Measurement*

Measuring the performance provides governance and increase certainty of what is being received (Bielski, 2006, Willcocks, 2006). In addition to the buyer getting the assurance that what they are receiving is what was promised, measuring improves timely information about performance and its effects on other processes (Barthelemy, 2003. Koh (2004) indicated that timely information allows buyers to make informed change management decisions including termination decisions.

#### *Vendor Training and Knowledge Transfer*

Training from the buyer reduces the chance of miscommunication (Koh, 2004). Service performed by outsource provider's ultimately have to be integrated back into the systems and processes of the buyer. Vendor training transfers necessary organization information to the provider and reduces uncertainties about buyer needs (Tompkins, 2005).

### *Dedicated Outsourced Service Oversight*

Oversight is one of the critical success factors for any contract-based relationship. Having dedicated staff to manage the various steps of the outsource project assures consistency, improves relationship management, and improves communication effectiveness (Bielski, 2006). Oversight ensures that the vendor is delivering what was expected.

### *General Outsource Plan*

A general outsourcing plan should guide all outsourcing decisions. According to Kakabadse (2003), a general outsourcing plan ensures that the organization has deliberately (a) planned the outsourcing efforts, (b) identified what can and cannot be outsourced, (c) calculated the value to be anticipated from each outsourcing project, (d) documented the methodology for integrating outsourced services back into the organization, (e) identified the skills and other resources needed to monitor and measure the performance of the vendors, and (f) planned the transitioning needs to other vendors or back in-house in case of a failure.

### *Integrated Outsourced Activities and Processes*

To improve the effectiveness and efficiency between two partner organizations, outsourced operations efforts

should be coordinated with in-house processes. According to Enlow (2006), coordinating the efforts between the buyer and the provider enables the buyers to integrate coherently the two organization's activities and ensures the timely receipt and delivery of inputs and outputs from and to service providers.

#### *Retention of Core-Competency and In-house Expertise*

Retaining expertise and knowledge of outsource services ensures the ability to provide adequate change management and measure vendor performance (Enlow, 2006; Punj, 2006). When an organization loses core-competency skills such as the ability to determine what technology can enable an organization to expand and grow they become very incapable of making informed decisions regarding (a) what to expect of the vendor, and (b) what changes to make in vendor relationship. Most support services that an organization performs have core-competency functions or knowledge that affects the overall organization wide decision-making. Loss of expertise in core-competency functions lead to hollow and disintegrated organizations.

#### *Specific Measurable Outsourcing Goals*

Measureable outsourcing goals makes it is easier for an organization to determine whether their outsourcing

vendor is allowing them to achieve their desired goals. According to Kakabadse (2003), quantifying goals such as reduce cost of operations by three percent or achieve 10% increase in sales are preferred means of specifying measurable goals. Quantifiable goal becomes the metric against which organizations can compare what was expected versus what was achieved.

#### *Confidentiality, Privacy, Security Consideration*

Determining information disclosure risks such as disclosure of customer data or proprietary information, and assessing the vendor's capability to prevent the disclosure enables organizations to prevent various risks of violating standards, rules, and regulations (Weiss, 2007).

Outsourcing organizations should determine the vendor's information confidentiality, privacy, and security protection, policies, procedures, and methods used prior to engaging in outsourcing relationships.

#### *Exit Strategy*

An exit strategy ensures the smooth transition of failed or less-than satisfactory outsource services. The exit strategy provides flexibility and enables a buyer to pursue other better alternatives especially when the provider's performance is unacceptable (Kakabadse, 2003).

According to Barthelemy (2003) organization's should always explore new opportunities to improve any aspect of their business operation and having exit strategies enables organizations to effectively transition into better competitive positioning.

### *Change Management*

Change management allows organizations to make necessary and ongoing changes in contract terms and in-house processes required to stay competitive. Changes can occur in the buyer's needs or the vendor conditions (Enlow, 2006). These changes can significantly affect the outsourcing process and should be constantly monitored and controlled. Change management helps organizations manage changes in a controlled manner.

### Summary and Research Question Implication

This literature review attempted to consolidate findings from various outsourcing studies in an attempt to discover (a) the value of outsourcing, (b) current experiences of organizations that use outsourcing, (c) the reason for these experiences, and (d) that recommended risk management methods for mitigating the exposures in terms of negative economic outcomes.

Literature review was replete with suggestions that outsourcing is an excellent method for organizations to improve their overall business performances. However, almost all current research-based studies found that currently organizations are not realizing their intended outsourcing objectives. In their separate and independent studies regarding failed outsourcing relationships, Barthelemy (2003), Bielski (2006), Enlow, (2006), Farrell (2006), Gurung (2006), and Willcocks (2006) all found that the reason that organizations fail to achieve their outsourcing goals is because they do not use responsible risk management strategies to control three main types of outsourcing risks. These included (a) contract management risks, (b) process management risks, and (c) other extrinsic risks.

Synthesis of findings from these studies indicated that outsourcing organizations could meet their outsourcing goals if they can mitigate the risks inherited during the outsourcing practices. These studies recommended that outsourcing organizations should adopt responsible risk management strategies to control contract management risks, process management risks, and other extrinsic risks.

In order to control contract management risks, data gathered from this literature review indicated that organizations should implement strategies to control incomplete contract and imperfect information risks. For controlling process management risks, researchers recommended that outsourcing organizations focus on reducing incoherent process integrations between the two partner organizations and control loss of in-house knowledge, expertise, and capabilities risks. Studies by Weiss (2007), suggested that outsourcing organizations should control risks such as disclosure of confidential information and loss of intellectual properties. Weiss indicated that ensuring that the outsource provider organization's privacy, confidentiality, and security policies are similar to the outsourcing organization was an important control.

Literature review was also replete with suggestions that responsible risk management strategies was not an option but a requirement for any organization that uses any form of contract management partnerships to meet their organization's performance goals. According to (Tompkins, 2005) outsourcing is a "business imperative" therefore; organizations must adopt the necessary strategies to

achieve their outsourcing objectives and goals. Enlow and Ertel (2006) indicated that failure to adopt responsible risk management strategies could lead to severe economic distress.

The literature review discussed in chapter 2 highlighted both the risks inherent in an outsourcing practice and the critical need to reduce these risks. This literature review provided a framework of potential risk management strategies that studies claim could effectively control outsourcing risks. This consolidated framework of risk management strategies will serve as the variables that were tested to answer the two research questions that guided the study. Chapter 3 presents the overall research design and the data collection and analysis methods used to answer the study's research questions.



## CHAPTER 3:

### RESEARCH DESIGN

During the first two chapters, the problem of the study, research questions, and the relevant and pertinent literature were presented. This chapter discusses the research design used to answer the research questions. Figure 1 presents a two-step systematic approach used to construct the research design. In the first step, synthesized list of literature review and theory were used to develop a list of theoretically validated risk management strategies. These risk management strategies were also called best practices (BP). In the second step, the process for collecting and analyzing data is explained.

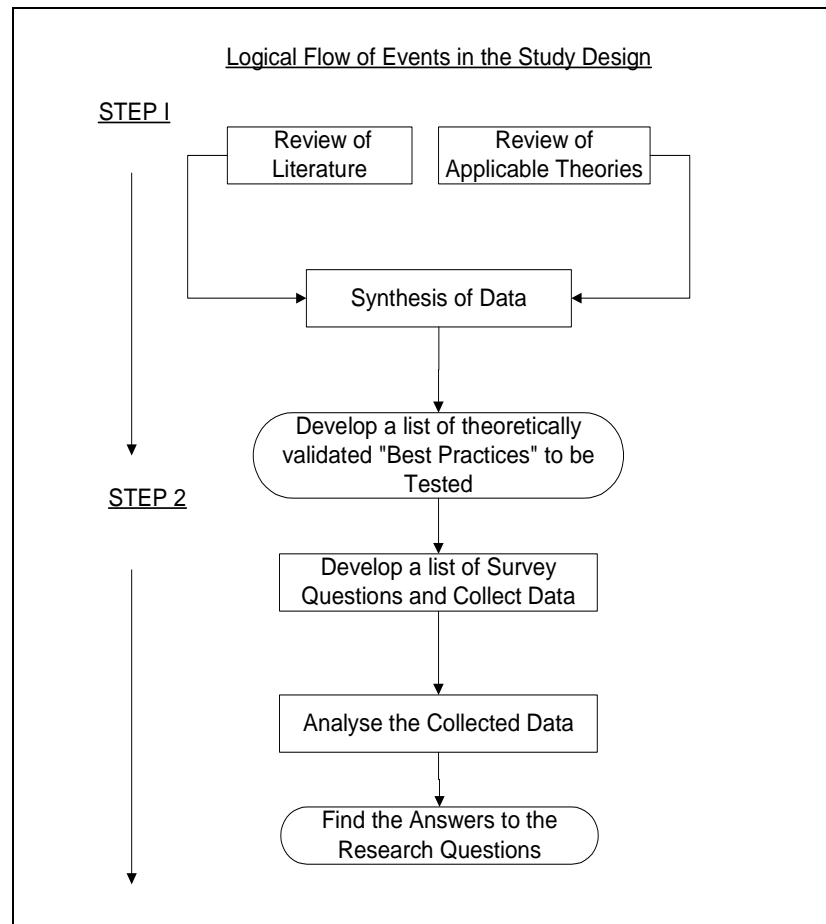


Figure 1. The two steps in the research design.

#### Research Methodology and Design

The study design followed a logical flow of events starting with the literature review findings and ending with the data collection and analysis activities. This logical flow of events is demonstrated in Figure 1. The list of BP or the responsible risk management strategies based on the findings documented in the literature review served as the baseline of variables that was tested. This baseline of responsible risk management strategies guided

the remaining steps in the research design. Survey research method was the method used to collect the data. Descriptive data analysis helped determine the answers to the research questions.

*Develop a List of Best Practices To Be Tested*

Literature and theory indicated that there were three main categories of risks inherent in the outsourcing practice. Further, literature and theory review indicated that multiple factors were the underlining cause for each risk category. As a result, researchers Kakabadse and Kakabadse (2006) indicated that a responsible risk management strategy consisted of multiple best practices that mitigated the individual factors within each category of outsourcing risks.

A consolidation of findings from literature review yielded a list of twenty theoretically validated best practices that research-based studies supported were good characteristics or the framework of responsible risk management strategies. Kakabadse (2006), Barthelemy (2003), and Weiss (2006) agreed that these BP help organizations achieve their established outsourcing goals and helped reduce resource waste. Figure 2 shows the 20 BP and the corresponding outsourcing risks each BP helps

mitigate. Visual Summarization of the relationship between the three categories of risks of be controlled and the 20 BP.

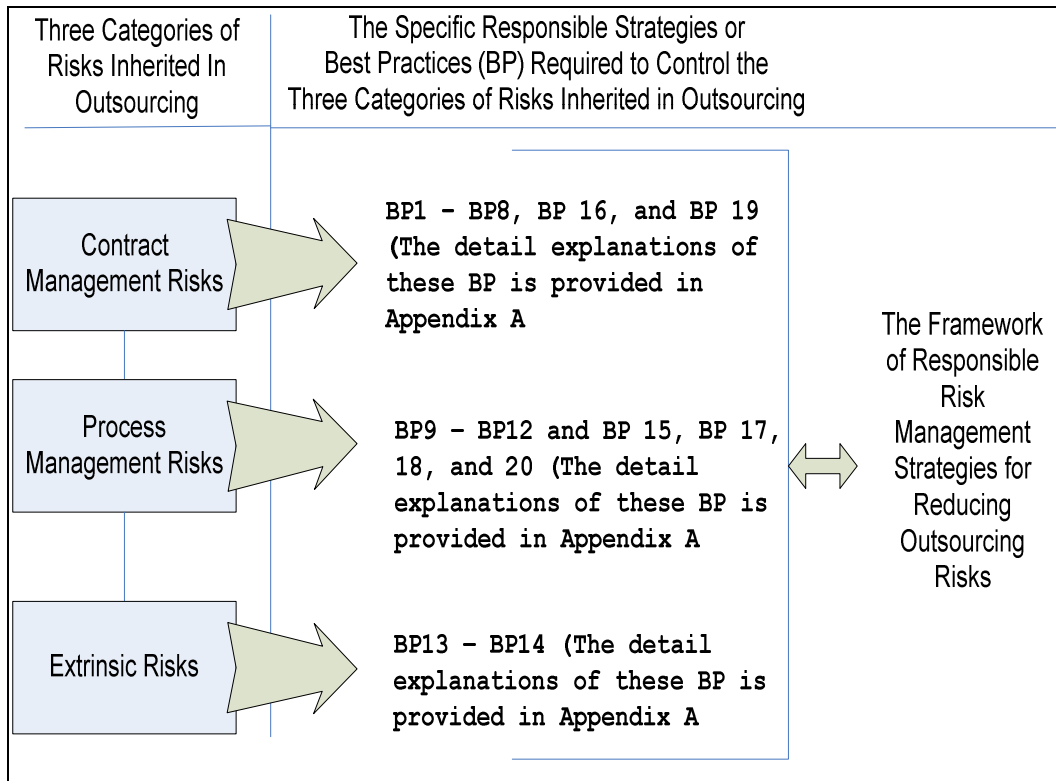


Figure 2. A framework of responsible risk management strategies.

The 20 BP listed in figure 2 were used as the baseline to control the various validity issues in this research. According to Johnson (2004), having this type of a baseline allows the researcher to collect data that is relevant to their research questions. A full explanation of how these BP helps reduce the three categories of outsourcing risks are demonstrated in Appendix A. Appendix

A includes a consolidated list of the outsourcing risks, best practices needed to mitigate these risks, and the reason these best practices are good characteristics of responsible strategies as indicated in the literature review section of this study.

#### *Develop a List of Survey Questions*

A survey instrument was designed to explore whether outsourcing organizations and offshore outsourcing organizations used the framework of risk management strategies or best practices. Descriptive data analysis was used on the survey responses to determine whether outsourcing and offshore outsourcing organizations used the framework of risk management strategies. Descriptive statistics further allowed analysis and explanation the results of the study in terms of whether the extent to which organizations used the strategies enabled them to reduce the exposures of outsourcing risks.

For each characteristic of responsible risk management strategy or best practices listed (BP 1-20) in column B of Appendix A, a specific corresponding survey questions was developed. These survey questions are listed in Section II of Appendix B and referenced in Column A of Appendix A.

To explore the relationship between the application of risk management strategies listed in Section II of Appendix B, Questions 6, Numbers 1 through 20, and whether U.S. organizations mitigated risks more diligently with time, Questions #4 and #5 in Section I was used. Table 1 shows the relationship between the 20 BP questions listed in Section II, Question 6 of the survey instrument and the specific category of outsourcing risks.

Table 1

*Independent and Dependent Variable Relationships*

Dependent variable: category of risk reduced	Independent variables: BP that reduce inherited risks
Reduced contract management risks that can expose organizations to unnecessary economic losses	Best practices related to contract management risks (Relationship between questions #6: 1-8, 16 and 19 listed in Section II in Appendix B and question #4 and #5).
Reduced process management risks that can expose organizations to unnecessary economic losses.	Best practices related to disintegrated franchise risks (Relationship between questions #6: 9-12, 15, and 17, 18 and 20 - in Section II in Appendix B and question #4, and #5).
Reduced other extrinsic management risks expose organizations to unnecessary economic losses.	Best practices related to other extrinsic risks (Relationship between questions #6: 13 and 14 in Section II in Appendix B and question #5 and #6).

### Sample and Data Collection

Survey research was used to determine which risk management strategies are most commonly and least used by outsourcing organizations. Risk Managers, Outsourcing Managers, and consultants that manage outsourcing contracts from 472 United States companies on a list of companies confirmed by CNN. The list was also published in *Exporting American Jobs* (Dobb, 2007). A request to participate in this dissertation study was sent to the risk management experts in these companies. The survey instrument was designed to ensure that only qualified survey respondents were included in the study. Qualifying questions such as the position of the person filling the survey, the number of years the organization had been using outsourcing, and dollar amount range of the outsourcing contract was used to eliminate responses that can reduce the reliability of the study. An option to indicate that outsourcing was not used at all at the company was also provided to ensure that responses from only companies that outsourced were used in the data analysis part of this study.

A survey is one of the most frequently used modes of research in the social sciences. In a typical survey, a

standardized questionnaire is administered to a selected sample of respondents (Johnson, 1997). For this study, from a list of 780 companies all companies that employed over 1000 employees were selected. Four hundred seventy-two companies on this list employed more than 1000 employees. Most all organizations selected had annual income of almost or over \$1billion. Of the 472 companies on the list, 167 were fortune 500 companies, 112 companies employed over 10,000 employees, 72 employed 5000 employees; and the rest of the companies with over 1000 employees.

For each company listed on the sample list, the Director of Internal Audit, Chief Risk Management Officers (CRMO), or the Chair of the Board of Directors (BOD) was emailed a request to respond to the survey. The reason for selecting these individuals is that the Sarbanes Oxley (SOX) Act of 2004, a current mandate by the U.S. government, requires these individuals to determine the risks in their organizations and implement adequate risk management strategies as responses to these risks. The request sent to them included a link to the online web-based survey. It was requested in the email for the receiver to forward the email to their outsourcing managers if they were not directly knowledgeable or in-charge of



controlling the offshore outsourcing risks. In most cases, the Chair of the BOD will not be responsible for controlling the outsourcing risks. However, the Chair was included in the email list to ensure a greater response rate since according to SOX the Chair is ultimately in-charge of all risk management strategies. Since the chair has such responsibility, the assumption was made that they knew the management within the company who had the answer to the risk management questions on the survey.

Survey Monkey, a Web-based survey program was used to design and deploy the survey instrument. Various control features of the Survey Monkey survey program was used to control the design, access, and the responses to the survey. The Web-based survey was hosted on a server located at Surveymonkey.com. Each email to a potential respondent contained a live hyperlink to the survey document on the server. Each respondent went directly to the web based survey and answered the questions.

An anonymous survey was administered to increase the chance of getting a higher response rate and potentially a valid response. A first, second, and third request was sent to ensure a high percentage response rate. The second and third request started with a thank you note, since in a

anonymous survey, responses could not be tracked and there were no ways to determine which companies had responded. To reduce the chance of duplicate responses from respondents once a respondent has answered the survey question, the respondent no longer was able to access the survey. These control features can be turned on by using survey monkey's survey restriction features. The potential problem with this feature is that once a manager had opened the survey, if they forwarded the survey to someone else, the next person could not open the survey either. On the positive side, this eliminated the chance of someone responding multiple times.

Rubin and Babbie (1990) have indicated that survey research is one of the best methods available to social scientists. They indicated that this is especially true for social scientists interested in collecting original data for describing a population too large to observe directly. Converse and Presser (1986) indicated that carefully choosing respondents whose characteristics reflect those of the larger population of interest, and constructing standardized questionnaires that provide data in the same form to all participants was an important consideration for a good survey research.

## Instrumentation

A Web-based survey was used as the primary source of data collection for this quantitative research study. Tuckman (1988), and Cohen and Manion (1989) indicated that survey research is a regularly used method for this type of research. A survey is a system for collecting information to describe, compare, or explain knowledge, attitudes, and behavior (Fink, 1995). According to Fink, surveys involve setting objectives for information collecting, designing research, preparing a reliable and valid data collection instrument, administrating and scoring the instruments, analyzing, and reporting the results.

Appendix B titled "Risk management strategies to mitigate outsourcing risk questionnaire" lists the questions used in the survey instrument. These questions were organized in the web-based survey instrument within the limitations of Survey Monkey's web-based survey templates. In the data analysis section of this study, the data from the web-based survey instrument was sorted in the same order as questions listed in the survey questionnaire or Appendix B.

Two research questions were used to determine whether U.S. organizations use outsourcing used responsible risk management strategies suggested in research-based studies to reduce the impact of these risks on the future ability of U.S. organizations to sustain values created by outsourcing and reduce unnecessary resource waste. These two research questions guided this study:

The first research question was, "What risk management strategies are being used most and least by U.S. organizations that outsourced?"

The second research question was, "to what extent organization that use offshore-outsourcing and have been outsourcing for longer than five years use responsible strategies?"

Outsourcing risk management strategies or BP are the interventions suggested in theory and current literature as requirements to enable organizations to reduce the risks inherited in outsourcing. Contract management, process management, and other extrinsic factors such as loss of intellectual properties are the three categories of risks commonly present in a contract based outsourcing relationship between two different organizations. The reason why these strategies or best practices work is that

it directly controls the negative impacts on the three categories of risks that are inherent in outsourcing relationships.

### Validity and Reliability

A survey research is the most appropriate method of data collection for the purpose of this study. However, while survey research is generally very strong on reliability, they pose some threat to validity issues (Babbie, 1973). The validity of a survey instrument refers to the appropriateness, meaningfulness, and usefulness of specific inferences made from scores (Borg & Gall, 1996). In other words, validity checks ensure that researchers take the necessary steps to deliver a quality research.

By breaking it down to this level, the research can provide greater internal validity. The validity of survey data depend to a considerable extent on the technical proficiency of those running the survey. If the questions are incomprehensible or ambiguous, the exercise may not produce accurate results. These risks are controlled by providing clarity in written questions and ensuring that business terms that are commonly used in business processes, vendor, and contract management are used.

External validity refers to the ability to generalize the research findings from the study to the population. In addition, external validity addresses whether there is consistency between what people say they will do and what they actually do. There is always a chance that some outsourcing managers will say what is not true. However, with sufficient response to the questionnaire the chance of getting answers that is true increases. Since it requires various risk management strategies to effectively control several categories of business risks, it is unlikely that outsourcing managers would feel there is a need to provide an answer that is not correct.

Additionally, the content validity of the survey instrument validates the extent to which the instrument covers investigative questions relevant to the study. This validity was controlled by ensuring that risk management strategies were first derived from various theoretical frameworks and validated against research-based studies. The survey instrument was created based on the nature of the research questions and therefore the questions are relevant to the study. Construct validity addresses the question of appropriateness of fit. Robson (2002) explained it very simply when he wrote, "The issue then becomes: does

it measure what you think it measures?" (p. 102). The fit that Robson speaks about is the fit between the theory in question, the measurement tools chosen, and the results. A few steps were taken to ensure the fit between all these elements. First, the construct or list of variables was developed from the study of theories and validated with literature reviews. Second, applicable statistical analysis, given the type of data measured, was chosen. Finally, survey questions capable of answering the research questions were developed. To ensure the survey questions were applicable the framework to be tested was verified with theory and research based studies. Outsourcing managers from outsourcing consulting companies including Tata Group, EDS, and Accenture Group were asked to validate the survey questions used in the study. The reason to include expert opinion on the wording of the questions ensured discrepancies between industry and research-based study terms were reduced. Outsource consultants at Electronic Data Corporation (EDS) were sent a copy of the survey and asked to provide a feedback first. Based on their responses to the questions additional clarifications were added to the survey instrument. Outsource experts at Tata Consulting and Unisys were consulted for further

clarification. Both Tata consulting and Unisys are very well known and highly respected outsourcing organizations that offer outsourcing services throughout the globe. These measures also increase the reliability of the study by ensuring that information is validated by qualified sources.

Reliability is much easier to control in this type of study. According to Floyd (2001), presenting all respondents with the same standardized questions, and carefully wording the questions can result in high reliability of response. In this exploratory and descriptive study, the survey questions itself was a form of validation. Therefore, duplication of result by others is not an important consideration for this study. Furthermore, a step was taken to control this risk. Qualifying survey questions in the survey was used to eliminate responses from unqualified respondents, scan for and treat outliers.

#### Sample Design

The simplest form of sample design was used for this study. From the list of 780 U.S. companies that outsourced, 472 companies were chosen for the sample frame. The companies on the list include 163 companies



listed on the U.S. Fortune 500-company lists and the rest with at least 1000 employees. For each company, the senior risk manager as defined earlier was sent an e-mail with a request to respond to the survey questions. The sampling frame therefore included 472 individuals who had experience and knowledge about U.S. organizations' risk management practices. According to Cohen (1992), a specific sample size is not an important consideration for this type of study. However, using a 5% margin of error and given a 95% confidence interval, about 45 responses are considered sufficient for this test. The most important criterion according to Cohen was to get at least five responses for each risk management strategy question listed in Section II #6 questions on Appendix B. Since Cohen indicated that as the sample size increases the reliability of the results increases, the survey was kept open for 2 months with an attempt to get a high response rate. The survey was closed for data analysis after three requests were sent to each company. Forty-three complete responses were collected at the close of the survey.

#### Data Analysis

Descriptive statistics and other forms of data analysis were conducted on the survey questions. For this

type of study it was indicated that judgmental statistical analysis was sometimes more meaningful than just statistical analysis (Aczel, 2006). To examine research Question 1, "to what extent do organizations use the best practices or risk management strategies", ranked ordered frequencies and percentages of Section II, Questions 1-20 was conducted. To examine the second research question, is there a relationship between how long an organization has been using offshore-outsourcing and the responsible strategies used, descriptive statistics and a trend analysis study was conducted. According to Barthelmey (2006), the need for the use of risk management strategies increases with time and when outsourcing organizations use offshore outsourcing. The trend analysis can show whether the outsourcing organizations that use offshore outsourcing and have been outsourcing for longer than five years, use these strategies more.

#### Summary

Table 2 provides a summary of the data analysis section and aligns the research questions, survey questions, and statistical analyses methods used to answer the research questions. An explanation of the statistical analyses also provided.

Table 2  
*Research Questions and Corresponding Data Analysis*

Research Questions	Survey Questions	Statistical Analyses
RQ1: What best practices or risk management strategies were most and least used by outsourcing organizations?	Section II, Questions 1-20	Rank order the frequencies and percentages of each question and sub-questions
RQ2: What best practices or risk management strategies were most and least used by offshore outsourcing organizations that have been outsourcing longer than five years?	Section I, Question 5	Descriptive statistics and a trend analysis between the answers to the question in Section II 1-20 and Section I, Question 5

As indicated in Table 2, the frequency and percentages calculation helped answer the Research Question 1 and 2. Trend analysis on Research Question #2 provided additional guidance to answer the Research Question #2. The answers to Research Question #1 and 2 served as the basis for validating or rejecting the null hypotheses statements.

Chapter 4 presents the findings of the study and detailed data analysis that led to the answer to the two research questions. Chapter 5 presents the answer to the research question, the implications of the findings,

recommendations for future studies and course of actions for controlling and mitigating outsourcing risks.

## CHAPTER 4

### INTRODUCTION

This chapter presents the process, data collection instrument, summary of findings, and the analysis of the data. The first research question for this study was; to what extent U.S. organizations use the best practices (BP) or risks management strategies to mitigate three categories of risks inherited in outsourcing. The second question was; "do organizations that have been outsourcing longer use responsible strategies more than those that have been using outsourcing for a lesser amount of time?"

Research-based studies suggested that when organizations outsource they inherit contract, process management, and other extrinsic risks. Enlow (2006) studied failed outsourcing relationships and noted that outsourcing organizations should use responsible risk management strategies to prevent negative consequences such as failure to remain in business. Williamson (2000) indicated that the responsible strategies allowed organizations to reduce imperfect information risks that can prevent organizations from making optimal decisions regarding how well the outsourcing vendors were meeting the contract requirements. According to Fehle (2005), risks evolve with time

therefore; responsible risk management strategies should allow organizations to monitor changes continuously. Fehle (2005) indicated that since outsourcing organizations become dependent on other organizations for their resources, monitoring and adapting to changes were required strategies for organizations to control their own destiny, remain flexible, and have buying alternatives and choices. Barthelemy (2006) indicated that as time increases circumstances change for both organizations, which significantly increases the likelihood of experiencing the negative exposures. Responsible strategies such as change monitoring and knowledge and expertise retention were responsible strategies needed for organizations that outsourced for longer period. Rossetti (2005) indicated that organizations that used offshore outsourcing had a higher risk for resource waste exposures and should be required to use responsible risk management strategies more diligently.

Two research questions were asked to determine whether U.S. outsourcing organizations used responsible risk management strategies to reduce the exposures of the risks they have inherited due to their outsourcing practices. To examine the Research Question 1, to what extent

organizations used the best practices or risk management strategies, ranked ordered frequencies and percentages of Section II, Questions 1-20 listed on Appendix B was conducted. Trend analysis and ranked ordered frequencies and percentages were used to answer the second research question. The rank order frequencies and percentages of yes and no answer to Questions 1-20 only provide empirical evidence and answer the question in terms of averages and likelihood of occurrence for the population. Further analysis of the data is required to answer the research question, which is; what vulnerabilities are least and most controlled by outsourcing organizations. The analysis process used the descriptive study findings and related them with theoretical explanations to provide meaning of the finding. The framework of risk management strategies presented in chapter 3 indicated that the use of BP indicated that organizations were mitigating the exposures of outsourcing risks. These exposures were expressed in terms of resource waste and negative economic consequences for the company and the U.S. economy. Comparison of empirical findings to the framework described in Figure 2 will provide the foundation for supporting the meaning of the findings in terms of whether or not the responses to

the survey questions indicate that outsourcing organizations can prevent future economic losses for their own companies and for the U.S. economy. A two-step process was used to answer the research questions. First, data presented in the findings section helped determine if the outsourcing organizations used the framework of the responsible risk management strategy. Second, the explanation of the findings helped determine whether the exposures such as economic losses were preventable. The answer to the second-part question helped verify or reject the null hypotheses statements.

#### Description of the Process

In this section, we discuss the process used to send the online survey to the sample frame and the controls used to ensure that everyone in the population frame had an equal chance of receiving and responding to the survey questions. The sample frame of the study was large U.S. organizations that used outsourcing. The number of U.S. companies contacted and the methods and controls used to communicate to this sample frame is outlined next.

An online database, ABI/INFORM, was searched to find major U.S. companies that outsource. The search yielded a list called "U.S. companies that export U.S. jobs" (Dobbs,



2004). Since the list was several years old, the survey instrument was updated to include questions to confirm whether these companies used outsourcing. The name of the list indicated that these companies used offshore outsourcing. To ensure that these organizations were indeed using offshore outsourcing the survey instrument explained both terms. The list contained 780 names of large U.S. companies. In order to reduce the sample size, a threshold of 1000 minimum number of employees was set as the criteria to define large U.S. companies for this study. Based on this threshold, 472 U.S. organizations were selected to participate in this study. The sample frame consisted of mainly publically traded companies listed on the Fortune 500, Fortune 1000, Standard and Poor's 500, and other major U.S. organization lists.

Email was the main method of communication with the survey receivers. Each of the 472 organizations selected to participate in the study were sent an email. The subject of the email message indicated that this was an invitation for U.S. company risk managers to participate in a Ph.D. study concerned with mitigating outsourcing risks. The email message further explained the purpose of the study, obtained consent, and informed the participants

that the survey responses were being collected anonymously. Two databases were searched for the names of risk managers of these outsourcing companies. The first database was lead411.com and the second database was linkedin.com. Where an email was not located during these two searches various means were utilized to find the email address. Local chapters of audit association were also used to determine if an auditor from any of these companies could be consulted to find the email address of the outsourcing risk manager. Auditors are chartered to monitor, audit, and recommend risk management strategies for an organization. Therefore, the last strategy proved to be the most successful in finding email addresses not found on the two databases previously indicated. Almost all email addresses were located. When the above methods failed, a mail was sent to the address listed to the company at either linkedin.com or lead411.com. The mail was addressed to the Internal Audit Manager of the organization.

The surveys were sent out between November 15, 2008 and January 15, 2009. First, second, and third requests for participation were sent to the email lists before the survey was closed. No return address was included on the

mail to maintain the anonymity of this study. A message was included in each email request not to send an email back to the sender to ensure anonymity of the study. Only one traditional mail request was sent to each company. The survey was closed after the third notice was sent.

Unfortunately, only 43 responses were collected after this effort and of those only 42 responses were usable in this study. According to Johnson (2003) and as explained in the research methodology section the most important requirement for this type of study is to obtain at least 5 responses for each BP question listed on the survey instrument. On the positive side, at the close of the survey, at least 35 and up to 37 responses were obtained for each BP question. Johnson (2003) also indicated that 45 is a good sample size for this study. At the sample size of 45 and with a 95% confidence level the confidence interval would have been 13.91. For a sample size of 42 and a 95% confidence level, the confidence interval is 14.45. Getting to the sample size of 45 would have required changing the sample frame to include outsourcing companies with less than 1000 companies. Since a sample size of 42 only affected the confidence interval by half a percent, the choice was made to stay within the sample

frame and accept a lesser confidence interval for predicting results for the population.

The design and publishing of the online survey, was accomplished by using the online survey creation tools at Survey Monkey. Survey Monkey is an online survey application service provider and allows users to create, publish, and distribute the survey to the sample frame. The provider also has a database system that allows for storing, securing, and analyzing the data. Three different outsourcing companies tested the questions on the survey instrument. Outsourcing experts and research specialists at EDS, Unisys, and Tata Consultancy took the online survey and suggested various clarifications and improvements. Two responses from Unisys, 2 from Tata Consultancy, and 4 from EDS was used to improve the content on the survey instrument. Ten outsourcing consulting companies listed in the top 30 quality outsourcing companies by Outsourcing Institute, were asked to participate and only these three companies responded. After the design phase was completed, a hyperlink to the survey was created. The hyperlink was cut and pasted in the email that was sent out in each e-mail or mail to the 472 outsourcing U.S. companies in the sample frame.

Appendix B lists the 20 BP and the other general and qualifying questions that were included on the final survey instrument that was sent to the outsourcing companies.

#### Data Collection Instrument

This study used the survey research method as the primary mode of data collection. Survey research is an appropriate method for descriptive, explanatory, and exploratory studies that have individual people or organizations as unit of analysis (Johnson, 2004). The online survey questions were grouped in three sections. The first section included questions about the goals an organization was trying to achieve from outsourcing and offshore outsourcing and for how long. The second section included questions about the 20 BP that served as the framework of responsible strategies. The third section included qualifying questions such as the type of service outsourcing used, the person answering the question, the percentages offshore outsourcing. Next, a detail explanation of the different sections of the survey instrument is presented.

The first section was designed to let the subject explain their outsourcing goals and practice and collect

data about how long the organization had been using outsourcing. Barthelemy (2006) indicated that outsourcing risks increases with time and as organizations become more dependent on others for information. It was indicated that this more so when an organization used offshore-outsourcing. In order to analyze data for all types of outsourcing and be able to separately analyze BP use in offshore-outsourcing practices, two different questions regarding outsourcing goals and duration of use were asked. One of the questions asked about outsourcing and the other specifically about offshore-outsourcing.

Section II of the survey instrument listed the 20 BP questions and provided the respondents with three choices. These three answer choices were yes, no, and not applicable. The reason to include the not applicable choice was to ensure that managers were not forced to choose a yes or no answer. Since, only five responses for these BP questions were needed to conduct data analysis, the choice to use not applicable choice was used to improve the quality of the data. To further ensure that a yes or no answer was not chosen at random, additional qualifying questions were added below the BP questions.

The third section included verifying and qualifying questions. The first question in this section asked what type of outsourcing was used at the respondent's organization. This question was used to ensure that all respondents were talking about service outsourcing projects at their organizations. The next question asked about the position of the person filling out the survey. This question was asked to ensure that only qualified person was responding to the questions. The third question asked about the total percentage of offshore outsourcing vendors being used. This question was asked to ensure that individuals with knowledge about outsourcing were answering these questions.

The data collected was kept in summarized form as well as detailed individual responses in its original form at the online survey company's database. The database management system capability at Survey Monkey allowed for the viewing of the data in many ways including the ability to filter responses by different criteria. The database management system allowed the downloading of data in various format including Microsoft Excel spreadsheet. After the survey was closed the data was downloaded in excel format. The findings and the data analysis that

resulted after the data was downloaded is listed in the next two sections of this chapter.

### Findings

Of all the surveys where the respondents answered the BP questions, 91% indicated they used offshore outsourcing and most of these responses indicated that more than 50% of their outsourcing practice included offshore vendors. This seems contradictory since the sample frame included a confirmed list of companies that exported American jobs. However, research-based studies since 2005 indicated that local U.S. based outsourcing service vendors are becoming popular source for obtaining outsourcing services (Punj, 2006). Other studies also indicated that since 2005 some U.S. companies find local alternatives to failed offshore-outsourcing vendors since it is less riskier and the organizations themselves do not have the ability to bring these failed outsourced process in-house (Barthelemy, 2006). Therefore, the qualification questions asked on the survey instrument proved useful in validating that most of these organizations still used offshore outsourcing.

Next, the summary of findings related to the two research questions is listed. For research questions one and two, descriptive statistics as well as ranked order of



frequencies of responses and percentage of responses of non-use of BP is shown. A full explanation of why each BP is required is demonstrated for both research questions. In addition to the descriptive statistics analysis, trend analysis is shown for Research Question #2.

*Findings Related to Research Question #1*

Figure 5 shows the findings related to the research Question 1, to what extent U.S. organizations use and not use each of the 20 BP to manage their outsourcing risks. The first set of the two bar combination represents the total number yes response to the BP question. The second bar represents the number no responses. The tabulation of total number of yes and no responses for each BP is listed below the bars in Figure 3.

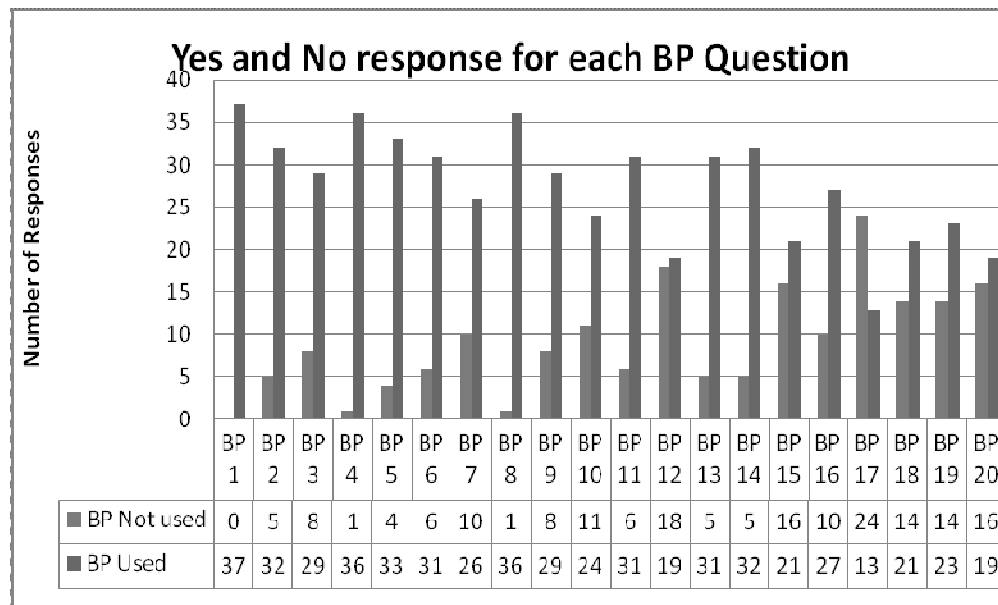


Figure 3. Summary of yes and no responses to the BP question.

To answer the research question, to what extent organizations do not use responsible strategies, ranked order of percentage of times each of the 20 BP was not used is shown in Figure 4.

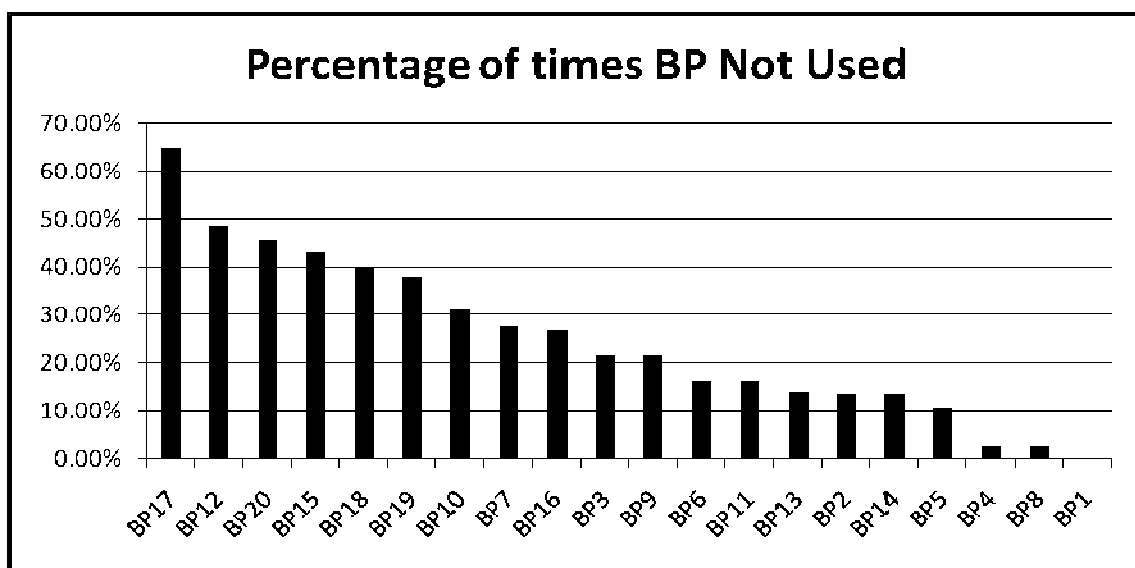


Figure 4. Rank ordered percentage of times each BP not used.

Figure four shows that according to the responses collected BP 17 was least used by outsourcing organizations and BP 1 was most frequently used. The ranked percentages of less frequently used BP are as follows: BP 17 was not used 65% of the times, while BP 12, 20, and 15 were not used more than 40% of the times, BP 18, 19, and 10 were not used more than 30% of the times. Four BPs including BP9,

BP3, BP16, and BP7 were not used more than 20% of the times. The remaining nine BPs were not used less than 20% of the time.

The same findings are further grouped according to the three categories of outsourcing risks. The first 8 BPs listed in Figure 5 are responsible strategies that reduce the outsourcing process management risks, the next set of two BPs reduce other extrinsic risks, and the remaining 10 BPs help reduce the contract management risks. More specifically, BP 17, 12, 20, 15, 18, 10, 9, and 11 are responsible strategies required to manage process risks. BP, 13, and 14 are related to mitigating extrinsic risks. The other remaining 10 BPs are required to mitigate contract management risks.

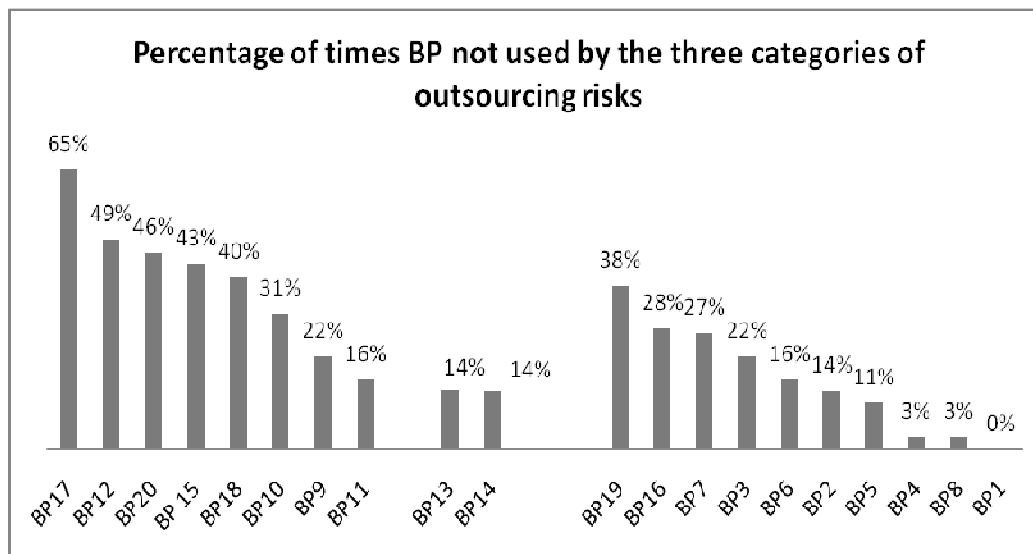


Figure 5. Percentage of BP not used grouped by risk category.

Descriptive statistic calculations in table 3 show the mean times of non-use of BP by all respondents. In addition to the mean, the percentile rank for percentage of time BP and the number of BP that were within 1.5 standard deviations from the mean for each BP was also calculated.

Table 3.

*Mean, Percentile Rank Calculation for BP Not Used*

Category of outsourcing risk	Mean	Percentile rank calculation (90, 80, 50)	Within 1.5 std. dev. From mean
Process management	39%	55%, 48%, 40%	6 out of 8 BP
Contract management	16%	28%, 27%, 10%	9 of 10 BP
Extrinsic	14%	.13852, .13814, .137	2 of 2

For each category of outsourcing risk the ranked orders from highest to lowest in terms of percentage of times BP not used is shown in Table 4, 5, and 6 below. Aczel (2006) indicated that grouping data helps facilitate the organization and explanation of large amounts of data in smaller groups. Along with ranked order of percentages

of least frequently used BP, an explanation is provided regarding what risk the BP reduces.

Table 4. *Percentage of Times BP Required to Manage Process Risks Was Not Used*

<u>The objectives related to using each of the 7 BP required to manage outsourcing process risks</u>	<u>% BP Not used</u>
BP 17: The use of BP 17 ensures the smooth transition of a failed or less-than satisfactory outsource service project (Barthelemy, 2003).	64.86%
BP 12: Retaining expertise and knowledge of outsource services ensures that the organization does not lose the ability to keep up with changes, improves change management (Enlow, 2006), and can adequately measure vendor performance (Punj, 2006).	48.65%
BP 15: Dividing the risk between different vendors and not becoming too dependent on one vendor ensures the ability to pull out unsuccessful projects or segments of a project away from one vendor (Fehle, 2005). According to Williamson, (2000) this can help prevent moral haggling.	43.24%
BP20: Barthelemy (2006) indicated that failure to have a general plan makes it difficult to determine how outsourcing affects other processes and having a general plan shows that an organization has deliberately planned their outsourcing efforts.	45.71%
BP 18: Retraining existing staff ensures the internal processes are still coherently run and enables appropriate change management of skills sets required to manage the changed processes (Enlow, 2006).	40.00%
BP 10: Having dedicated staff to manage the various steps of the outsourced project assures consistency, improves relationship management, and improves communication effectiveness (Bielski,2006)	31.43%
BP 9: Vendor training reduces the chance of miscommunication (Koh, 2004). It also transfers necessary organization information to the provider and reduces uncertainties about buyer needs (Tompkins, 2005).	21.62%
BP 11: Coherently integrating the outsourced processes with internal process allows for the coordinating of the efforts between and ensures the timely receipt and delivery of inputs and outputs from and to service	16.22%

providers (Enlow, 2006).

Table 5. Percentage of Times BP Required to Manage Extrinsic Risks Were Not Used

The objectives related to using each of the 7 BP required to manage outsourcing process risks	% BP Not used
BP 13: The use of BP 13 allows the organization to evaluate the impact of outsourcing on the organization's confidentiality, privacy and security of information in terms of customers' privacy, confidentiality and security rights.	14.29%
BP 14: The use of BP 14 ensures that the outsource provider's data privacy, confidentiality and security policies and procedures are acceptable before signing contracts	12.89%

Table 6. Percentage of Times BP Required to Manage Contract Risks Were Not Used

The objectives related to using each of the 11 BP related to managing the outsourcing contract:	BP not used
BP 19: Monitoring vendor technical skills and changes in financial abilities ensures that changes in vendors and financial abilities are still aligned with the organizations goal and the contract terms (Enlow, 2006). It is suggested that while BP 1 and BP 2 are implemented before the start of the contract, BP 19 is required on an ongoing basis to ensure quality of services and ability of vendor (Kakabadse, 2004).	37.84%
BP 16: Specific and measureable goals help organization determine what objectives are they trying to achieve in outsourcing and be able to measure the success of their outsourcing practice (Kakabadse, 2003).	27.78%

BP 7: Writing detailed specification and project requirements allows the buyer to determine exactly what they are paying for and sets expectations for the vendor regarding what they need to be deliver to the buyer (Punj, 2006)	27.03%
BP 3: Writing "well-defined" scope prevents unfair and unnecessary haggling and negotiation by buyer, reduces project misunderstanding and reduces complexity, enables the buyer to determine exactly what they are paying for (Williamson, 2003).	21.62%
Bp 6: Specifying in the contract the organization's right to change the specifications establishes the organizations right to change and improves the organization's ability to change with changing needs of the organization (Enlow, 2006).	16.22%
BP 2: Verifying vendor has financial resources provides assurance that vendor has the financial resources to acquire skilled resources and make necessary investments in operations to meet the buyers needs (Willcocks, 2006). It was indicated that BP 2 is only effective is subsequently BP 19 is implemented.	13.51%
BP 5: Writing in the contract that the buyer has the right to monitor and measure enforces the buyer's right to monitor and measure contracts and control their contracts and their own destiny (Koh, 2004).	10.81%
BP 4: Stating in the contract that the buyer has the right to terminate the contract allows the buyer to set terms for exist and replacement and right to control destiny (Koh, 2004)	2.70%
BP 8: Monitoring the vendor's performance provides assurance that the buyer is receiving what they were promised. Measuring improves timely information about performance and its effects on other processes (Barthelemy, 2003; Punj, 2006).	2.70%
BP 1: Determining the vendor has the technical skill set provides assurance that vendor has the technical skills needed to perform the services (Willcocks, 2006).	0.00%

*Findings Related to Research Question #2*

The purpose of asking the second research question was to determine whether organizations that had been outsourcing longer than 5 years and used offshore outsourcing used responsible strategies. To answer the question only respondents that used offshore outsourcing were included in the data analysis. The reason to study offshore outsourcing separately is because Willcocks (2006) indicated that due to the long distance nature of offshore-outsourcing more risks are inherited. In offshore outsourcing, additional risks were inherited because of the social, political, and other cultural difference present when offshore vendors are used. Rossetti (2005) indicated that time was another factor that increased the inherited risk because financial and technical capabilities of vendor or provider organizations change over times. Of the 34 qualified offshore-outsourcing responses, 16 responses indicated that they had been using offshore outsourcing for less than 5 years and 18 indicated that they had been outsourcing for more than 5 years. To present the findings for Research Question #2, Question #5, Section I in Appendix B, and Question, #6 1-20 BP questions were used.



Descriptive statistics and a simple trend analysis are shown in Table 7, and Figure 7, respectively.

Table 7. Mean and Percentile Calculation for Question #2

Number of BP used	Mean Offshore- Outsourcing	Percentile rank calculation (90, 80, 50)	Within 1.5 std. dev. From mean
All	14.62	18, 17.4, 14.5	27 of 34
Less than 5 years	14.37	17.5, 17, 14.75	13 of 16
More than 5 years	14.83	18.5/18/ 14.5	15 of 18

As indicated by Harrison (2007), offshore-outsourcing carries higher risks and therefore risk management strategies become more critical. In addition, Fehle (2005) indicated that with time the risks increase and therefore it becomes even more critical to use the framework of risk management strategy more responsibly.

Figure 6 shows the trend for using number of BP for offshore-outsourcing as the time of off-shoring use increases. The x-axis shows the number of respondents and the y-axis shows the number of BP used. The first 16 responses shown on the x-axis are for those companies that used offshore outsourcing between 0 and 5 years. The data shown for the remaining 18 responses indicate the BP use for offshore outsourcing users that have been outsourcing for greater than 5 years. The lower line in the graph shows

the number of years the organization used offshore outsourcing and the upper line shows the number of BP the organization used.

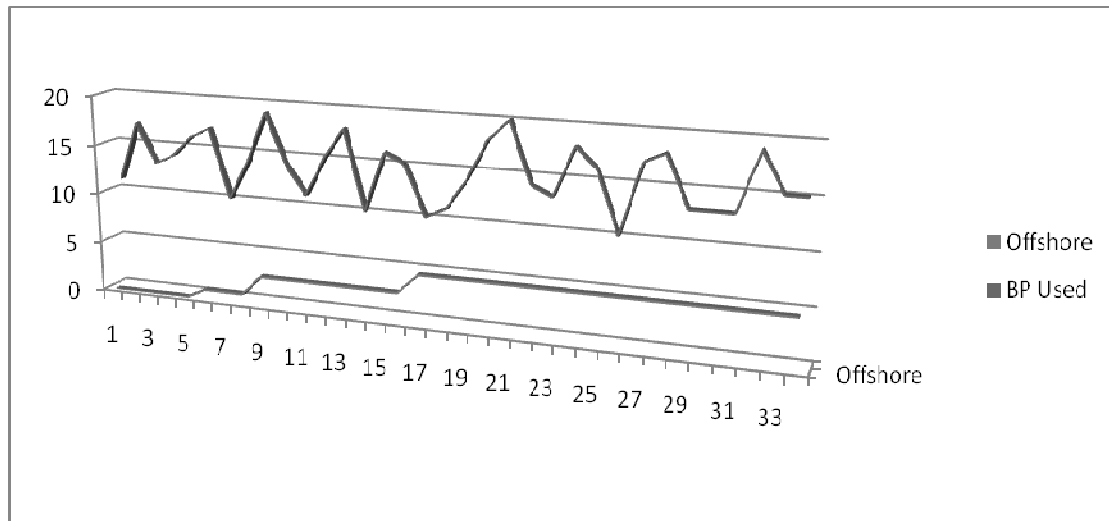


Figure 6. Trend in BP use as time of outsourcing increased.

According to Fehle (2005), risks are evolving, and therefore risk management strategies that allow organizations to monitor changes and take actions to replace or terminate contracts become critical. Of the 20 BP in the framework of responsible risk management strategies, BP 6, 10, 12, 15, 17, 18, 19, and 20 are practices that allow an organization to monitor changes and keep up with change management needs. The findings for these 8 BP showed that organizations that outsourced for more than 5 years on the average did not use 4.3 of the 8 BP. In other words, less than 50% of the required BP were

used by organizations who had inherited risks that exposed them to an increased likelihood of exposures such as economic loss. Organizations that had been outsourcing for less than 5 years on the average did not use 3.5 of these eight BP. In other words offshore outsourcing organizations with a lesser exposure of economic loss also did not use the required BP for inherited risks. Figure 7 presents another view of this finding. Figure 7 shows the list of all 34 offshore-outsourcing responses for these eight BP questions. For each response, the percentage was calculated by using the number of BP not used divided by 8.

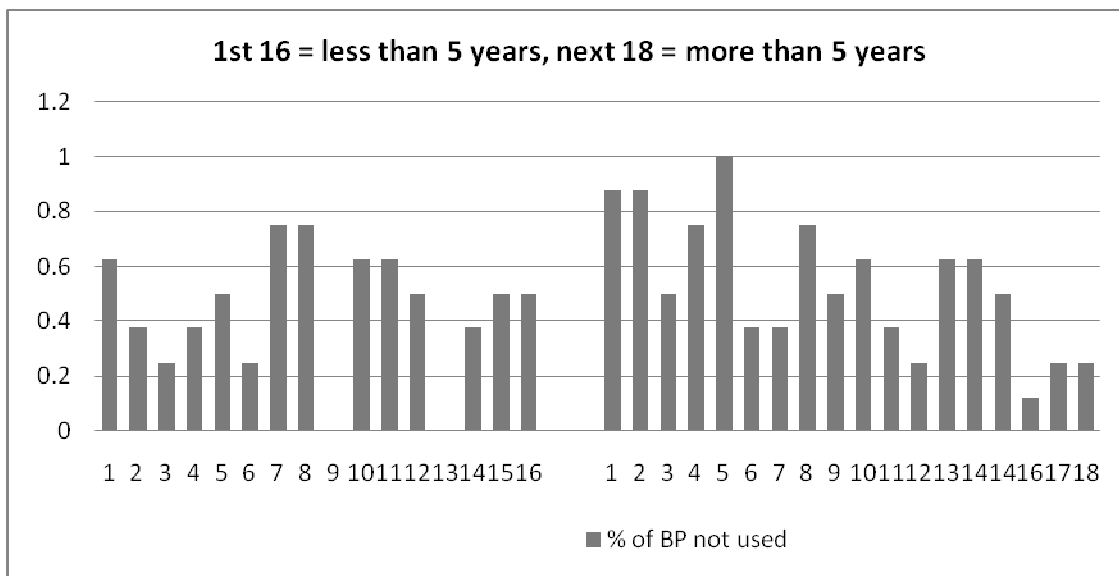


Figure 7. Percentage of times the 8 BP were not used.

Since it was indicated by Fehle (2005) that with time the use of the responsible strategies related to change

monitoring and change management becomes a necessity, the percentage of non-use of each of the 8 BP for organizations that had been outsourcing for longer than 5 years is presented in figure 8. The percentages in figure 8 was calculated by the total number of no responses for each of the 8 BP. Figure 8 shows that 72% of the responses indicated that BP 17 was not used. Other findings show that 61% of the times BP 15 was not used, 44.44% times BP 12 and 19 were not used, and 37.5% times BP 18 was not used.

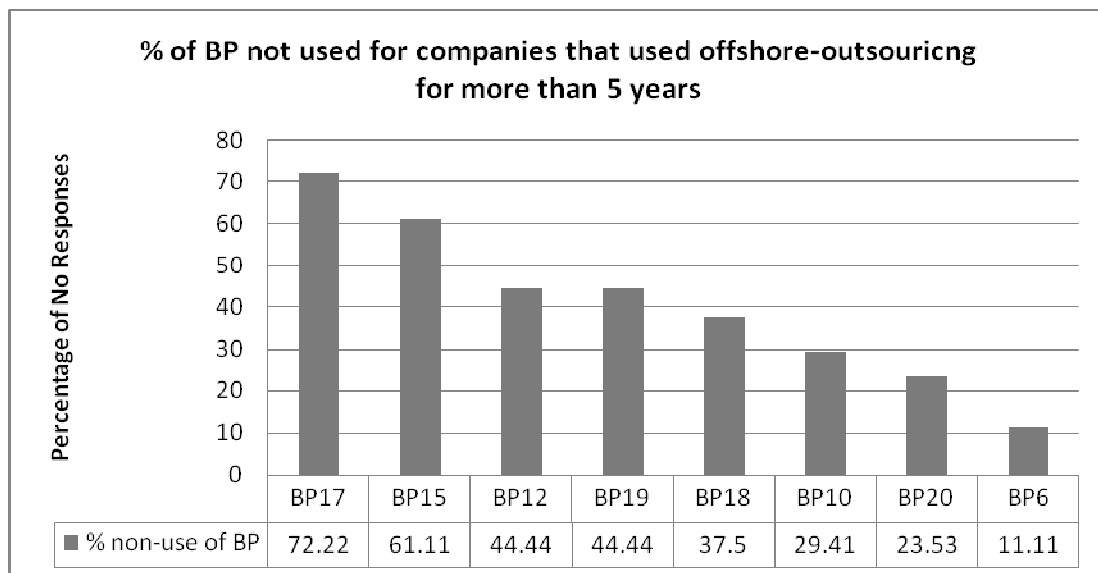


Figure 8. The percentage of non-use of each BP

#### *Summary of the Findings*

The finding section included the summary of the data collected and presented the ranked order frequency of no answers to each BP question asked along with the ranked order percentages of these no responses. Descriptive

statistics calculation helped answer the research question #1 and #2. In order to explain the meaning of the answers to the research questions, the answers to the 20 BP questions were organized according to the three categories of outsourcing risks. The trend analysis of increase in time versus the number of BP not used helped describe the findings related to the second research question. Ranked order frequencies related to eight specific BP related to Question #2 along with the trend analysis further allowed for the explanation of the meaning of the findings in terms of whether or not U.S. organizations that use offshore-outsourcing and for longer than 5 years reduce the potential of economic losses.

The data analysis section further discusses the meaning of the descriptive statistics, the ranked order frequencies of how often the BP were used and not used, and the findings in terms of answering the two research questions.

#### Data Analysis

In this section, the data presented in the findings section was analyzed to first answer the research question and then provide meaning to the two research questions. The first research question was, "to what extent organizations

use the framework of responsible risk management strategies to mitigate their outsourcing risks"? The second research question was, "do organizations that use offshore outsourcing and have been outsourcing longer, use the framework more to keep with the increasing risks"?

To answer the research question the explanation of the descriptive statistics is provided. The descriptive statistics by itself is not as significant in explaining how the findings answer the question or the implications of the answer. The descriptive statistics calculation and an explanation of the individual category of the multiple categories of best practices that constitute the framework of risk management strategy is required to answer both research questions.

Aczel (2006) explained that when many related variables are studied, organizing the data and explaining them in related groups of ideas helps facilitate data interpretation. The purpose of the study was to determine if outsourcing organizations' practices indicate that they have adopted a framework of responsible strategies to manage the outsourcing risks that they have inherited. Providing an answer to both research questions will help meet the objective of this study. To provide further

meaning and clarify the framework of responsible strategies concept, it is important to establish the relationships between the outsourcing contract, process management, and extrinsic risk.

A contract is created to manage the relationship between the two partners in any contract-based relationship (Williamson, 1999). According to Barthelemy (2006), contract risk management practices should include qualifying the vendor, clearly specifying the buyer's needs, including termination criteria and monitoring rights, and clearly stating the performance requirements. BP 1, 3, 4, 5, 6, 7, 8, 16, and 19 were all BP related to responsibly reducing the risk related to the management of the contract. The outsourcing process risks arise because outsourcing creates process disintegration and gaps. Best practices related to process management are natural steps needed to re-integrate and fill the process gaps (Punj, 2006). The gap management can include creating new processes (Heidi, 1994) or as Fehle (2005) indicated simply having knowledge, expertise, and ability to dynamically make timely and optimal decisions to minimize negative impacts. Retaining in-house or hiring outside expertise, retraining existing staff to fill the gaps, having good

plans, knowing when and be ready to exist and replace, and monitoring changes are responsible strategies indicated by Fehle, Punj, and Enlow (2006). BP 2,9, 10, 11, 12, 15, 17, 18, and 20 consists of the list of responsible strategies that help organizations manage the outsourcing process risks. Weiss (2007) indicated that included in the list of inherited risks in outsourcing are the potential loss of data and information privacy, security, and confidentiality. BP 13 and BP 14 were best practices in the framework of responsible strategies to reduce these extrinsic risks.

#### Data Analysis for Research Question #1

##### *Descriptive Statistics Explanation*

The mean is the most valuable descriptive statistics for analyzing the use of multiple variables to provide a summary number of observations (Aczel, 2006). The mean value of BP not used for the management of outsourcing process risk was almost 39%. This indicates that on an average almost 39% of outsourcing companies don't use the BP that help responsibly control the risks related to outsourcing process management. Of the eight BP questions on the survey related to process management risks 6 out of the 8 BP or 86% based on simple empirical rule fell within



1.5 standard deviation of the mean value of 39%. Fiftieth percentile of all no responses for this category of risk was 40%. On the contrary, the average mean for BP not used for outsourcing contract management and extrinsic risks were 16%, and 14% respectively. The answer to the research Question 1 therefore is that organizations use BP to reduce contract management and other extrinsic risks more often than they use them to reduce the process management risks.

The implications of the non-use of BP at an average rate of 39% for all respondents are further explained by the use of the various theories that guided this study.

*Detailed Explanation the non-use of BP Related to Process Management Risks.*

As noted in the findings section, BP 17 was indicated as not being used by 65% of the respondents. Comparing the use of BP 17 and cross referencing this practice with other BP within and across the two categories of risks will help explain the meaning of this finding in terms answering the research question and help provide detailed analysis of the data. Table 9 outlines the implication of 65% no responses to BP 17 and lists other BP related to process management risks and contract management that either affect or are affected by the non use of this BP.

Table 8

*Findings Related to BP 17 and Other Related BP*

BP 17: 65% times not used	Related Process Management BP	Related contract management BP	Implication of these relationships
BP 12 - 49% not used		BP 4 and 8: used 97%	97% use of BP4 and BP 8, and 90% use of BP 5 indicate that most organizations' contracts specify the right of the organization to monitor and measure the performance of the vendor and right to terminate the contract. However, 65% of the times these organizations do not have a plan to terminate and replace the vendor or use BP 17.
BP 18 - 40% not used (BP 10 is affected if 12 or 18 are missing)		BP 5: used 90%	
BP 10 - 32% not used.			
BP 20: 46% not used			
BP 15: 43% not used			

The Implication of not using BP 17 can be explained by reviewing the dynamic risk management theory that guided this study. According to Fehle (2005), dynamic risk management formulas should include optimal timing to initiate risk management contracts, early termination, and the replacement of expiring and terminated contracts, contract maturity choice, and frequency of adjustment. Implementing BP 17 provides organizations with the ability

to have a planned exit that can facilitate the smooth transfer of the outsourced service either in-house or to another outsourcing vendor. Ferle indicated that this strategy reduces the unnecessary interruptions to the business and customer service and reduces less-than-optimal and unplanned decision-making. Since 65 percent of respondents indicated that BP 17 was not being, this shows that most outsourcing organizations do not have the responsible strategies to optimally time terminations and replacements of expiring or terminating contracts.

Ferle (2005) also indicated that spreading the risks around by having different contracts placed with different companies or departments within a company makes it easier to terminate and replace underperforming providers, help with contract maturity choices and allows for frequency of adjustments. BP 20 tested whether the organizations had a general plan to help with the transitions or the adjustment. Forty-five percent of the respondents indicated that they did not have a general outsourcing plan. The dynamic risk management theory also stated that organizations should have the ability, knowledge, and expertise to monitor their needs. Forty-nine percent of the responses indicated that they did not retain in-house or

hired outside expertise. With as many as 49% of outsourcing organizations that do not retain the knowledge and expertise and 45% without a general plan this exposes the organization to imperfect information and less-than-optimal decision making (Williamson, 1999). The resource dependency theory further explained why dependent organization's need to exercise various means to minimize their own dependencies by creating other relationships (Pfeffer, 1978). BP 15 tested to see if outsourcing organizations used this practice. Forty-three percent of the respondents indicated that they did not use BP 15. With as high as 65% responses indicating the non-use of BP 17 and 43% not using BP 15, according to the dynamic risk management principles outsourcing organizations are not ensuring optimal contract maturity choices and frequency of adjustments to keep up with termination and replacement requirements.

The findings that 49% organizations don't retain expertise or knowledge to estimate the change needs of outsourced services, and that 40% times organizations don't monitor changes also indicates that organizations do not consider the risk of failed outsourced relationships in their outsourcing risk management formula. The implication of 49% non-use of BP 12 can be explained by reviewing the

control principles explained in Chapter 1. Retaining and having the expertise is required to monitor the outputs according to the terms established in the contract (Aulack, 1996), and terminate smoothly without interruption to the organizations' input supply or total process (Heidi, 1994). Willcocks (2006) referred to the failure for the organization to retain knowledge and expertise or retrain internal resources as creating a "disintegrated franchise". Enlow (2006) called organizations without knowledge of the outsourced process as a "hollow organization". With as many as 49% of the outsourcing organizations without the knowledge or expertise to monitor changes or adjust to changes it can be stated that U.S. outsourcing organizations are at risk of becoming disintegrated and hollow organizations.

An alternative strategy to minimize this risk, become capable of monitoring inputs and outputs, and keep up with changes is to use BP 10. Thirty-two percent of responses indicated that they did not use BP 10. BP 10 requires the use of dedicated staff to measure the performance of the vendors. According to Ferle (2005) initiating a risk management contract, or using good practices to manage contract risks, is just one component of the risk

management formula. In other words, the framework of risk management strategy is made of several components and each component has an important role in reducing the outsourcing risk. With 49% organizations without knowledge and expertise even in the case of 68% that do have dedicated staff that monitor the performance of the vendors, it is not likely that the quality of the monitoring is good. In other words, even if outsourcing organizations used BP 3, 4, and 8 frequently to manage the contract risks, the infrequent of BP 17, 12, and 18 makes the risk management formula less effective.

The framework of risk management strategies has 20 components and each component plays an important role in reducing the overall outsourcing risk. Therefore, responses to the BP questions cannot be viewed in isolation. When results such as 65% times non-use of BP 17 or the practice of having exit plans is compared with 97% times use of BP 4 or the right to terminate a contract is included in the contract, Fehle (2005) calls this an inadequate risk management formula. Therefore, when the framework of risk management strategies are considered the data shows that outsourcing organizations are not reducing their inherited risks responsibly.

Given the descriptive statistics conducted on the data, the null hypothesis  $H_{01}$  is rejected. The findings from this study does not indicate that U.S. organizations that have inherited outsourcing risk use the framework of responsible strategies needed to control the exposures such as ineffective and inefficient processes, business interruptions, and unnecessary economic losses. While the data shows that organizations used some components of the framework of risk management strategy, it was indicated that the presence of multiple risks requires the use of multiple best practices. The failure to use multiple responsible strategies demonstrated that the negative exposures of inherited as a result of outsourcing practices of U.S. outsourcing organization such as economic loss is not controlled.

#### Data Analysis for Research Question 2

Given the reduced transparency in offshore-outsourcing relationships, more risks are inherited in offshore-outsourcing (Enlow, 2006). Barthelemy (2006) indicated that as time increases the risks increases due to changes that can occur at both organizations. The BP that allowed organizations to keep up with changes included BP 6, 10, 12, 15, 17, 18, 19, and 20. Data summarized in Figure 8

showed that 72% of the responses indicated that BP 17 was not used by the 18 companies that had been using offshore-outsourcing for more than 5 years. Other findings show that 61% of the times BP 15 was not used, 44.44% times BP 12 and 19 were not used, and 37.5% times BP 18 was not used.

In order to dynamically control risks and keep up with changing needs the outsourcing organization needs to adopt those strategies that allows them to monitor changes in the vendor's company, and keep up with the knowledge and expertise requirements to effectively monitor progress, negotiate new terms, or even plan the exit strategies (Fehle, 2005). The data analysis for question #1 showed the implication of non-use of BP 17, 15, 12, 19, and 18. In the case of offshore-outsourcing users that had been outsourcing for longer than 5 years, all responsible risk management strategies were used even less than all outsourcing relationships. Two significant differences were the non-use of BP 17 and BP 15, which are both needed according to the dynamic risk management theory to make timely and optimal termination and replacement decisions. The non-use of BP17 was 72% instead of the 65%, the non-use of BP 15 was 61% instead of 43%. The fact that these two BP are required to make the necessary adjustments to non-



performing vendors and the risk of non-performance grows with time; a decrease in the non-use of the two BP shows irresponsibility.

The lack of use of BP 18, and 12 in more than 40% and up to 48% of the cases indicates that a lot of U.S. based outsourcing and offshore outsourcing have been stripped off the required knowledge and expertise for more than five years. These practices are needed to keep up with ongoing changes and be prepared to make quick termination decision choices (Fehle, 2005). The 30% non-use response for BP 19 indicates that for over 5 years 30% of the outsourcing companies have not monitored the outsourcing vendors' technical skills sets and financial capabilities. Given the rate of deterioration of the financial conditions of companies worldwide, this indicates that most organizations are not just vulnerable to interruptions due to their own weakened financial conditions but also at risk of further unplanned interruptions to their business. As stated earlier, Willcocks (2006) stated that U.S. organizations that use offshore-outsourcing and do not retain knowledge and don't monitor changes can become disintegrated and hollow organizations.

The findings listed for the research Question #2, indicated that (1) offshore-outsourcing organizations do not use risk management strategies more responsibly with time, and (2) the use of strategies that are mostly needed to keep up with growing risks that are inherited as a result of time are not used more often. Given that no changes were noted in the use or non-use of responsible strategies for organizations that had outsourced for longer than 5 years and less than 5 years, it can be said that U.S. organizations that have been offshore-outsourcing for over 5 years are vulnerable or at risk of becoming hollow and disintegrated organizations.

As a result, null hypothesis  $H_{02}$  has to be rejected. Organizations that use offshore outsourcing and for longer than five years do not control their risk exposures. The analysis of the findings from this study does not indicate that organizations that use offshore outsourcing for more than 5 years use a framework of risk management strategies to reduce all risks inherited in outsourcing. With growing time as risks of economic loss increases, there is no change in the risks management strategy behavior or U.S. organizations that outsource. These findings indicate that the extent to which U.S. organizations use risk management

strategies does not indicate that the exposures of economic losses is being controlled.

#### Chapter Summary

This chapter presented the process of data collection, the data collection instrument, findings, and the data analysis section of this study. The purpose of collecting the data, designing the data collection instrument, summarizing the findings, and analyzing the data was to find the answer the two research questions that guided this study. The first research question was asked to determine whether U.S. outsourcing organizations used a framework of responsible strategies to mitigate the risks inherited in outsourcing. The second research question was asked to determine if organizations that had been using outsourcing for a longer than 5 years used the framework more responsibly to keep up with changes and new risks.

To answer the two research questions, the data collected was first summarized and listed in the finding section of this study. The research question, what BP was most and least used by outsourcing organization was summarized in an excel spreadsheet after the data was downloaded from the database located at Survey Monkey's

database server. After the download, the data was sorted according to the ranked ordered frequencies and percentages of the number of responses to the 20 BP questions listed in Appendix B, Section II. The data was presented first by listing the number of yes and no responses for each of the 20 BP questions listed on the survey instrument. The yes responses indicated that the organization used the BP or the strategy. The no responses indicated that the organization did not use the required BP. The responses were grouped by process management, contract management, and extrinsic category of risk. All data for each category of risk was ranked by the frequency of occurrence based on the percentage of no answer or non-use of each BP question included in the survey instrument. Basic descriptive statistical analysis was conducted on the data and these statistical calculations were included in the finding section. To answer the second question the responses to the number of years outsourcing was used at the organization in Section I, Question #5 was totaled. Question #5 asked the total number of years the organization had been using offshore-outsourcing. Descriptive statistics analysis was conducted on the data

collected and the answers were included in the findings section.

The data analysis section first explained the calculated descriptive statistics in terms of how it answered the research questions. In addition to the descriptive statistics, to answer research Question #1, the findings were compared to the theories that guided this study. For example, the mean value of 39% indicated by the descriptive statistics calculations for all process management related BP was first explained. Following the descriptive statistics explanation of the mean calculation, further explanations were offered to provide meaning of the no answers in terms of the explanations offered in the theoretical framework that guided this study. To answer the second question, the descriptive statistics, and the trend analysis was first explained. Next, the ranked ordered frequencies of the non-use of BP most appropriate for the risks related to time and change over time were once again discussed. Limited cross-functional analysis of data was conducted to show the implications of one risk in the framework on another risk within this framework.

The next chapter of this study summarizes the study, provides a conclusion, makes recommendations for future

research work, and discusses the social implications related to why organizations should use responsible risk management strategies to manage their outsourcing risks.

## CHAPTER 5

### CONCLUSION, RECOMMENDATION and SOCIAL CHANGE IMPLICATIONS

#### Introduction

In this chapter, a summary of the findings, the conclusion of the study, the recommendations, and implications for social changes is stated. The problem statement and the research questions stated in chapter 1 guided the literature review, research methodology, and the data collection and analysis of this quantitative study. The data analysis and the findings section from Chapter 4 served as basis for the conclusions reached, and the recommendations made in this chapter.

The summary section restates the purpose of the study, the research questions, the methodology used to conduct the study, and what was discovered because of this study. The conclusion section is a summary of the implication of the findings in terms of whether U.S. organizations using outsourcing control the risks they have inherited. The recommendation section includes a list of potential future research that can further clarify the problems and exposures of uncontrolled risks in outsourcing. The social impact section states the impact of the findings from this

study on the U.S. economy as well as the future welfare of U.S. citizens.

### Summary

The purpose of the study was to determine to what extent U.S. organizations that form outsourcing alliances use responsible strategies to reduce the risks they inherit. Two research questions guided the study. The first question was, "what responsible strategies were most and least used by outsourcing organizations?" The second question was, "do organizations that have been using outsourcing longer use responsible strategies to keep up with changing risks. Descriptive statistics and other exploratory and explanatory data analysis method were used to answer the research questions.

For the purpose of this study, responsible outsourcing risk management strategies indicated in different studies were compiled to form one list of 20 best practices (BP). These 20 BP were called the framework of responsible risk management strategies. According to Aczel (2006) when a study has many variables further sub-grouping is helpful in organizing the study. Since there are three categories of outsourcing risks, the 20 BP were further grouped according to the type of risks the strategy helped reduce. According



to the literature review, contract management, process management, and extrinsic factors such as privacy, confidentiality, or security of data were three different categories of risks inherited by outsourcing organizations. Therefore, each of the 20 BP was associated with one of these three categories of outsourcing risks.

Survey research method was used to collect the data to answer the two research questions. Both descriptive statistics and theoretical framework that guided the study were used to analyze the findings of the study and determine the answer to the research questions. The resource dependency theory, the dynamic risk management theory, and the control principles provided the basis of the conclusion reached for this study.

#### Conclusion

The conclusion for this study is the answer to the research questions. The answer to the first question is that the data collected for this study showed that BP related to managing outsourcing process risks were least used by U.S. organizations. These BP were explained by the dynamic risk management theory as needed to continually monitor and reduce knowledge and expertise loss, remain in control of one's one destiny, and remain flexible and

prepared to make optimal decisions about outsourcing relationships and benefits (Fehle, 2005). Next, it was shown in this study that while outsourcing organizations used most of the BP needed to reduce the contract management risks inherited in outsourcing, the BP related to ongoing monitoring of changes in the contract was not used. On a positive note, the data obtained did not support the claim that Weiss (2007) made. Weiss indicated that outsourcing organizations did not adequately mitigate privacy, confidentiality, and security of data or extrinsic risks associated with outsourcing. The findings from this study indicated that 86% of the times organizations did mitigate this category of risk.

The answer to the second research question is, while risks increase with time the data collected in this study indicated that outsourcing risk management practices remained unchanged for organizations that used offshore outsourcing for more than 5 years. In other words, data collected during this study did not show that organizations that have been using offshore outsourcing for longer than 5 years used risk management strategies more responsibly than the organizations that had been offshore outsourcing for less than 5 years. The data analysis showed that the

strategies most needed to reduce risks associated with long-term outsourcing were less often used.

The first concluding statement refers to the lack of use of BP 17. Outsourcing organizations should use BP 17 to responsibly plan exit strategies, establish orderly replacement and termination plans, and improve their flexibility to choose between methods and negotiation terms for replacements (Fehle, 2005). The use of BP 17 also responsibly reduces the exposures of failed and underperforming contracts (Enlow, 2005). Analysis of data indicated that 65% of the respondents in this study do not responsibly reduce the risks of failed or underperforming outsourcing contracts. This irresponsibility shows that most U.S. based outsourcing organizations do not have a planned and optimal timing for orderly termination and the replacement of expiring and terminated contracts. Failure of outsourcing vendors and even doubt about the legitimacy of some of the offshore outsourcing vendors has been shown as a reality of outsourcing (Leahy, 2009). Given recent financial and economic crises leading to business failures all around the globe, the exposures related to the lack of use of a planned exit strategy can leave organizations stranded for inputs needed to meet their operational goals.

While contract management risks were shown in this study to be mitigated most of the times only 70% of the organizations used BP 19 that ensured that vendor's financial and technical skill capabilities were monitored after the contract was signed. This finding should be analyzed with the prior finding. For the 65% of the organizations that did not have any termination plans given the fact that almost 30% don't even monitor their outsource vendor's financial and technical skills indicates that at least 30% of all outsourcing organizations are vulnerable to imperfect information. The risks associated with imperfect information are the inability to make optimal decisions and falling prey to moral haggling (Williamson, 1999).

Even more dire conclusions can be reached when the above exposures are combined with the fact that almost 50% of the organizations do not retain in-house or external expertise to keep up with the changes that can occur overtime in the outsourced area. Besides not being able to make optimal contract maturity choice, (Ferle, 2005) lack of knowledge and expertise exposes these organizations to what Willcocks (2006) calls hollow organizations and disintegrated franchises. According to Cascio (2007), this

exposure reduces the ability of U.S. companies to pursue better alternatives and find less costly options. A compensating control for not retaining knowledge and expertise of the outsourced services was retraining existing staff to manage the changes that occur because of outsourcing. Almost 40% of the organizations in this survey study indicated that outsourcing organizations do not retrain their existing staff to deal with the changes related to the outsourced services.

Currently, there is mounting evidence that outsourcing companies such as Satyam in India, fraudulently show the existence of employees, skills, and financial strength (Leahy, 2009). Given the potential of these types of misrepresentation, U.S. outsourcing companies should use BP 17, 12, 18, and 19. The data from this study indicated that more often than not resource dependent organizations did not use BP 17, 12, 18, and 19. In the case of Satyam, Leahy indicated that highly respected Auditors work did not find certain unethical practices at the outsourcing vendor. Given this finding, loss of internal knowledge and expertise expose current outsourcing U.S. organizations to total loss of ability to control their destiny. Harrison (2006) noted that offshore outsourcing as a practice has

reduced the number of jobs for U.S. employees. If the risk management strategies that require the retention of knowledge and expertise of outsourced service or retraining of existing staff in new skills are not used responsibly, further reduction in knowledge base can also be anticipated.

A quick review of the answers to Research Question #1 allows us to reach this conclusion: U.S. outsourcing organizations do not use responsible risk management strategies to reduce the outsourcing process risks. As a result, these organizations have become vulnerable to moral haggling and less than optimal outsourcing decision-making (Williamson, 1999). This irresponsibility has stripped the organizations of internal knowledge and expertise needed to monitor and manage changes (Sheng, 2006). Furthermore, failure to use responsible risk management strategies to reduce process management risks have reduce their ability to make planned decisions about optimal contract timing (Fehle, 2005). The exposures, given the current economic conditions in the U.S. and around the globe, can lead to unnecessary resource waste and lead to further economic problems.

The findings related to research Question #2 is similar to the first one. That data collected and analyzed during this study did not indicate any difference in the use of responsible risk management strategies for organizations that had been offshore outsourcing for over 5 years compared to those that had been outsourcing for less than 5 years. The responsible strategies needed to reduce the risks that arise with the passing of time were shown in many cases as being used even less. Strategies that allowed the organization to plan for smooth transfers and exist or spread the risk across different outsourcing vendors were not used in 75% and 61% respectively by the organizations that responded to this study. Therefore, the responsible strategies that were most needed to prevent organizations from becoming hollow and disintegrated were not being used by organizations that had been offshore-outsourcing for more than 5 years. The other strategies needed to keep up with changes were shown as not being used as well.

The extent to which U.S. organizations are not mitigating some of the risks they have inherited can cause multiple negative outcomes such as failure to operate as a coherent, effective, and efficient organization. Failure to control outsourcing risks can leave outsourcing

organizations incapable of providing their core functions and suffer significant economic losses. These irresponsible practices expose outsourcing organizations to (a) waste of valuable resources, (b) reduced competitiveness, and (c) business interruptions. Business interruptions can lead to customer dissatisfaction, which is counterproductive in a highly competitive global marketplace (Modarress, 2007). Offshore outsourcing has already relocated jobs that were once performed in the U.S. (Harrison, 2006). Given the findings in this study, it can be added that U.S. organizations that outsource are also becoming vulnerable of losing knowledge and expertise it once possessed.

#### Recommendations

According to Chopra (2004), operational alliances such as outsourcing relationships are important to become competitive, but much research was needed to demonstrate what strategies are needed to effectively control the problems that arise because of these alliances. This study attempted to gather data from various sources, compiled, and tested a framework of responsible strategies using survey research. Survey research method used to test this



framework demonstrated several weaknesses in the current outsourcing risk management strategy practices.

Since 2004, a lot of research has also been dedicated to understand the outsourcing dilemma. Those studies have proven significant loss in terms of unmet goals (Harrison, 2006), net financial resource loss (Barthelme, 2006), and major business interruptions (Enlow, 2006). This research study established that there is a gap between the framework of responsible risk management strategy suggested by research and the practices currently used by outsourcing organizations. In order to reduce these gaps U.S. organizations should maintain internal knowledge and expertise of the outsourced service, plan replacements and termination of underperforming contracts, monitor changes and be capable of making optimal decisions. This study therefore, provides a starting point for organizations to realize that various risk management strategies needed to mitigate their outsourcing risks are not being used. The next step should be for organizations to implement the risk management strategies that can reduce these unmitigated risks.

This study also provides a foundation from which further research can be pursued. Research can be conducted

to assess the implication of loss of knowledge and expertise in terms of technical skill markets around the globe. An area of research could include skill-based economies and what it means in terms of a global skill based networked operations. Other areas for research include, what financial and skill set changes have major outsourcing and offshore outsourcing companies experienced in the last few years. The answer to this research can potentially increase or reduce the impact of the finding that most organizations do not monitor financial and technical skills after their contract is signed. Research can also be conducted to determine how often U.S. outsourcing companies face unexpected contract price changes. The answer that research question can help answer whether the exposures of moral haggling is already present.

Recent news of offshore-outsourcing companies' untruthful disclosures and fabricated financial statements (Leah, 2009) should trigger several case studies to determine how organizations currently treat the internal or control audit and how many times the financial statements of the vendor whether an outsource or an offshore-outsource provider is included in the company's annual financial audits. It was also reported that the recent outsource

vendor fraud affected at least three large U.S. corporations. Quantitative or qualitative studies should be conducted to determine the direct and indirect implications in terms of customer service interruptions, stock price drops, and other unanticipated panic or loss that was suffered by the U.S. companies that used Satyam.

Grounded theory on the subject of hollow organizations and disintegrated franchises and its implication on organizational behavior and structure should also be pursued. Part of this theory development should concentrate on determining the business management model changes that is needed to sustain growth despite this disintegration. Besides determining the level of disintegration of processes across the globe, it should be determined how this would impact professional training and relocation of trained professionals around the world. Resource dependent theory warns that disintegrated franchises can reduce the effectiveness of organizations. In a globally interconnected economy, the failure of organizational units anywhere can be disruptive to the total global economy. Therefore, recommendations should be made as to how to coherently join these processes of organizations across the

globe to ensure the effectiveness of each separately functioning business unit.

An area of recommendation for public policy intervention would be to promote research to determine what role U.S. companies can play in creating value added offshore-outsourcing products and services to other countries. A country rich with resources in the areas of R&D and business models should be able to create segments and sectors that can be easily developed based on current core-competencies already available and can easily be produced given the current education and training system. This model should concentrate on offsetting some of the negative effects on the job market shifts and reduce the total impact of knowledge and expertise loss.

#### Implications of Social Change

In terms of a social implication, not controlling the risks inherited in outsourcing can reduce the competitiveness of U.S. organizations, which can have a devastating effect on the already struggling U.S. economy. The BP that were least used by U.S. outsourcing organizations are much needed to reduce imperfect information risks and improve an organization's ability to negotiate cost and quality terms more effectively. Taguchi

(1992) explained that when organizations work under imperfect information and are unable to effectively negotiate cost and quality terms, the loss-to-society such as missed opportunities or lower grade service or product is incurred. In terms of loss-to-society, failure to use the responsible strategies can increase the cost of production for outsourcing companies, which can lead to uncompetitive product and service pricing. These can lead to loss of business and further reduction in U.S. work force. Therefore, the loss-to-society can also include economic distress in terms of job loss for the individuals and profit loss in terms of lost-business for the businesses.

From a social change perspective, findings from this study can serve as a means to other ends. First, this can trigger research focused on reducing loss of knowledge and expertise risks for resource dependent outsourcing organizations. Knowledge from research such as this can be used as an assessment point for various risk management professionals in outsourcing organizations. Not using responsible strategies by U.S. companies has already had a tremendous impact on the social welfare of the U.S. citizens. From the president of the USA to the employees who have suffered loss from irresponsible practices in the

financial sectors, no one would disagree that U.S. businesses need to become more responsible in reducing risks that make businesses vulnerable to profit loss and failures.

In terms of positive social change, effort should be made to restore lost knowledge and expertise by U.S. organizations. Given the current rate of non-use of responsible risk management strategies, U.S. organizations have become vulnerable to loss of critical knowledge and expertise required to reduce potential unfair pricing and moral haggling by the outsourcing suppliers and vendors. Responsible strategies can reduce these risks, lead to more stable and informed decision making, and reduce unnecessary resource waste, which benefits the businesses and consumers. These strategies also contribute to better labor markets and overall economic conditions. In terms of positive social changes, using responsible risk management strategies can improve the competitiveness of U.S. businesses and improve the overall economy.

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APPENDIX A: CONSOLIDATED LIST OF BEST PRACTICES, CATEGORIES  
OF RISKS CONTROLLED, AND WHY THESE BEST PRACTICES WORK

<b>Strategies or Best Practices</b>	<b>Risks Prevented</b>	<b>Reasons for Using the Strategies</b>
BP 1: Qualify vendor's skill sets	Contract Management Risks:	Assurance that vendor has the technical skills needed to perform the services (Willcocks, 2006).
BP 2: Qualify vendor's financial capabilities	Contract Management Risks:	Assurance that vendor has the financial resources to acquire skilled resources and make necessary investments in operations to meet the buyers needs (Willcocks, 2006).
BP 3: Use "well-defined project scope" to negotiate outsourcing contract terms.	Contract Management Risks:	Prevents unfair and unnecessary haggling, and negotiation by buyer, reduces project misunderstanding and reduces complexity, enables the buyer to determine exactly what they are paying for (Williamson, 2003).
BP 4: Specifies in the contract your organization's right to terminate the contract	Contract Management Risks:	Enforces the buyers right to control destiny (Koh, 2004)
BP 5: Specify in the contract that your organization has the right to monitor and measure the performance of the vendor	Contract Management Risks:	Enforces the buyers right to monitor and measure and control destiny (Koh, 2004).
BP 6: Specify in the contract that	Contract Management	Ability to change with changing needs of the

your organization has the right to change project specification terms listed in the contract as organization need changes	Risks	organization (Enlow, 2006).
BP 7: Writes detail specification and deliverable requirements for each outsourced service projects	Contract Management Risks	Detailed specification of a project (a) allows the buyer to determine exactly what they are paying for, (b) sets expectations for the vendor regarding what they need to be deliver to the buyer (Punj, 2006), and (c) becomes the standard against which a vendor's performance can be monitored and measured.
BP 8: Monitors the performance of the vendors based on pre-established goals	Contract Management Risks	Assurance that the buyer is receiving what they were promised. Measuring improves timely information about performance and its effects on other processes (Barthelemy, 2003; Punj, 2006). Helps with BP4 objectives.
BP 9: Trains vendor and transfer organizational knowledge to outsource providers	Process Management Risks Also improves contract management	Reduces the chance of miscommunication (Koh, 2004). Service performed by outsource provider's ultimately have to be integrated back into the systems and processes of the buyer. Vendor training transfers necessary organization information to the provider and reduces uncertainties about buyer needs (Tompkins, 2005).
BP 10: Uses dedicated staff	Process Management	Having dedicated staff managing the various steps

(in-house expertise of outsourced services or outside consultants) to monitor outsource provider performance and provide project oversight	Risks  Also improves contract management	of the outsource project assures consistency, improves relationship management, and improves communication effectiveness (Bielski, 2006). Oversight ensures that the vendor is delivering what was expected.
BP 11: Integrates outsource services and projects with internal processes	Process Management Risks	Coordinating the efforts between the buyer and the provider enables the buyers to coherently integrate the two organization's activities and ensures the timely receipt and delivery of inputs and outputs from and to service providers (Enlow, 2006).
BP 12: Retains in-house expertise and core-competency of outsourced services	Process Management Risks  Also improves contract management	Retaining expertise and knowledge of outsource services ensures the ability to provide adequate change management, and adequately measure vendor performance (Enlow, 2006; Punj, 2006).
BP 13: Evaluates the impact of outsourcing on your organization's confidentiality, privacy and security of information in terms of customers' privacy, confidentiality and security rights	Extrinsic Risks: data privacy, security and confidentiality	Reduces uncertainties regarding consumer rights protection, increases chance of compliance with data privacy and confidentiality laws, and protects against competitive disadvantages (Weiss, 2007).
BP 14: Ensures that the outsource	Extrinsic Risks: data	Reduces uncertainties regarding consumer rights

provider's data privacy, confidentiality and security policies and procedures are acceptable before signing contracts	privacy, security and confidentiality	protection, increases chance of compliance with data privacy and confidentiality laws, and protects against competitive disadvantages (Weiss, 2007).
BP 15: Uses a different service provider or writes a different contract for each outsource project	Process Management Risks.	Helps ensure the ability to achieve the objectives of BP3, BP7, and BP16.
BP 16: Writes specific measureable goals for each outsourced project	Contract Management Risks	Specific and measureable goals such as reduce cost of operations by three percent or achieve 10% increase in sales or increase customer satisfaction help organization determine if outsourcing objectives are really met (Kakabadse, 2003).
BP 17: Has an exit strategy plan for outsourced projects with detail plans for replacement	Process Management Risks	Ensures the smooth transition of failed or less-than satisfactory outsource services (Barthelemy, 2003).
BP 18: Retrains existing staff to adjust to changes caused due to outsourcing	Process Management Risks	Ensure appropriate change management of skills sets required to manage changed processes (Enlow, 2006).
BP 19: Monitors changes to vendors skill sets and financial abilities during the cause of the contract	Contract Management Risks	Helps with decision making regarding necessary and ongoing changes in contract terms and in-house processes required to stay competitive (Enlow, 2006).
BP 20. Prepares a general outsource plan for the	Process Management Risks	Ensures that organizations deliberately plan their outsourcing efforts



organization		(Kakabadse, 2003).
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APPENDIX B: RISK MANAGEMENT STRATEGIES USED TO MITIGATE  
OUTSOURCING RISKS SURVEY QUESTIONIONAIRE

Section I: Offshore-Outsourcing and Outsourcing Goals

1. What goal/s and objective/s is/was your organization trying to achieve by outsourcing?
  - i. Reduce the organization's operating cost (Y/N))
  - ii. Improve the organization's ability to focus on core competency functions (Y/N)
  - iii. Improve the ability to perform difficult function more effectively and efficiently (Y/N)
  - iv. Improve overall productivity
  - v. Other goals and objectives (open ended).
2. Has offshore- outsourcing allowed your organization to meet your established goals or objectives? (Y/N).
3. Has outsourcing allowed your organization to meet your established goals or objectives. (Y/N).
  
4. Number of years you have been using outsourcing to meet this objective?
  - a. Less than 1 year
  - b. More than 1 year but less than 5 years.
  - c. Less than 5 years
  - d. More than 5 years
  
5. Number of years you have been using offshore-outsourcing to meet this objective?
  - a. Less than 1 year
  - b. More than 1 year but less than 5 years.
  - c. Less than 5 years
  - d. More than 5 years

Section II: For the 20 Best Practices (BP) or Risk Management Strategies listed choose the ones that your organization uses.

Question # 6

1. qualifies outsourcing vendor's technical skills before signing outsourcing contracts
2. Qualifies outsourcing vendor's financial capabilities before signing outsourcing contracts
3. Uses "well-defined project scope" to negotiate outsourcing contract terms.
4. Specifies in the contract your organization's right to terminate the contract

5. Specifies in the contract that your organization has the right to monitor and measure the performance of the vendor
6. Specifies in the contract that your organization has the right to change project specification terms listed in the contract as organization need changes
7. Writes detail specification and deliverable requirements for each outsourced service projects
8. Monitors the performance of the vendors based on pre-established goals
9. Trains vendor and transfer organizational knowledge to outsource providers
10. Uses dedicated staff (in-house expertise of outsourced services or outside consultants) to monitor outsource provider performance and provide project oversight
11. Integrates outsource services and projects with internal processes
12. Retains in-house expertise and core-competency of outsourced services
13. Evaluates the impact of outsourcing on your organization's confidentiality, privacy and security of information in terms of customers' privacy, confidentiality and security rights
14. Ensures that the outsource provider's data privacy, confidentiality and security policies and procedures are acceptable before signing contracts
15. Uses a different service provider or writes a different contract for each outsource project
16. Writes specific measureable goals for each outsourced project
17. Has an exit strategy plan for outsourced projects with detail plans for replacement
18. Retrains existing staff to adjust to changes caused due to outsourcing
19. Monitors changes to vendors skill sets and financial abilities during the cause of the contract
20. Prepares a general outsource plan for the organization

### Section III:

7. What service/s is being currently outsourced or off-shored?
  1. IT services
  2. Business process (BPO)
  3. Customer services -call center
  4. Human resources
  5. Legal
  6. Accounting/ Financial
  7. Others: (Please Specify) \_\_\_\_\_
8. What is the total size of the offshore outsourcing contract (about which you are answering the following question?
  - a. Under \$5 million
  - b. Over \$5 million but under \$10 million
  - c. Over \$10 million
9. What is your role in this offshore outsourcing service contract?

- a. Senior or Executive Management, Risk Management or Internal Audit Director (Internal Outsourcing Managers responsible for organizations enterprise risk management strategies).
- b. Outsourcing manager, project manager – internal staff other than executives managing the organization's outsourcing practices.
- a. Outsourcing consultant managing another organizations outsourcing practices
- b. Other (Please Specify) \_\_\_\_\_

APPENDIX C: MESSAGE SENT OUT IN THE EMAILS

**Email Subject Line: You have been randomly selected to participate in a Ph.D. dissertation study concerned with mitigation of outsourcing risks.**

**Email Content**

The purpose of the study is to determine what outsourcing management practices is commonly used by U.S. organizations that use outsourcing as a means to achieve some of its goals. In this study the term outsourcing is used to mean an alliance with a third party vendor. Offshore-outsourcing means the vendor is in a different country. You are receiving this survey because our research indicates that your organization uses outsourcing as a means to perform some of its tasks.

**This anonymous study will not collect any data about your company or the person answering the questions. The link to the survey is provided below:**

[http://www.surveymonkey.com/s.aspx?sm=\\_2ba3ByKOa1wcQRc7SEV61Mw\\_3d\\_3d](http://www.surveymonkey.com/s.aspx?sm=_2ba3ByKOa1wcQRc7SEV61Mw_3d_3d)

The survey is only 3 pages and will take between 10-15 minutes to complete. Please send it to another manager in your company if you are not familiar with your organization's outsourcing management practices.

This survey can remain truly anonymous if you don't respond to us about your participation.

**Note:** Responses from all survey takers will be collected and analyzed anonymously. This study will not collect any personal and company identifying data and any IP addresses. The participation in this survey is voluntary and there is no compensation. There is no penalty for refusing to or discontinuing participation once you have started the survey. Since this is an anonymous survey, no consent signature is requested. If you agree to the terms above, then your completion of this survey signifies your consent to participate in the research study. No foreseeable risk or discomfort should be experienced when taking this survey.

Thank you very much for your contribution to this dissertation study.

Erica Bains,

[ebains@stmarys-ca.edu](mailto:ebains@stmarys-ca.edu)

Louis Taylor, Ph.D. Dissertation Faculty Mentor

Research Participant Advocate: Dr. Leilani Endicott, 800-925-3368 ext. 1210

APPENDIX D: LETTER MAILED TO THE COMPANY:

Dear Audit Department Manager

Your company has been randomly selected to participate in a Ph.D. dissertation study concerned with mitigation of outsourcing risks.

You are receiving this survey because our research indicates that your organization uses outsourcing as a means to perform some of its tasks. The purpose of the study is to determine what outsourcing management practices is commonly used by U.S. organizations that use outsourcing as a means to achieve some of its goals. In this study the term outsourcing is used to mean an alliance with a third party vendor. Offshore-outsourcing means the vendor is in a different country.

If you are responsible for outsourcing risk management practices please visit the online survey at:

[http://www.surveymonkey.com/s.aspx?sm= 2ba3ByKOa1wcQRc7SEV61Mw\\_3d\\_3d](http://www.surveymonkey.com/s.aspx?sm= 2ba3ByKOa1wcQRc7SEV61Mw_3d_3d)

This anonymous study will not collect any data about your company or the person answering the questions. The survey is only 3 pages and will take between 10-15 minutes to complete.

If you are not responsible for outsourcing risk management practices can you please send this letter to another manager in the organization who is.

Thank you very much for your contribution to this dissertation study.

**Note:** Responses from all survey takers will be collected and analyzed anonymously. This study will not collect any personal and company identifying data and any IP addresses. The participation in this survey is voluntary and there is no compensation. There is no penalty for refusing to or discontinuing participation once you have started the survey. Since this is an anonymous survey, no consent signature is requested. If you agree to the terms above, then your completion of this survey signifies your consent to participate in the research study. No foreseeable risk or discomfort should be experienced when taking this survey.

Erica Bains,

[ebains@stmarys-ca.edu](mailto:ebains@stmarys-ca.edu)

Louis Taylor, Ph.D. Dissertation Faculty Mentor

Research Participant Advocate: Dr. Leilani Endicott, 800-925-3368 ext. 1210

## CURRICULUM VITAE

*Erica K. Bains*

### **Education:**

Ph.D. Candidate, Applied Management and Decision Sciences, May 2009

MBA, Financial Management, May 1988

B.S., Management Information Systems/Accounting

### **Academic Experience:**

2007 - Current      Lecturer of Accounting Information Systems and Auditing in the School of Economics and Business Administration at Saint Mary's College, California

2002 - 2007      Adjunct Professor of Computer Information Systems and Accounting Information System in the School of Economics and Business Administration at Saint Mary's College, California

### **Professional Experience:**

2003 - 2008      President/CEO Ark Strategies, Inc, a Consulting company specializing in leadership and organization development training, enterprise risk management, knowledge management, and globalization strategy solutions

2000 - 2001      Director of Product Development and R&D at ProjectArena, Inc, an application service provider specializing in enterprise resource planning application services

1997 - 2000      Senior Auditor and Senior Quality Assurance leader at AAA, a national insurance, travel, and roadside service provider.

1988 - 1997      Served in various positions including Audit Senior at Countrywide Financial Corporation, CFO for Global Mortgage Corporation, Staff Management Auditor for California State Lottery, and various consulting work for Computer Sciences Corporation.

### **Current Memberships**

Women's Technology Cluster (WTC)  
Information System Audit and Control Association (ISACA)  
Institute of Internal Auditors (IIA)  
Software Engineering Institute (SEI)

American Society for Quality (ASQ)

**Honors:**

Who's who in American Women Executives in 1992

Who's who in Global Business Leaders in 1993 and 1995