

Chapter 10

IT Sourcing

Outsourcing is now a widely accepted part of doing business. In IT, companies are outsourcing everything from operations and help desks to maintenance and development. What started as a mechanism largely to lower costs has become an integral part of a much larger IT strategy. IT departments are finding that outsourcing gives them access to a wider range of skilled resources, helps them focus on their core strengths, and speeds the time to market of products and services. Lower operational costs, reduced up-front investment, and the ability to convert fixed to variable costs also make outsourcing an attractive option for some IT services.

As IT organizations have gained experience with outsourcing, they have learned to do it more effectively—to better manage the relationships, risks, benefits, and outcomes involved. As a result, interest in outsourcing is growing, although a 2002 study found there is still considerable reluctance to use it (Mackie 2002). Clearly, outsourcing has found a place in the IT executive's toolkit.

The danger now is complacency. Thinking that they have a handle on outsourcing, IT managers could fail to consider newer forms of outsourcing, different options, different strategies, and/or changing economies. Certainly, there are new players on the horizon and new approaches to sourcing that will change yet again how IT sourcing decisions are made. Some of these include strategic sourcing practices; offshore contracting; and nearshore sourcing using companies based in India, Ireland, Asia, and Eastern Europe. Better connectivity, the availability of high-quality staff, and much lower costs are changing sourcing markets and expanding sourcing possibilities for companies.

In previous research, we examined outsourcing through application service providers (ASPs) and concluded the following:

The emerging external IT services marketplace offers rich opportunities and many possibilities for IT organizations to become more cost effective. . . . Strategic business applications development and management for mission-critical applications will [continue to] be in-house, but delivery for standard and meta-industry applications, processes and technology will be off-site. Thus . . . it is likely that external IT providers will form part of [a] future service delivery package. . . . However, as is so often the case in the IT industry, today's reality falls far short of what the industry promises. Companies wishing to take advantage now of what the external IT services marketplace can offer must evaluate [it] carefully and . . .

126 Section II • IT Governance

proceed in full awareness of the risks involved. It is recommended that organizations articulate a sourcing strategy which balances internal versus external capabilities. (McKeen and Smith 2003)

This chapter first explores how sourcing strategy is evolving in organizations. Then it looks at emerging sourcing models, with particular emphasis on offshore/nearshore outsourcing. Next it discusses some new critical success factors for effective sourcing. Finally, it looks at how the role of IT itself is changing as a result.

THE EVOLUTION OF SOURCING

The concept of outsourcing IT services—that is, transferring some or all of a company’s IT activities to a third party that performs them on behalf of the enterprise—has been a significant factor in IT decision making since the early 1990s (Lacity and Willcocks 2001). Globally, the outsourcing industry was estimated to be more than \$1 trillion in 2000 (Kern et al. 2002). It is growing steadily as companies explore new possible sourcing models and outsourcing companies become better at what they do and expand the range of their services. At first, sourcing decisions were driven largely by economics, with outsourcers promising to remove millions of dollars from a firm’s IT budget. However, today they reflect a significant shift in business strategy from diversification to a focus on core competencies. In turn, evolving sourcing models are transforming the underlying economics of IT (Lacity and Willcocks 2001).

As our understanding of sourcing has developed, three distinct yet complementary approaches have emerged:

- 1. Outsourcing for operational efficiency.** This is the most well-established approach to sourcing, dating from the early 1990s, and is still by far the most common one, according to researchers (Lacity and Willcocks 2001). Here the “utility” functions of IT (e.g., computer operations, communications, infrastructure, and help desk) are transferred to an outsourcer, often along with company staff. The objective is to save money by sharing staff and resources with other companies in areas that do not make the company distinct and that have become routinized (Carr 2003). Outsourcing companies are typically autonomous entities that use their extensive experience in these areas, economies of scale, and the discipline of a contractual relationship to reduce the overall cost to a company while generating a profit for themselves. Many organizations have found that outsourcing to businesses that specialize in these services allows them to offer the same or better service at a reduced cost. Over time, this form of sourcing has become increasingly successful as companies have learned how to negotiate and manage contracts to make outsourcing work.
- 2. Outsourcing for tactical support.** In the late 1990s, companies recognized that outsourcing could be used to help free up their own IT staff to perform selected support and development work and eliminate some of the peaks and valleys of the IT staffing cycle. “We are always under continual pressure to reduce the cost of our existing applications,” stated one manager. “We spend 85 percent of our development budget on maintenance and support.” Facing the dual challenges of Y2K and the dot-com bubble, and the resulting staff shortages they caused, many businesses began to use outsourcing in new ways. They offloaded their mature IT to an

outsourcer who could “keep the lights on” while company staff introduced new applications. They also used outsourcers as a way to introduce new technologies quickly (e.g., e-business) through such practices as managed hosting of a Web site and using outsourced staff to transfer their experience and skills to in-house staff. With this approach to sourcing, IT managers seek to rapidly add to their capacity to deliver applications and new technology to their organizations (Lacity and Willcocks 2001). Although cost is still important, the primary driver for using tactical outsourcing is to achieve flexibility and responsiveness. As tactical outsourcing has developed, contracts have become more flexible and outsourcers have come to be viewed increasingly as partners who can add other forms of value rather than simply reducing cost.

3. *Outsourcing for strategic impact.* Over the last decade, sourcing has been increasingly recognized as a tool for achieving an organization’s strategic objectives as well as driving costs down and adding capacity. As companies have become more focused on their core competencies, new possibilities for sourcing have opened up. With greater connectivity, it is now possible to outsource whole business processes that are not considered business critical. Noncore applications (e.g., accounting) can languish in-house because they cannot justify the same business value as other projects. By outsourcing these processes, companies can get full functionality without having to develop the applications themselves. Some organizations are using outsourcing to drive organizational change. “Today we consider outsourcing at a higher level,” explained a manager. “We look at sourcing holistically. While you still need to outsource routine activities, you also need to look at it from the top down. Sourcing shouldn’t be an ad hoc process.” Companies are seeing that outsourcing can give them access to world-class capabilities, disciplines, quality, and innovation. To this end, some have established strategic alliances with a few vendors to take advantage of what they can offer. These preferred relationships are typically broad in scope and complex in nature and are designed to deliver significant business value (Smith and McKeen 2003). “Our supplier alliances are now part of getting any project approved,” said another manager. “We must present the full continuum of sourcing options in any business case.” Finally, organizations are learning that “right-sourcing” (i.e., choosing the right sourcing option for a given activity) can change with time. Certain functions that have been outsourced can become business critical, and others that were deemed core can now be outsourced. One manager explained, “In our company we are constantly testing what should be outsourced. The business has to be fully engaged in the process so they understand the implications.” Strategic sourcing is a very recent trend, and companies have very little experience doing it. The focus group suggested moving carefully into this area until more is known about how to accomplish it successfully. Members also cautioned that customers should watch for hidden costs at this level (e.g., the need for integration by the customer) that can be quite expensive and could kill a business case for this type of sourcing.

Each of these three approaches to sourcing represents an increase in the size, scope, and impact of what is sourced. Table 10.1 summarizes these approaches. It should be stressed that one does not preclude the other. Companies tend to begin outsourcing for operational efficiency and move toward tactical and strategic approaches as they gain experience and confidence at each level.

TABLE 10.1 Three Complementary Approaches to IT Sourcing

Approach	Driver	Mode	Activities	Relationship
Operational Effectiveness	Cost reduction	Utility	Infrastructure, operations, support	Fee-for-service
Tactical Support	Capacity, flexibility	Service delivery	Mature technology, new technology	Partnership
Strategic Impact	Focus, business value	Toolkit	Processes, transformation, innovation	Strategic alliance

Companies have become quite good at basic utility, fee-for-service sourcing. In fact, by far the majority of sourcing is of this type (Lacity and Willcocks 2001). All of the companies in the focus group had some sourcing initiatives to improve operational efficiency, although none had completely outsourced their services, even at this level. Overall, studies show that about 38 percent of IT functions have now been outsourced to vendors (Barthelemy 2001).

Research has also identified five factors that are critical to the success of *current* outsourcing initiatives:

1. *Use selective sourcing.* Careful selection of what to outsource and what to retain in-house is a demonstrably more effective approach than total outsourcing or total insourcing. Companies find it more controllable and satisfactory as well as considerably less risky (Chen et al. 2002).
2. *Have joint business–IT sponsorship.* When both the business and IT executives are involved in making outsourcing decisions, the results are far more likely to meet expectations than when either group acts alone (Lacity and Willcocks 2001).
3. *Ensure a thorough comparison with internal operations.* Too often companies don’t get expected savings because they forget to include or identify the hidden costs involved in outsourcing when problems such as extra maintenance or consulting fees arise (Overby 2003b).
4. *Develop a detailed contract.* Tighter contracts with carefully thought-out flexibility, evolution, and reversibility clauses lead to more successful sourcing (Barthelemy 2001).
5. *Limit the length of the contract.* Short-term contracts (one to three years) are more likely to be successful than mid- or long-term contracts. This is because they involve less uncertainty, motivate supplier performance, help ensure a fair market price for services, and enable recovery from mistakes more quickly (Lacity and Willcocks 2001).

In spite of all that has been learned, between 14 and 78 percent of outsourcing functions are deemed failures (Barthelemy 2001; Overby 2003b), and repatriating functions are becoming more and more common (Overby 2003b). A major reason for this huge discrepancy in success rates is that companies are experimenting with increasingly more radical options to extend outsourcing models, thereby moving into areas of higher risk.

**OFFSHORE AND NEARSHORE OUTSOURCING:
EMERGING SOURCING MODELS**

In addition to outsourcing larger and more complex chunks of work (e.g., innovation, business processes) and developing more complex relationships with vendors (i.e., strategic outsourcing), companies are also working with vendors at increasingly greater distances, typically in other countries. Known as *offshore outsourcing* (or simply *offshoring*), the primary driver for this sourcing model and its many variations is economic (Aron 2003; Kripalani and Engardio 2003). The increasing globalization of large companies and the need for global processes is also a factor (Chen et al. 2002). Vendors located in other countries, such as India, can charge a fraction of what it costs to provide the same service in the United States. Facilitated by ever-greater connectivity; ubiquitous, cheap bandwidth; and Web technologies, companies can afford to knit together people, processes, and platforms in different ways than have been possible previously (Aron 2003). Forrester Research has found that 44 percent of Fortune 1000 companies are offshoring some activities (cited in Blackwell 2003).

According to Chen et al. (2002), IT organizations are unclear about how offshoring fits into a company’s overall sourcing strategy and are even less clear about how to make it successful. Undoubtedly, global outsourcing represents a significant shift in how organizations manage their IT activities (Elmuti and Kathawala 2000). Therefore, today’s IT managers are approaching offshoring cautiously and building on what they have learned about other forms of outsourcing. “There is certainly a lot of hype about offshore outsourcing,” said one, “but we’re still skeptical about its benefits. We had a bad experience ten years ago. The level of professionalism and understanding just wasn’t there, so it didn’t work.” Nevertheless, the cost differentials and the “hype” are forcing everyone to look seriously at offshoring as part of their sourcing strategy.

Offshore Outsourcing Benefits

It is cheaper to do IT work outside the United States. Even doing work in Canada can reduce costs for many United States–based firms. However the big savings come from sending work to Third World countries, where salaries are 40 to 60 percent lower than in North America. Most Third World countries have significant numbers of well-trained professionals and offer considerable tax breaks.¹ As a result, even with additional travel and connectivity charges, companies are expecting to save 20 to 40 percent on costs such as managing infrastructure or operating a help desk (Bhandari 2003). The differentials are so significant that the increased competition is also driving down the rates of traditional North American outsourcing vendors (Blackwell 2003). These vendors are also setting up centers in India so they can compete more effectively (Kripalani and Engardio 2003).

Typical activities that are being sourced offshore include help desk, personal computer repair, disaster recovery, back office processes, application maintenance, network management and operations, application and IT support, and problem resolution (Chordas 2003). These are relatively routine and straightforward utility types of functions

¹There are more IT engineers in Bangalore, India, alone than there are in Silicon Valley, California (Kripalani and Engardio, 2003).

that many companies feel very comfortable in outsourcing. Thus, in moving these functions offshore, they are limiting risk while taking advantage of the resulting cost benefits. However, many offshore outsourcers, especially in India, are also seeking to scale up the types of activities in which they are involved. Quality standards in India, for example, are often higher than in North America (Blackwell 2003). In many cases Indian companies have better software and risk management processes and have been among the first in the world to achieve the highest SEI CMM rating of five (Satyam 2003). These firms are seeking a larger presence in the high-end software development and consulting areas of the market (i.e., tactical and strategic outsourcing). Big vendors, such as Oracle, Accenture, and Microsoft, are also establishing partnerships and software development centers in India to take advantage not only of the cost savings involved but also the skills available (Blackwell 2003).

Offshore Outsourcing Locations

Although 85 percent of offshore outsourcing work currently goes to India, several other countries are looking to increase their share of this work. China, Russia, and the Philippines are the most serious competition, although they are far behind India at present (Overby 2003a). Canada is also involved in this market because of its proximity to the United States, even though it is more expensive than other offshore vendors. Ireland, Israel, Mexico, and South Africa are also positioning themselves in this market. Forrester Research predicts that by 2015, about 3.3 million jobs will have moved offshore—70 percent to India, 20 percent to the Philippines, and 10 percent to China (cited in Chordas 2003).

All of these countries offer reduced or substantially lower costs, but they are not considered equal in other important characteristics, which should be considered before a company makes a significant outsourcing decision. These factors include language, cultural similarities, time differentials, political stability, quality, project management skills, education, and infrastructure. Table 10.2 summarizes these for the five main countries involved in offshore sourcing with the United States.

TABLE 10.2 A Comparison of Offshore Outsourcing Nations

Country	Language	Cultural Similarities	Time Differential	Political Stability	Project Management Skills	Education	Infrastructure
Canada	English	Many	None	Excellent	Very good	Excellent	Excellent
India	Good English	Some	Large	Good	Excellent	Excellent	Improving
China	Limited English	Few	Large	Good	Unknown	Good	Good
Philippines	Good English	Some	Large	Good	Unknown	Good	Very good
Russia	Limited English	Few	Large	Fair	Poor	Good	Unknown

Source: Based on Chordas 2003; Damsell 2003; Gallagher 2002; Overby 2003a.

Offshore Outsourcing Risks

As Table 10.2 shows, offshoring involves considering a number of factors, such as language and political stability, which have not traditionally been part of outsourcing decision making. Comments from practicing IT managers clearly illustrate some of the risks involved.

“We outsourced a call center to India and then brought it back. There were problems with the time to transfer calls, language, and spelling. The accents weren’t bad, but there was often poor understanding on the phone.”

“We outsourced project management and then lost all their interfaces with the users when they left. Now we have 100 percent internal project management.”

“We outsourced our help desk. It was brutal. We had the mix wrong. We needed more decomposition of activities and a more granular understanding of what we were doing.”

A number of additional risks must also be addressed as part of the offshore outsourcing decision-making process:

- **Hidden costs.** These include the cost of finding a vendor, drafting the contract, and managing the effort, as well as the cost of transitioning to a new vendor if the first doesn’t work out. Monitoring, bargaining, and negotiating needed changes to a contract typically add up to about 8 percent of the yearly contract amount (Barthelemy 2001). Travel and visa costs are also often substantial (Blackwell 2003). As a result, many companies are finding they are not achieving the savings they anticipated (Elmuti and Kathawala 2000).
- **Reduced control.** Although outsourcing in general reduces an organization’s control over how its services are delivered, offshore sourcing can greatly increase these risks because the vendors operate in substantially different business environments. A company may, therefore, have greater liability exposure and face problems with such issues as confidentiality, security, and time schedules (Elmuti and Kathawala 2000).
- **Legal and political uncertainties.** Working in other countries means dealing with a wide variety of unfamiliar government regulations and restrictions, legal systems that may be unable to cope with the types of disputes that may arise between companies or between companies and the government, and weak intellectual property rights (Overby 2003b). Furthermore, governments in Third World countries may be considerably less secure than in North America or Europe. India has lost work recently due to the instabilities in that part of the world following the attacks of September 11, 2001.
- **Cultural differences.** Different cultural backgrounds can cause numerous difficulties. In addition to language problems, such matters as the pace of daily life, employees’ relationship to authority, attitudes to security, and adherence to socialist principles can lead to misunderstandings that can be daunting (Overby 2003b).
- **Social justice.** Practicing IT managers were also very aware of the “optics” of offshore outsourcing. “Public perceptions are important to us,” stated one. Another manager noted that his company has a labor code of conduct and a risk rating for different countries that assesses their labor practices and other dimensions of risk. Government organizations in particular are especially sensitive to the issues of moving jobs out of the country. For example, a recent public outcry forced the state of Indiana to cancel a \$15 million contract with a firm in India (Kripalani and Engardio 2003).

Variations in Offshore Outsourcing Models

Some of the risks and concerns cited above are forcing vendors and companies to rethink the basic offshore outsourcing model. Some are distinguishing between offshore and nearshore sourcing. Not only are some U.S. vendors setting up sourcing centers in Canada, but some Indian firms are doing so as well. For example, Satyam Computer Services has recently opened a development center in Toronto to ensure that North American clients can “deal with a company that’s always close to home, close to their unique needs” (Satyam 2003). Although much work actually can be completed in India, having relationship managers and business analysis in closer proximity to their customers provides additional security and mitigates many of these risks.

Other companies are looking at nearshore opportunities in lower-cost areas of their own countries. One Canadian firm is using nearshore sourcing to move development work to New Brunswick—a province with cheaper labor. Several Native American reservations have gone into the sourcing business as well. They argue that they can offer the same low-cost, high-value work that is done offshore but without the headaches of language barriers, remote management, or security concerns (Field 2001). These options are particularly attractive for sensitive legal and government work that should not be sent overseas.

Other firms are finding that they can get many of the benefits of offshore sourcing by working with a major vendor who will undertake to manage the offshore work and relationships. “You can have global options if you pick your vendor carefully,” said one. “We triage our projects with our partner to find the best sourcing choice possible.”

Sourcing today is actually a continuum of practices that can be “sliced and diced many different ways,” depending on the needs of the company and the particular activity involved. Partnerships with key vendors are especially important in these situations so they can optimize the blend of internal and external staff appropriately. “You shouldn’t go with a one-off project offshore,” one manager explained, but rather with a carefully designed strategy that enables experimentation with different sourcing models and includes the ability to reverse a sourcing decision if it doesn’t work out.

SUCCESSFUL SOURCING

As experience with sourcing increases, organizations are learning more about what it takes to manage sourcing successfully. However, although some critical success factors are well established (see above), as new models of sourcing emerge and as sourcing takes on a more central part of IT and organizational strategy, understanding what is involved in successful sourcing is still evolving. The focus group identified several factors that are essential in its effective management.

Sample Sourcing Criteria

What are our industry dynamics, and where are we in the food chain?	What should we be good at?
What are we good at?	Do we want to invest in this function/activity?
What do we want to be good at?	How many vendors do we want to deal with?

Sourcing Strategy

Whether a company uses sourcing strategically or not, every organization should have an overall sourcing strategy. This helps it determine what to source, where to source, and to whom to source. Experts have suggested many different ways of determining what to source—what’s core and what’s not, contribution to business value, maturity of technology, activities that are routine and less knowledge intensive, and entry-level functions (Aron 2003; Barthelemy 2001; Lacity and Willcocks 2001). In practice, however, numerous approaches to “right-sourcing” are possible. What is right for one organization is not necessarily right for another. Companies should consider the following:

1. First develop an in-depth understanding of business drivers and strategy before developing a sourcing strategy.
2. Then IT managers should develop a detailed understanding of the IT functions, processes, and overall portfolio. Without this, it is possible that too much or too little could be outsourced, leading to significant problems.
3. Then they should apply their particular sourcing criteria to IT activities (see “Sample Sourcing Criteria”) to determine which parts of IT can be successfully sourced.
4. Finally, the sourcing strategy must be continually tested and reevaluated as the industry, business strategy, and sourcing possibilities change frequently.

Risk Management/Mitigation

“War stories” abound. Every firm can cite examples of activities that had to be resourced to a different vendor, tasks that needed to be reinsourced, or contracts that were renegotiated because of problems. The fact is sourcing introduces new levels of risk to the organization. Loss of control, security and privacy problems, poor-quality work, hidden costs, lack of standards, unmet expectations, and bad publicity are just some of the problems that have been experienced. When moving into new forms of sourcing, it is important to incorporate risk management and mitigation into every aspect of sourcing.

- Detailed planning is essential. Precise definitions of roles, responsibilities, and expectations must be developed. Specialists in outsourcing are now available to provide advice on how to select a vendor and plan the work involved. The specialists can assist—but not replace—the IT sourcing team in understanding how to assess and engage a vendor. This is especially important when considering offshore sourcing because of the additional complexities involved.
- Monitoring and an audit trail must be incorporated into the contract to both encourage self-correction and ensure all parties live up to their commitments.
- All potential risks should be rated as to both the likelihood of occurrence and their impact if they do occur (Aubert et al. 2001). Appropriate steps should be explicitly taken to reduce and/or manage these risks.
- An exit strategy must be devised. “Any well-designed sourcing strategy must retain alternatives to pull activities back in-house,” explained one manager.
- Finally, exercise caution when moving into new avenues of sourcing. The hype in the popular press, often originating from vendors, greatly inflates the benefits that

134 Section II • IT Governance

can be achieved while minimizing the risks. It is recommended that managers experiment with a “simple, substantial pilot” before committing the company to a significant new outsourcing initiative.

Governance

“With any sourcing initiative, governance must be super-good,” said a manager. Most IT functions now recognize the importance of relationship management at all levels (i.e., the frontline, middle, and senior management) in delivering value. Nevertheless, it cannot be underestimated. “When the relationship between the client and its vendor is adversarial, the vendor will take advantage of gaps in the agreement. When there is mutual trust, vendors often work hard to deal fairly with the gaps” (Barthelemy 2001). “Layers of governance are critical to successful sourcing relationships,” said one manager. Others also suggested retaining strong internal project management and ensuring that vendors also have these skills. “You can’t outsource project management or the relationship with the customer,” they agreed. Governance problems are exacerbated when offshore sourcing is undertaken because of the difficulties of managing relationships at a distance (Chordas 2003). This is one reason the larger offshore vendors are setting up local development centers. At minimum, an offshore outsourcer should name an internal manager who will act as the organization’s champion and be responsible for quality assurance. Ideally, an outsourcing relationship should be structured to ensure shared risk so both parties are incented to make it work (Garr 2001).

Cost Structures

One of the most important elements of successful sourcing is a complete understanding of the cost structures involved. Previously, vendors have profited from their ability to squeeze value from outsourced activities because they had a better and more detailed appreciation of their costs. Furthermore, they were able to apply disciplines and service-level agreements to their work, which IT organizations were often prohibited from doing (Lacity and Willcocks 2001). Today this is changing. Companies are applying the same standards to their own work, enabling them to make more appropriate comparisons between the costs of doing an activity in-house and outsourcing it. They also have a better understanding of the true costs of outsourcing, including relationship management and contract management, which have frequently been underestimated in the past. “We need to thoroughly understand our economic model,” said one participant. “Vendors have the advantage of knowing best practices and economies of scale, but they are at a disadvantage from a profit and knowledge point of view. If we can’t compete in-house, we should outsource.” Interestingly, many companies believe they can compare favorably in many areas with outsourcing vendors. Ongoing cost comparisons are ideal, according to researchers, because they motivate both parties to do their best and most cost-effective work (Lacity and Willcocks 2001). The reduced cost of labor is simply one element of the outsourcing value proposition. “We must learn to understand and track every cost involved,” said an IT manager. “There are new governance costs; privacy, legal, and regulatory costs; and other hidden costs that have to be articulated and monitored.” The need to better understand the total cost of ownership of each IT activity is forcing managers to become considerably more aware of the financial implications of their decisions and develop a whole new set of skills as a result.

THE CHANGING ROLE OF IT

New IT Roles and Responsibilities

- Solution delivery
- Task decomposition
- Task costing analysis
- Right-sourcing decision making
- Designing for collaboration and connectivity
- Supplier relationship management
- Contract management and monitoring
- Sourcing marketplace analysis

The growth of sourcing over the past decade has led to a number of new roles for IT managers and has changed the relative importance of key IT skills. As lower-level IT activities are outsourced, what is increasingly left behind is the high-value-added work that only knowledgeable, in-house IT practitioners can provide. “The development skills we need these days are not coding, but integration, business analysis, and project management. We need to hone these skills to do the jobs that are difficult to outsource,” explained one manager. Although important pieces of development can be done off-site, it is still IT’s job to put all the pieces together and make technology work for the enterprise. In short, organizations need to improve their solution delivery skills, which is by no means a straightforward or simple task.

Systems thinking skills are becoming increasingly critical as well. They are fundamental to the detailed decomposition of tasks, which is the first step in better understanding both cost structures and the relative strategic importance of each task. IT organizations also need more formal processes and decision-making frameworks within which to tackle the key sourcing questions of what to outsource and how it should be done. These should include the parts of the business that will be affected by outsourcing and involve both tactical and strategic discussions with business management.

Emerging sourcing models will also need to be incorporated into the organization’s technology plans as well as its business strategies. IT architectures must be designed for greater connectivity and collaboration across organizational boundaries. Companies should anticipate a wide variety of possible options in how their processes and transactions will be undertaken.

Finally, IT organizations are recognizing that they need new management skills, governance structures, and organizational processes to make outsourcing work effectively. Several companies now have a “supplier relationship management” function, at a mid to senior management level, responsible for ensuring that outsourcing arrangements are working well. Similarly, some companies are learning how to develop effective sourcing contracts and monitor them, both for supplier compliance and for internal satisfaction (Smith and McKeen 2003). In the future, companies will also need skills to better analyze the external sourcing marketplace and their industry to select the most appropriate options for their organizations.

Conclusion

Sourcing has become an integral part of almost all IT organizations today. Originally a straightforward mechanism for reducing operational costs, sourcing is rapidly evolving into a strategically important means of delivering optimal IT value. At present, companies

136 Section II • IT Governance

and vendors are experimenting with new models of sourcing, only some of which will be sustainable. Increasingly, it is IT's job to guide the organization in making the best sourcing decisions possible and to ensure that the anticipated value is obtained from vendor relationships. This involves developing new IT skills that incorporate an understanding of technology with strong business knowledge and analytic capabilities. As a result, despite the fact that sourcing is changing the nature of

the work that is done internally in IT, it is unlikely that sourcing will eliminate internal functions altogether or reduce their value to that of a utility, as has been suggested by some (e.g., Carr 2003). To the contrary, more and more organizations will need the systems thinking, architectural understanding, and strategic awareness embodied in a modern IT department in order to ensure that they don't end up with a hollow shell of an organization that provides limited added value.

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