
The Relationship Advantage as Practice: Reflections

INTRODUCTION

The cross-case analysis in the previous chapter illustrated the adequacy of our framework in characterizing IT outsourcing relationships. Prior to that, the individual case analyses in Chapters 3–7 elicited a number of strong links between the dimensions which, combined with Chapter 8’s detailed analysis, provide a number of important pointers for outsourcing relationship management. This section makes use of the framework in a normative sense to determine a number of critical propositions for relationship management practice. We also suggest some small but important revisions of the framework, for future use by practitioners. The discussion below follows closely the main dimensions of the framework, and, for coherence in the discussion, some repetition here of findings from the previous chapter is inevitable.

Based on the comprehensive analysis we carried out in this book on IT outsourcing, and the relationship dimension, we will now reflect further on the evidence and elicit key learning points and relationship management pointers. In the second part of this chapter we identify three ways of thinking about, and striving for understanding of the possible relationship advantages to be gained. We structure these discussions by way of three additional frameworks that can be used by practitioners as they debate, move towards, or are heavily involved in IT outsourcing. The first issue is the nature of the Winner’s Curse in IT outsourcing, and how its risk can be minimized. The second issue is diagnosing the type of IT outsourcing arrangement you might be involved in, and the implications this will have for the relationship dimensions. The third relates to the six phases of an IT outsourcing arrangement identified by earlier research in which we participated. The evidence in this book strongly corroborates the usefulness of thinking in these terms. Therefore we describe here the framework, and use the case histories to pull out the implications for managing relationships across the six phases of our relationship framework.

RELATIONSHIP MANAGEMENT: PRACTICAL IMPLICATIONS

Although the analytical framework (see Chapter 2) depicts relationship management as static and systematic, in actuality it has to be very iterative and dynamic. Van de Ven and Ring (1994) argued—correctly—that relationship management is cyclical rather than sequential, and suggested that relationships are maintained ‘not because they achieve stability, but because they maintain balance between formal and informal processes’. Our framework actually acknowledges this aspect and addresses it indirectly through the ‘time element’. A constant interplay between the relationship dimensions occurs over the lifespan of the venture. In practice, the unidirectional flow of the diagram is deceiving, as it only refers to the passing of time.

As part of this dynamism, it is clear that the relationship dimensions we isolated for analytical purposes have an intrinsic dynamism. They interpenetrate and have mutual effects on each other, and in combination affect other factors in the IT outsourcing arrangement. The five figures in the sections below summarize the cross-case analysis findings of the strongest cause and effect links, and present an indicative value judgement of their positive and/or negative impacts. Since these links identify the main relationship management issues that client and vendor organizations were confronted with, the authors point to an understanding of these as being critical for developing robust relationship management practices.

Outsourcing Intentions in Relationships

Unlike the framework’s suggestion, Figure 9.1 shows that outsourcing intent primarily affects the contract, the structure, and the efficiency outcome of the venture. Still these findings corroborate the position of intent as an input dimension of the relationship, and as the measure against which to evaluate its efficiency outcome. Since managers’ tasks and actions tend to be directed by outsourcing intentions, it seems paramount that these are pervasive. Financial, business, and technical intentions can be readily communicated to managers across the organization for they can be formalized. However, those intentions that focus on ‘reciprocity’ or partnering can only be stated as a directive, as the transfer of ‘soft’ intentions, behaviours, and established relations is infeasible (as we saw in Xerox’s case). This needs to be taken into account when planning intentions and for managing organizational expectations.

Outsourcing intent affects the contract as the promises agreed to, in essence, should reflect the client’s objectives. All cases illustrated that the core objectives pursued were ingrained into the shape, structure, and nature of the contractual arrangements. Decisive for relationship management here is the ‘tightness and looseness’ of the requirements specified in the contract. This determines, in respect of relationship management, the degree to which

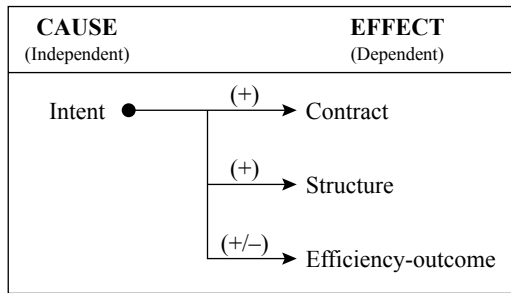


Fig. 9.1. *Intent links*

managers can depend on the contract as a guide to effectuating the arrangement.

In terms of structure, strategic intent prescribes the size, complexity, and stability of the venture. These are decisive factors influencing relationship management, defining for example the extent and costs of the deal, the number of suppliers, and the length of the venture. Hence, strategic intent will also inform the resources to commit to the management structure for handling the relationship. The findings generally suggest that for any deal resourcing should span four groups of management that include senior oversight managers, senior operational managers, operations managers, and technical managers. The number of managers involved depends in part on the organization’s management culture, the size, and the complexity of the undertaking. For example IR started with a team of forty managers, whereas ESSO had only four managers.

Strategic intent also affects the outcome of the outsourcing venture in terms of outlining the client’s objectives. This implies that depending on the outsourcing intent, procedures need to be put in place that ensure achieving the objectives and managing the expectations. The negative effect of intent on outcome occurs when the objectives are not clear. In their study of fifty deals, DiRomualdo and Gurbaxani (1998) found poor outcomes are often due to unclear intentions and goals, and not aligning these with the contract and relationship. Xerox and the IR case illustrate such circumstances, where intent is so dynamic and uncertain that few clear goals can be pursued. In turn, relationships also suffer when strategic goals are at a too high level to inform local operations, or be influenced by local intents and conditions.

Contract Management in Relationships

The contract not only outlines the ‘bare bones’ of the deal, it assumes a much more active role in relationship management. Indeed, the contract governs relationships over their lifespan. The framework, therefore, argues that the contract is implicit to most interorganizational operations—be they strategic,

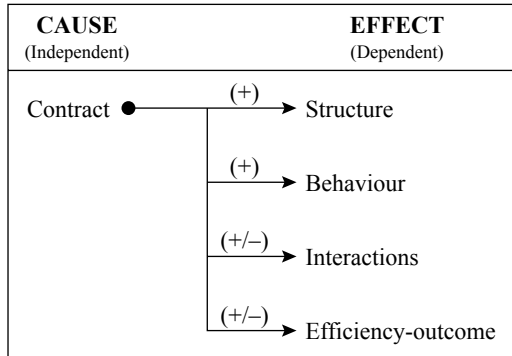


Fig. 9.2. *Contract links*

technical, or operational in nature. It often delineates the area of operation, circumscribes the tasks and activities, and identifies key deliverables for the short and long term. Therefore, it should not be perceived just as a ‘shield and sword’ as lawyers so often emphasize, but as an integral means to clarify, guide, and aid managers in achieving the outsourcing intentions. In line with Macneil’s (1974a, 1974b) and Macaulay’s (1963) suggestions, the cases illustrate that contracts are essentially vehicles for ‘relational development’. Managers on both sides, especially during the transition period, look to the contract to provide structure to their operations and to describe their roles and tasks. Contract management in this respect was found to have a positive and negative impact on structure, interactions, behaviour, and efficiency outcome of relations (see Figure 9.2).

In terms of delineating the relationship, the contract incorporates a macro-structural overview of the deal. This comes back to the ‘bare bones’ notion identifying the parties involved (i.e. size), outlining to a certain degree the complexity, specifying the length (i.e. stability) of the venture, and giving some indication of key individuals and processes (as for example in the IR). The case findings suggest all of these should be integrated into the contract, as well as details of the management structure. The cases highlighted the problems that emerge when they are not. In terms of managing structural issues, the contract managers or contract group will then assume an important oversight and control function of the relationship. They will become a key reference point for problem adjudication and performance monitoring at the operational level.

The contract, and particularly the degree of promissory clarity, has a strong impact on the exchange content, i.e. service levels. In terms of management this link determines whether client managers are able to monitor and oversee the vendor’s performance, and generally control their outsourcing destiny, or not. The importance of this causal link emphasizes the criticality of short-term clarity and long-term requirement transparency. Presentation of services in

turn needs careful planning and regular review to ensure interactions remain accurate. Good practice according to the findings suggests that contracts should be realigned and updated to ensure representativeness either on an annual or at least on a two-year basis.

The contract also sparks a particular set of behaviours in managers with both positive and negative effects. Most commonly, it gives rise to a sense of power or dependency (Lacity and Hirschheim 1993; Kern and Silva 1998). Operation managers should be particularly aware that this will affect their attitudes in terms of being cooperative or in control.

Finally, contract management influences relational efficiency and outcome. It is evident that contractual uncertainty in terms of promissory clarity and presentation will increase transaction costs, as it raises coordination efforts. The issue of bounded rationality will undoubtedly arise as it is impossible for managers to foresee and unambiguously define every contingency that could possibly be relevant (Blois 1996). This will in turn invite vendors to behave opportunistically. The contract plays an important part in compensating for uncertainties, while it may equally introduce uncertainties. In terms of outcomes it is important that contracts state explicitly what is expected from the supplier. Only by carefully stipulating the requirements and managing the contract will clients achieve their outcomes. However, bounded rationality always needs to be taken into account—a key role, indeed, of relationship management.

Structure in Relationships

Structure was shown to be a surprisingly overlooked aspect in relationship management. In fact, mismanaged structure was responsible for the greatest relational problems. The most common issues were misalignment of either party’s management structure resulting in operational and/or management

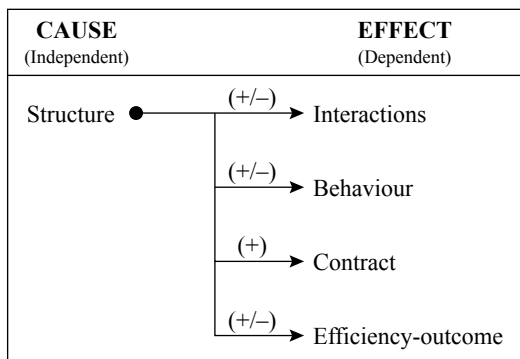


Fig. 9.3. *Structure links*

'bottlenecks' and asymmetric centrality of information. Structure in general has a wide impact, but at the micro (i.e. relationship) level it particularly affects interactions, behaviour, contract, and the efficiency outcome of relations (Figure 9.3).

A well-functioning management infrastructure that is sufficiently resourced in terms of vertical and occupational density had a positive impact on managerial behaviour. It increased willingness to cooperate and allowed relational trust to evolve. The impact further gives rise to what Uzzi (1997) calls 'embeddedness' of relationships, which becomes particularly explicit with the arrival of joint problem-solving, trust, and rich information sharing. The effects of embeddedness can lead to substantial economic and relational benefits (as ESSO and BAe experienced). However, structure can also have negative behavioural effects, particularly when management resourcing problems persist over time or when the centrality of information is one-sided (e.g. in the Xerox-EDS case).

An appropriately resourced management structure is critical for effective communication in the relationship. This raises the stakes of having an appropriately resourced structure in terms of its vertical-occupational density. Successful relationship management has been shown to depend on the 'sharing of rich information' at all levels of the management structure. The findings suggest management representation needs to include senior management, a senior operations manager, an operations manager (multiple tasks of strategy, contract, and technical oversight) and technology managers. The work by Feeny and Willcocks (1998) as outlined in Chapter 1, receives further endorsement here. Effective communication becomes particularly important if the objective is to access value-added benefits. Structure has also been found to influence negatively the contract in situations of considerable complexity and size; the reason is that both size and complexity make promissory clarity and presentation difficult to achieve (cf. Xerox, IR, and BAe). In turn, management should be prepared to encounter significant relational inefficiencies and difficulties in such situations where a sizeable proportion is outsourced and/or those functions contracted out entail substantial complexities. Therefore, an adequately resourced management team with expertise in contract management seems fundamental.

The findings further suggest that structure has a significant positive and/or negative effect on the relationship's efficiency outcome. Its primary impact is on transaction costs, and the degree of customization and uncertainty reduction experienced. Coordination, i.e. transaction costs escalated in those cases where an inadequate management team operated that subsequently had to be revamped and enlarged. The case findings also revealed that as complexity increases, so will specificity, uncertainty, and coordination costs. BPX's incremental outsourcing approach is a prime example. However, complexity costs can be controlled through formalizing requirements early on (diminishing uncertainty), updating service levels regularly, and closely overseeing the

vendor’s performance. These tasks become particularly important since an increase in complexity proportionally increases transaction specificity. As the need for customization increases, so also does the pressure on the relationship and the venture to be efficient. The relationship management task, in turn, becomes one of handling this tension.

Interactions—Process Management in Relationships

Process management in outsourcing is a relatively uncharted area and this study makes a positive contribution to its understanding. The framework prescribes processes as exchange, normative, and communication, and characterizes these along the lines of formal, informal, and/or standardized (i.e. institutional). Figure 9.4 depicts how interactions primarily affect contract, behaviour, and efficiency outcome. The study’s findings revealed that the core focus of process management is on exchange and communication. Operational managers thus need to concentrate their activities on planning, monitoring, and controlling these aspects in relationships.

One interesting finding is that interactions tend to negatively influence contracts. How does this happen? After all, some would argue, as we sometimes found, that interactions are positive in that they can fill in for incomplete, ambiguous contracts. But through interactions, exchange content changes and adapts over time to requirements, and as these change, contracts become unrepresentative and incomplete. New norms may develop as customs and practice render the contracts less representative. This may have a positive side, but what happens if a large discrepancy develops between the contract and informal custom and practice about acceptability of what is delivered and how? To reduce the negative impacts this can have, it is important to ensure that any changes are documented so that they can be integrated at a future contract alignment or update stage. Regular formal updates are fundamental. If they are neglected and dispute situations arise, parties will not have too few secure reference points for adjudication.

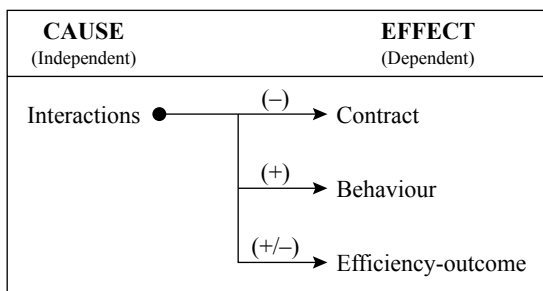


Fig. 9.4. *Interaction links*

Moreover, interactions were found to have a positive and negative behavioural impact in terms of exchanges and communication. Clarity in terms of exchanges can help to balance the degree of dependency. Exchange content clarity gives operations managers the means to control vendors' performance. A similar situation was evident for communication. Information generally gave managers power to monitor, enforce, and reward vendors. Asymmetry in either of them towards the vendor was found to put serious strains on the relationship, which stresses the importance of ensuring control over processes.

Most critical for the efficiency of the relationship was the exchange content's impact on the degree of uncertainty in the venture. Clearly, the uncertainty surrounding the core process of exchange in the relationship causes operational difficulties for managers, often giving rise to increased coordination costs and potential threats of opportunistic behaviour. Conversely, a high degree of clarity has a positive mediating affect on uncertainty and will minimize coordination costs and opportunism. This again implies careful management of exchange content in terms of clarity, completeness, and comprehensiveness.

Behavioural Impacts on Relationship Management

As noted in Chapter 8, outsourcing relationships emerged as being dependent, control (i.e. power) oriented, adversarial (i.e. conflict based), cooperative, and/or trusting, following closely our framework's delineation of behavioural dimensions. Over time these varied, even in the same outsourcing arrangement. Behaviours affect relational operations in many ways, and are integral to operations; but in this study behaviours were found to particularly influence interactions and the efficiency outcome of the venture (see Figure 9.5).

Behaviours were found to have a positive and/or negative impact on interactions in terms of improving communication (e.g. BAe and ESSO cases). Cooperation and trust in particular were found to affect the kind of information that was shared between the parties. The cases illustrated that as individuals grew more accustomed to each other and confidence increased, parties began to share 'rich information' (Uzzi 1997) about particular pressures and/or difficulties. The achievement of 'relational trust' in this form proved extremely

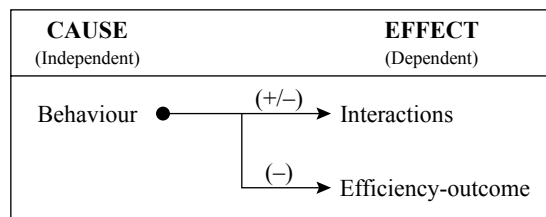


Fig. 9.5. *Behaviour links*

useful as, through the sharing of information, suppliers could apply their expertise and resources to add value or improve services.

Conversely, conflict and power and/or dependency asymmetries were shown to seriously diminish managers' willingness to communicate. In some cases communication was restricted, for example, to the transfer of information concerning only operational matters. Behaviours thus constrained one of the core processes, which in turn had a negative impact on the efficiency outcome of the venture (see for example ESSO and BPX). Curtailing the information flow will hamper operations and is likely to increase coordination costs to balance the lack of information. Relations in this way are likely to become inefficient and endangered by vendors' opportunistic behaviour. Awareness of these impacts can help managers anticipate and avoid inefficiencies.

Planning for Relational Efficiency and Outcomes

The case findings highlighted that clients and vendors have a strong tendency not to plan and resource sufficiently their relationship management arrangements prior to outsourcing. As a result, relational operations were often inefficient and prevented clients from achieving their goals. Three areas in particular suffered from this planning neglect—contract management, structure, and process management. All three had to be subsequently addressed, and this required significant investments in time, expertise, and resources. These areas were shown generally to be prone to transaction, i.e. coordination, costs due additionally to the factors of uncertainty, and increasing specificity.

In terms of preparation, the findings suggest that for, contract management, clients should shorten their promissory, i.e. service level planning horizon to a length that allows them to clearly presentiate their requirements. The cases suggest an annual renegotiation phase as best practice (see BPX and ESSO). In addition management should be prepared for unexpected promissory gaps, and may want to plan for procedures that provide adequate flexibility to compensate for such occasions. One suggestion might be to formalize an oversight board. This brings us to the second planning issue, namely structure. Client organizations should formalize a relationship management structure that comprises at least adequate competencies and skills to handle the relationship at the strategic and operational level, the technical requirements, and the contract in terms of service levels and legal matters (see Feeny and Willcocks 1998; Fitzgerald and Willcocks 1994). Once a structure has been formalized, vendors should be asked to present a formal management structure that identifies clearly the interface points, which at best should mirror the customer's structure. Of particular importance here is to check the contact points, i.e. information flows to avoid potential 'bottlenecks' (see Xerox case).

This brings us to the final issue of process planning. The cases emphasized the importance of regular information exchanges to ensure measurability of the vendor's performance. In terms of payments these exchanges are fundamental.

Thus formalizing the processes that ensure these exchanges seems good practice. Again, this requires cooperation between the parties to be able to define an appropriate management process. The case findings suggest at least weekly, monthly, and half-yearly or yearly management meetings should be established.

Careful planning of these issues contributes to ensuring an operationally efficient relationship and achieving outsourcing intentions. The value of being aware of the ‘efficiency’ dimension in terms of transaction costs, uncertainty, and specificity will help a client identify costs that it may need to anticipate and manage. Relationship efficiency does affect outcomes. But outcomes themselves need managing as much as any other part of the relationship—witness BPX’s use of the balanced scorecard, for example. Early clarification of the expected outcomes, such as the areas, for example, where innovation is expected will improve the possibilities of actually achieving them. In turn the framework provides a helpful overview for the purpose of planning, offering practitioners some valuable insights into how to conduct post-contract management and relationships.

REVISITING THE ANALYTICAL FRAMEWORK

The findings largely support the analytical framework’s characterization of the main dimensions of outsourcing relationships. However, a review of the evidence highlights for us four significant issues that could be usefully incorporated into the framework (see Figure 9.6).

1. *Endogenous and exogenous factors* were shown in the case studies to have a significant influence on outsourcing and the subsequent relationship. Endogenous factors that need consideration in this respect are the client’s overarching long-term vision, the business strategy, including the short-term organizational goals and objectives, and the IT strategy. In regard to the business and IT strategy, the outsourcing venture and hence relationship will have to be aligned to ensure the relationship provides the required services, technology, and benefits to achieve both the long- and short-term goals. Disregarding alignment may introduce inflexibility and additional cost factors. Conversely, exogenous factors were equally shown to influence operations as legislative, market dynamism, technological, competitive and economic factors affect the organization. A ‘systems theory’ perspective might be useful here to emphasize the ‘interactional’ impact exogenous factors may have on the organization and the outsourcing relationship.

2. *Contract complexity* was revealed as a significant factor to consider, especially in terms of operability. The findings showed that a too complex contract can hinder operations and relationship development, and introduce significant additional costs. A balance needs to be achieved by yearly contract revisits that help to maintain the up-to-dateness of the contract and service levels.

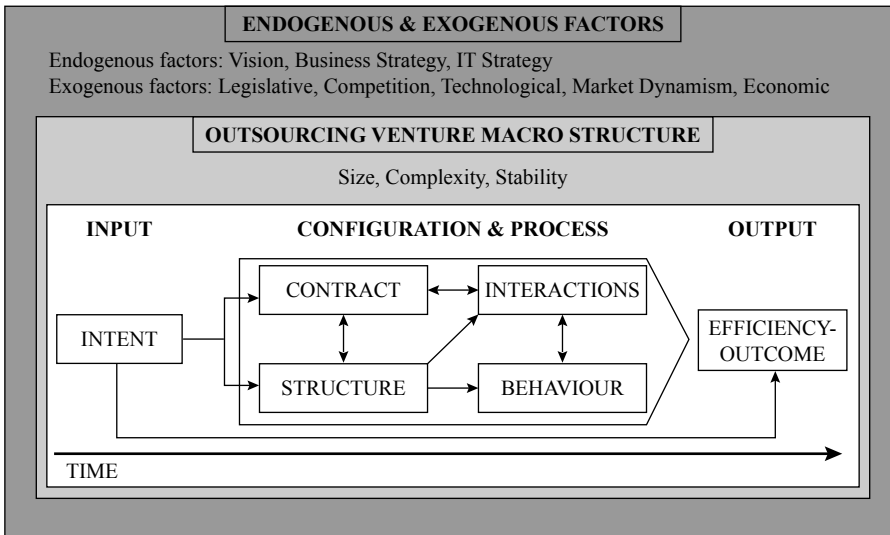


Fig. 9.6. Revised framework of outsourcing relationships

3. *Structure* in outsourcing needs to be considered in terms of both a macro and micro level. At the macro level, structure defines the overall shape and structure of the outsourcing venture. Findings show this to include size (e.g. number of parties and costs involved), complexity and overall length (i.e. stability). At the micro level or relationship level, structure focuses on the vertical and occupational density of the management infrastructure, the operational complexity, and the overall stability.

4. Finally, the rich case histories revealed that the relationship dimensions are *linked* in a number of ways that differ from, and could not really be incorporated into the initial assumptions. These are integrated into the revised framework, which now clarifies further how these dimensions and their elements are connected.

From the research undertaken for this book we are able to make three further reflections useful to improving relationship management practice, and achieving relationship advantage.

AVOIDING THE WINNER'S CURSE

IT outsourcing emerges from this study as mostly a high-risk, hidden-cost process. Explicit risk mitigation and relationship management practices are needed, as delineated in this book, if IT outsourcing is to leverage the IT services

market for business advantage. In the previous chapter and above we summarized many of these practices. However, here we would like to draw attention to a particular risk that seems to go to the heart of managing the cost-benefit trade-off and that can affect either or both client and supplier adversely (Kern, Willcocks, and van Heck 2000).

One of the more intriguing phenomena in auctioning/tendering is the winner's curse. The winner's curse occurs if the winner of an auction/tender systematically bids above the actual value of the objects and thereby systematically incurs losses. Acceptance of a bid in general is an informative event, and the failure to incorporate such contingent information into the bidding strategy can lead to excessive bids and subsequent losses for both parties. The outsourcing selection and bidding process has strong similarities to an auction situation, where various suppliers may be asked to make an offering for a proposed IT business, even though the exact value and service requirements can often not be clearly determined. Invariably, for both sides, there is also only incomplete information available. In BP Exploration's undertaking, for example, six suppliers were eventually asked to bid for the offered services in circumstances where the exact future service requirements were not certain. Decisive criteria for winning such bids tends to be costs, value-added benefits, technology, expertise, capabilities and reputation or prestige of bidders. The difficulty in such bidding circumstances is to select those supplier partners that offer the best deal, and here the focus tends to be not least on what cost efficiencies suppliers can deliver (Ang and Straub 1998; Lacity and Willcocks 1998, 2000*b*). The assumption here is that suppliers have sufficient economies of scale, and improved IT management practices, to be able to deliver improved services for a cheaper price, and that the resulting savings are those that the client will benefit from.

Two dangers have become more apparent over the years to researchers studying IT outsourcing experiences, and from this study. One is the often large disparity between what suppliers initially tout in their proposals and what at the end of the day is delivered. In fact, some companies and government institutions have found outsourcing services to provide few measurable improvements or additional benefits (Kern 1999; Lacity and Willcocks 1998); and in the late 1990s some have even subsequently terminated contracts early (for example American Express, East Midlands Electricity, Sears UK). These and similar cases seem to suggest that suppliers can be overly keen to win a particular deal for possible reasons of prestige, size, partnering, costs, and long-term business opportunities.

The second, related danger lies, as this study shows, in the general lure of ridding oneself selectively or totally of the 'bottomless IT investment pit' and instead paying a fixed monthly sum for IT services. This remains a major comparison measure for selecting a supplier (see also Ang and Straub 1998; Lacity and Willcocks 1998, 2000*b*), though we do not fail to recognize that organizations typically outsource for a mix of reasons.

However, a client's focus on cost savings can drive supplier organizations into the corner of making service delivery promises that are initially calculated on a slim or even nil profit margin (Willcocks, Lacity, and Kern 2000). They may do so, for example, because they are short of business due to recession, decreased competitiveness, or are a new entrant into the IT services market; they are keen to enter a new market segment; they want to shut out competitors; they have a strategic intent to dominate certain market segments; and/or they believe that they can recoup the investment and broaden margins later. It is precisely in such circumstances that the danger of a 'Winner's Curse' arises, as suppliers make bidding promises to ensure they win the contract, but inherently already know, or subsequently discover, that they are unable to recover their tendering, business, and operational costs, at least in the near future.

Instead they hope, as research has shown (Lacity and Willcocks 2000a, 2000b) that they can recover their costs by, for example, identifying service areas that are in need of particular attention and responsible for low service performance, and/or areas of immediate service provision excluded from the contract but needed operationally, so meriting excess fees. In addition, suppliers will attempt to offer additional services from their portfolio of technology capabilities, service management, and consultancy services over the life of the contract. Since supplier account management will need to concentrate disproportionately on recovering costs, and may well be under pressure from its senior managers to make stipulated margins in unfavourable circumstances, it is more than likely that trade-offs will occur that disadvantage the client. For example, case studies demonstrate that decreasing costs to the supplier can result in decreases in service quality and additional costs for the client (Kern 1999; Lacity and Hirschheim 1993). A supplier's disproportionate concern for containment of its costs can lead to inflexibility in the interpretation of the letter and spirit of the contract, which can also lead to adversarial relationships (Currie and Willcocks 1998). Thus operational performance and the client-supplier relationship will receive less attention and suffer (Kern 1999). As a consequence, we suggest that in 'Winner's Curse' situations suppliers may risk the success and effectiveness of the operations and outsourcing relationship as their focus settles primarily on recovering their costs, rather than on developing and maintaining the relationship and mutual objectives. A supplier would thus undertake opportunistic behaviour, seeking to reduce its own operational costs, often at the expense of the client.

We provide Figure 9.7 to dramatize the main possibilities in IT outsourcing. The Figure should be read as an indicator of the main extreme outcomes. In practice the experiences of many organizations will fall between these extremes. Furthermore organizations, through behaviours and actions of the interested parties, may well change positions, as was the case, for example, in the IT outsourcing arrangement at ESSO-ITNet.

Amongst our cases, the ESSO-ITNet case is the most obvious example of a winner's curse. Here ITNet over-bid and subsequently could not make its

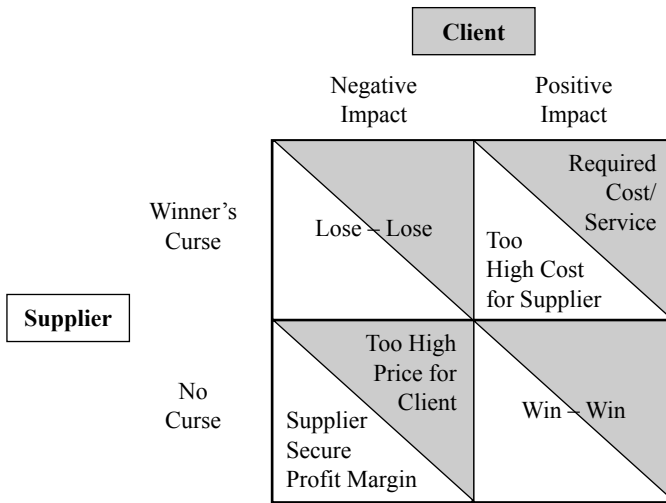


Fig. 9.7. *The winner's curse and other scenarios in IT outsourcing*

Source: Kern, Willcocks, and Van Heck 2000.

margins. The client contributed to making this a winner's curse for the supplier by tightly controlling price and service levels. But the supplier became so disadvantaged that service levels deteriorated and in fact both moved to the Lose–Lose quadrant in Figure 9.7—in other words a 'winner's curse' for the client also became an outcome. As we saw in Chapter 6, this was only changed when a relationship dimension was brought to bear, and when the contract was mutually reconstructed to move both parties to the Win–Win quadrant of Figure 9.7.

The bottom left quadrant is also a danger area for the client. As our case studies showed, it is quite possible for a supplier to disguise the fact that the deal is actually in this quadrant, by offering for example cost savings on parts—usually the more visible and front-end parts—of the deal. Thus at both Xerox and the IR EDS felt able to guarantee cost savings on operations and present requirements because it calculated that it could make much larger profit margins on future work. Xerox reacted against aspects of this subsequently, while BAE and the IR both experienced rising costs in the overall IT budget without always knowing exactly how to attribute these costs and how far the developing cost-service trade-off represented value for money.

Of course, such circumstances are rarely publicized and made explicit, but other evidence of them does exist (Lacity and Hirschheim 1993; Lacity and Willcocks 1998, 2000b). Indeed the possibility of these more adverse outcomes arising may well be increasing, if the growing competitive pressures on suppliers push them to compete increasingly on prices and service deliverables (Willcocks and Sauer 2001). There emerges from our study the importance of negotiating

contracts that allow a supplier a reasonable profit. But more than this the relationship management practices delineated in this study become a critical influence on how far the more adverse outcomes can be anticipated and mitigated.

TYPES OF RELATIONSHIP: IMPLICATIONS FOR MANAGEMENT

Distilling our findings, there emerged from our cases a strong relationship between the strategic intent a client organization chose to pursue, the kind of technical capability it needed to employ, and the type of relationship needed to match intent and supplier capability, and achieve expectations. A strong finding from this, and complementary research (Lacity and Willcocks 2000b), is that there are frequent misperceptions on the part of all parties as to the nature of the relationship, and what can be expected from each other as a result. Let us, first, classify the types of relationship we have observed, then illustrate, through examples, the importance of getting strategic intent, technical capability, and relationship definitions aligned.

The main types of IT outsourcing relationships are classified in Figure 9.8. Here strategic intent, in terms of expectations from outsourcing, is divided into whether the focus is on achieving business value and/or on achieving IT

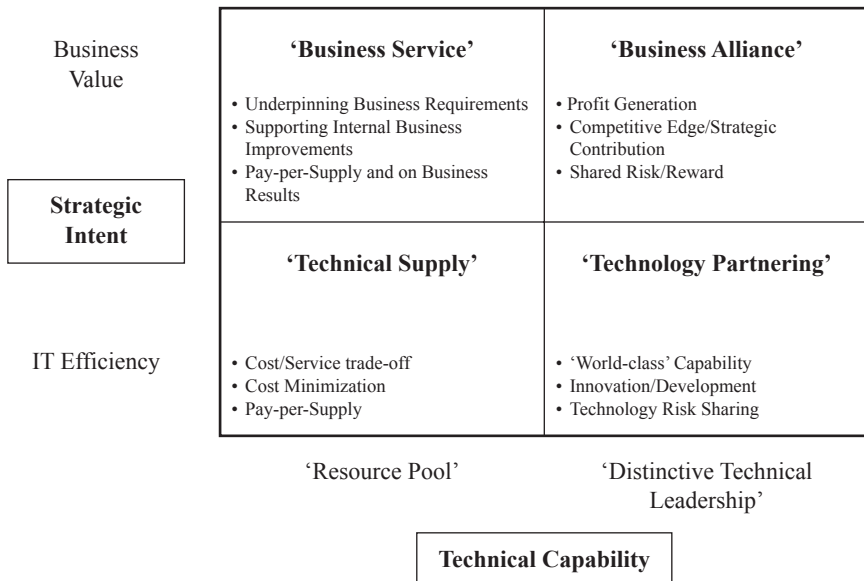


Fig. 9.8. IT sourcing relationships: intent and capability

efficiencies. On the horizontal axis, technical capability refers to choosing to externally source to gain a distinctive technical leadership, or to gain access merely to technical resources that form a resource pool not otherwise available to you, in cost per quality terms. The matrix sets up four possible relationships. By far the most common is the 'Technical Supply' relationship where the objective is to achieve IT efficiencies by hiring external resources. In such a relationship the fundamental focus is on cost minimization, and the rendering of IT as a variable cost. The major debates will centre around the cost-service trade-off, and measurement systems will also be constructed around this. The most obvious example in this study is the ESSO-ITNet arrangement. However, large components of the Xerox-EDS, SEMA-BPX and Syncordia-BPX, IR-EDS, and BAe-CSC deals were also of this nature, especially in the telecoms, mainframe processing, base operations, and support areas. One thing we have learned in this study is that even these elements need careful management not just on the contract, but on all the relationship dimensions (Kern 1999).

Another possible relationship we call 'Business Service'. Here the objective is to use an external IT supplier who can improve service to the business by not only delivering more precisely on changing business requirements, but also by, for example, being involved in business process improvement projects. Here the contract will be about both IT efficiency for business impact, and the supplier's contribution to business improvement. Here one would expect additional processes and relationship mechanisms for involving the supplier more closely in business issues. The evaluation debate would be more on business value and suitable metrics, based on the business impact of supplier performance. In this respect it is interesting to note that on some figures business process outsourcing may reach \$US14.7 billion in revenues in 2002. Again, BAe, Xerox, and the IR all perceived themselves as having 'business service' components in their deals with their major outsourcing suppliers. One example we noted was at Rolls-Royce in 1997/8, where EDS and its management consulting arm, A.T. Kearney, participated in business re-engineering projects with Rolls-Royce staff and were to be rewarded proportionate to the business improvements.

A third type of relationship is 'Technology Partnering'. BPX, for example, explicitly chose three suppliers because they had 'best-in-class' capability in particular areas. BPX expected future-proofing on the technological front, with the suppliers keeping BPX abreast of leading-edge technology, and also proactively innovating in technologies and their application to BPX. EDS and CSC presented themselves as potential technology partners in the IR, Xerox, and BAe cases also. Here one would expect sharing in technology risks, but also a sharing in the benefits that resulted. Here the supplier takes the lead on many IT issues. The focus is on innovation and supplier proactivity, a premium IT service, and leading-edge IT.

One creative example is the joint venture between FI Group and Bank of Scotland (BoS). In June 1998 they formed First Banking Systems. By 1999 the venture comprised 310 people from the BoS, and 120 people, including project

managers, from FI. Both groups remained employees of their respective companies, and both groups kept their own terms, conditions, and pay rates. FBS is jointly owned. The deal committed the bank to underwrite £30 million for five years. FI Group takes a loss on any costs over the fixed price. The joint venture has worked on development projects for the bank, including a new core banking system. In the first year FBS reduced overheads, and brought in new customers from the Bank of Scotland Group.

Finally, all too many large-scale outsourcing arrangements are presented as 'Strategic Alliances'. For us such an alliance assumes a working together to make offerings to the external market place, as for example at Xerox-EDS, and sharing risks and rewards of such endeavours. The focus here is on business expansion, the main debates will be around business goals, mutual contribution, and shared rewards. Lacity and Willcocks (1998) found many so-called strategic alliances in IT outsourcing to be largely fee-for-service contracts; moreover the risk-reward elements were too small a part of the relationship to make a difference in terms of motivation and focus. This was certainly the case in Xerox-EDS. One successful example was that of Philips Electronics, in the early 1990s, when it formed Origin with a Dutch-based software house. Over time Philips' development staff, then its data centre and processing staff went over to the jointly owned Origin, which provided services back to Philips, but also built up an external clientele for its services.

Clarifying these options, and when they are most suitable, is an important precondition for establishing the right relationship mechanisms and evaluation regimes. In practice we have seen all too many organizations contract and manage tightly for cost efficiency, but then also expect the sort of business value-added that could only be got from a 'Business Service' relationship, or the technical innovation and proactivity that could only be provided through 'Technology Partnering'. This partly explains why BPX was disappointed with at least two of its 1993–8 suppliers. In another way, and much to CSC's frustration, BAe managed CSC tightly though the deal ostensibly had 'Business Service' and 'Technology Partnering' components. It was only after several years, and after CSC had made large investments in making the IT function efficient, that BAe managers started being interested in allowing CSC to tap the other possibilities for revenue.

Cultural and financial factors often drive these misconceptions. We saw in BPX how early on traditional cost reduction approaches prevailed in the deals though the deals had been paraded as more about technology partnering. At the same time, for example, a supplier will find it difficult to sustain a 'Business Service' or 'Technology Partnering' orientation if the money is not going to be there. Sometimes it is lack of the right kind of partnering capability, in either or both client and supplier, as we saw in the IR early on, and at ESSO-ITNet. More frequently there is a lack of clarity at the scoping and evaluation phases of IT outsourcing, to identify precisely which components require what metrics and what relationship arrangements.

This is not helped by the fact that for any IT outsourcing deal of any significant size, different parts will be founded on different intents, and need qualitatively different relationship and evaluation arrangements. For example, Xerox clearly applied the notion of a 'strategic relationship' to apply to the vast majority of its deal, when certain parts required a business service orientation, and still others a technical supply or technology partnering one. BPX kept asking where was the value-added, but had put in relationship structures and processes, and had regional cultures that inhibited this value-added coming through. The situation becomes even more confused when there are a number of suppliers because each might require a different set of relationships, given the strategic intent for that part of the deal, yet the pressure may be on to treat them all in the same way—as was the case for example at BPX.

Given these considerations we offer the framework in Figure 9.8 as a way for a client to think through exactly what he/she is trying to achieve with different parts of its IT outsourcing, and what the implications of this analysis might be for relationship arrangements and assessment regimes.

MANAGING THE RELATIONSHIP ADVANTAGE ACROSS SIX PHASES

In complementary work in which both authors participated, we were able to identify six major phases in IT outsourcing arrangements (see Lacity and Willcocks 2000*a*, 2000*b*). A summary of these phases, and what the major focus of each needs to be, is shown in Table 9.1.

The present study corroborates this as a highly useful classification, and confirms the relevance of the objectives and tasks for each phase, as detailed in the table. From its findings in looking at over 100 case histories and carrying out extensive survey research, that previous work also brought attention to bear on why relationships were so difficult to manage, and also clarified the different kinds of relationships that could be found even within the same deal. Thus, that study pointed out the number and complexity of relationships to be found. It identified eight major groups of stakeholders each with their own set of expectations. Within the customer there are invariably senior business managers, senior IT managers, IT staff, and IT users. Within the supplier can be found senior managers, account managers, and IT staff. Invariably, as we found in all our case studies in the present study, there are a number of other contractors and subcontractors also providing IT services. Given that the expectations and goals of these stakeholder groups will frequently not coincide, it can be seen that relationship management in the areas studied by this book—intent, contract, structure, interactions, and behaviour—becomes a significant task.

The present study also corroborates our previous finding that stakeholder relationships are quite dynamic. For example, the same two people can fight

one minute, and collaborate the next. Four types of relationships were evident in both studies. The first was *tentative relationships*, when stakeholders had no shared history, and were unsure whether goals were shared, complementary, or conflicting—see for example all our cases at their beginnings. Secondly, we observed *adversarial* relationships when stakeholder goals were felt to be in conflict e.g. over realigning the contract at Xerox, on EDS's asset re-evaluation at the IR. Thirdly, stakeholders often operated *collaboratively*, where goals were shared, for example where supplier senior managers and account managers had the shared goal of negotiating a deal with enough leeway to ensure profit margins. Finally, *cooperative* relationships manifested themselves when goals were complementary. At Esso-ITNet each party needed something from the other party to succeed, thus moving the arrangement from a 'winner's curse' for both supplier and customer, to a more productive relationship.

However, the present study also deepens our understanding of what it is to manage across the six phases in three ways.

1. *The Relationship Dimension*. Our previous study focused a great deal on relationships in IT outsourcing. However, while it provided a great deal of rich evidence on how relationships were conducted, and many guidelines for practice, it focused on many other salient issues, and did not arrive at a comprehensive, codified understanding of the main elements in relationships and how they can be managed. The present study suggests that relationship management is something that deserves fundamental attention at the scoping phase, using for example the thinking embodied in Figure 9.8. Thereafter the construction, staffing, and dynamics of relations require specialized management, across all other subsequent phases. Here the thinking and prescriptions distilled and represented in Figure 9.6 becomes a comprehensive management guide, if relationship advantages are to be gained.

2. *Evaluation and Relationships*. Previous studies, by ourselves and others, have always come back to the importance of measurement/evaluation in IT outsourcing (see also Chapter 1). Dynamic, accurate evaluation is invariably placed by researchers and those involved in IT outsourcing as a 'necessary but insufficient' condition for success. On reflection, the present study actually shows there to be no great gulf between measurement and the relationship dimension; they actually should be mutually supportive. Put more boldly, implicit within Figure 9.8 is the notion of a fully working evaluation and metrics system, supporting the type of relationships being erected. We can see such evaluation regimes at work, though not always functioning optimally, in all our cases, with BPX perhaps being the most mature and consistently successful. Our observation is that the appropriate evaluation regime, arrived at in Phase 2 of Table 9.1, and incorporated in the 'Contract' dimension in Figure 9.6, is fundamental to achieving what we call 'the relationship advantage', with the other components in Figure 9.6 ensuring that the evaluation regime is in the right set of contexts and properly actioned. Let us consider this proposition in more detail, using an example.

Table 9.1. Six phases of an IT outsourcing arrangement

Scoping phase	Evaluation phase	Negotiation phase	Transition phase	Middle phase	Mature phase
Activities					
<ul style="list-style-type: none"> ● Identify core IT capabilities 	<ul style="list-style-type: none"> ● Measure baseline services 	<ul style="list-style-type: none"> ● Conduct due diligence to verify RFP baseline claims 	<ul style="list-style-type: none"> ● Distribute contract to IT users 	<ul style="list-style-type: none"> ● Benchmark performance to (theoretically) reset prices 	<ul style="list-style-type: none"> ● Recalibrate investment criteria to reflect shorter time horizon for recouping investments
<ul style="list-style-type: none"> ● Identify IT activities for potential outsourcing using business, economic, and technical criteria 	<ul style="list-style-type: none"> ● Measure baseline costs ● Create RFP ● Develop evaluation criteria ● Invite external and internal bids 	<ul style="list-style-type: none"> ● Negotiate service level agreements ● Create responsibility matrices ● Price work units ● Negotiate terms for employee transfer 	<ul style="list-style-type: none"> ● Interpret the contract ● Establish post-contract management infrastructure and processes ● Implement consolidation, rationalization, standardization 	<ul style="list-style-type: none"> ● Realign the contract to reflect changes in technology and business ● Involve the supplier on more value-added areas 	<ul style="list-style-type: none"> ● Determine if the relationship will be terminated or extended

Table 9.1. *Continued*

Scoping phase	Evaluation phase	Negotiation phase	Transition phase	Middle phase	Mature phase
Objective	Select best and final offer	Sign contract(s)	Establish operational performance	Achieve value-added above operational performance	No lapses in operational performance during final transition
Identify flexible IT organization, including IT activities for potential outsourcing			<ul style="list-style-type: none"> ● Validate service scope, costs, levels, and responsibilities for baseline services ● Manage additional service requests ● Foster realistic expectations of supplier performance ● Publicly promote the contract 		
		<ul style="list-style-type: none"> ● Negotiate mechanisms for contractual change, including benchmarking, open-book accounting, non-exclusivity clauses, and pricing schedules 			

We have already argued that in IT outsourcing many organizations operate on the mistaken belief that external IT vendors can be experts not only at technology supply, but at their own line of business as well. In practice, of course, expecting even a ‘world-class’ IT supplier to be similarly skilled in an area not their core business, e.g. oil at BPX and ESSO, tax collection at the IR, is unrealistic to say the least. Our cases show that if there is to be business advantage—not just technical efficiencies—to be derived from IT outsourcing, it must be driven from the business side, with the business managers and core in-house team accepting responsibility for key actions.

We can provide an example of the integrated performance measurement regime that could be put in place to support the relationships shown in Figure 9.8 in order to achieve optimal business advantage. The template in Figure 9.9, from Willcocks, Graeser, and Pisanias (1998), was developed for a major international and financial property service company (IFAPS).

The bottom half of the figure represents how outsourcing value can be maximized from the Technology Supply contribution in the ‘utilities area’ (legacy systems, mainframe, midrange, desktop, communications). Four significant features here are:

- a fully staffed contract management team—BPX, BAe, and the IR were particularly good in this area;
- A focus on developing measures that rewarded/penalized for the business impact of technical efficiency, rather than focusing just on technology performance—few of our case studies were good at this area;
- The stimulation of proactive behaviour through suitable metrics, for example how well suppliers interface with other suppliers, contract dispute, and commissioning new work metrics—again most of our cases were not good at utilizing such metrics;
- Smart contracting using market baselines regularly reviewed—all except ESSO were quite ‘smart’ on this.

With the utility systems up and running under this evaluation regime, the company would be more satisfied with its IT and suppliers, but would still be looking hard for the elusive added business value from its IT—BPX for example. The approach suggested to IFAPS was to develop an innovation team responsible for identifying additional business opportunities available from IT, for creating new business ideas, business process improvements, and step-change innovation. Business value drivers would also be regularly identified through the strategy-making process; e.g. at IFAPS these included prices to external customers, customer service/satisfaction, revenue growth.

All this needs to be converted into a measurement system. The process is shown in the top right of Figure 9.9. The business impactors for any new initiative are worked into a value proposition which can then be tested for alignment against the business value drivers. If this process is managed rigorously and in detail, various usable metrics can be derived. An important separation

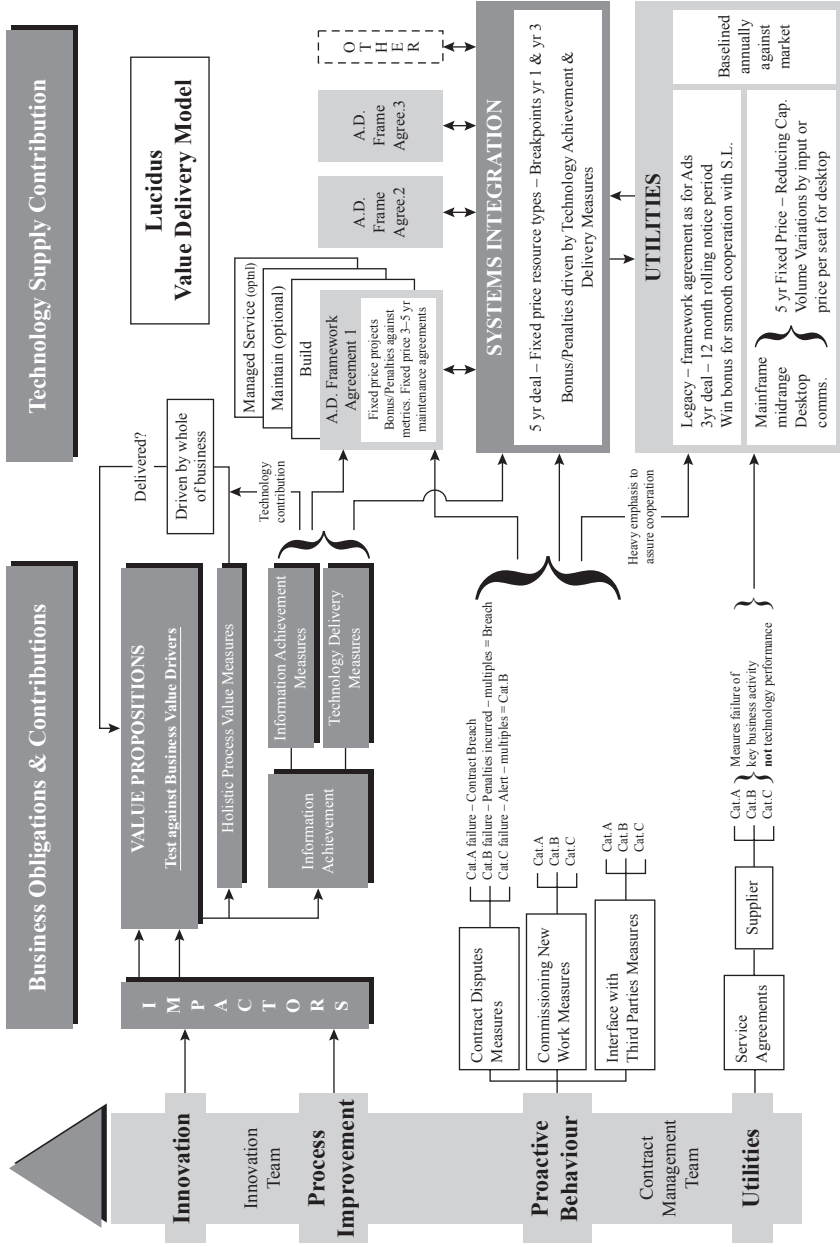


Fig. 9.9.
Example of an integrated performance measurement framework
 Source: Robert White and Lucidus.

occurs at this point between information achievement and technology delivery metrics—not once did we witness this in any of our case histories. The latter metrics are concerned with building and application of technology, for example budget milestones delivered to specification, timeliness, and efficiency of systems development. Information achievement is a more profound measure of business impact. For example, at IFAPs a centralized knowledge base was being developed. One information achievement target was the development of a library search engine for key words. One measure was that, using the system, a trained staff member could find a key word in under ten seconds.

The IT supplier would be tracked on the information achievement and technology delivery measures. Where these are fulfilled then payments, including agreed bonuses will result. Where these are not fulfilled, penalties should be raised. In the development area (Figure 9.9 top right-hand corner), if a project is abandoned, then the supplier would return a pre-agreed percentage of the development costs. It should be noted that the ‘information achievement’ measures feed into the applications development and systems integration components shown in Figure 9.9, rather than the utilities aspect of the technological supply contribution. The latter is much more about cost efficiency, while there is a lot more business value to be gained for the development area if clients know how to set up suitable measurement systems, incentivize suppliers, and link activity with business goals.

Though BPX linked supplier measurement with its own balanced scorecard system, no other client organization in our study came near putting in place such an integrated performance measurement approach. All—even BPX—complained of not achieving much valuable innovation, process improvement, and business value-added from their suppliers. However, we are very clear that unless an integrated performance measurement system—something like the one described here—is put in place to underpin, inform, and guide relationship management, this would continue to be an unsurprising outcome. In this area, as in many others, as we pointed out in Chapter 1, client organizations still expect too much from the supplier, and not enough from themselves.

3. *Supplier Capabilities.* We would like to draw attention to one final area that has received virtually no academic study, and is often in practice assumed to be unproblematic, but in fact emerges from our study as quite critical. It is intuitively obvious that suppliers too are heavily involved in relationship management, but all our cases show examples where they were not necessarily good at these tasks. At the IR it was at the client’s insistence that relationship processes and staffing began to happen. At Xerox, and BPX, the organization of supply and account management sometimes left something to be desired. At ESSO, ITNet was as responsible for the collapse of the relationship as the client. At BAe the partnering word was informally banned for a time as a result of disconnects between the supplier’s relationship promises and actual behaviours. This suggests that, just as we identified core IT capabilities for the client, so we need also to begin to identify core supplier capabilities that can help to lever-

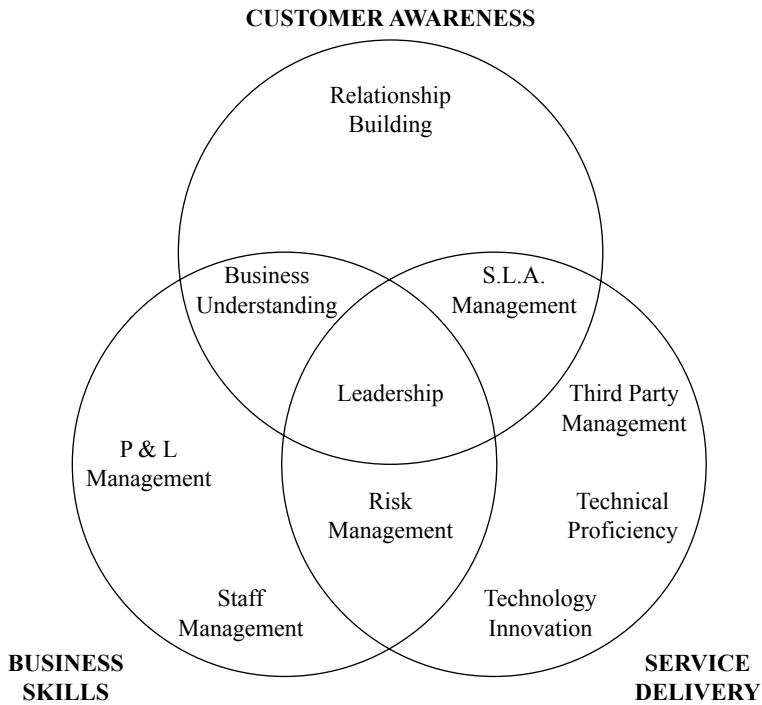


Fig. 9.10. *Supplier capabilities in IT outsourcing*

age the relationship into one of mutual business advantage. A review of the case evidence enables a first view on supplier capabilities needed to support the relationship advantage. These are shown in Figure 9.10.

Our view is that suppliers need to have three core capabilities in the areas of business skills, customer awareness and service delivery. Moreover their capabilities in these areas need to be in sufficient numbers and physically located and organized to fit with the capabilities of the client organization, and of any other suppliers involved. The proactive coordinating and governance skills lie in leadership and risk management—both applied on behalf of the client as well as the supplier. In the service delivery area the supplier needs to be able to also manage service level agreements and third parties well, and also have technology innovation capability. Its business skills, or lack of them, can directly impinge on the relationship with the client organization. These include profit and loss management (including cost control and budget management) and staff management. At the interface between business skills and customer awareness is business understanding, to include business applications knowledge and an understanding of the client’s business. Relationship building includes customer interaction skills. The interface roles of SLA management,

leadership, risk management, and business understanding are critical for coordination developing and facilitating the relationship.

This is a provisional perspective, which we intend to research much more fully, because the evidence from our study is that the possession and application of these capabilities can make a key difference to how the relationship dimension is conducted, and so to the levels of success experienced in IT outsourcing.

CONCLUSION

Our reflections for practice took us into several further contributions. A review of the many components of the relationship dimension clarified the relative importance of each, but also underlined how interdependent intent, contract, structure, interactions, and behaviour are. We also provided guidelines for planning for relational efficiency and advantageous outcomes. The original analytical framework was found to be highly useful as a guide to the issues needing attention if a relationship advantage is to be achieved. However, we developed the framework in three further ways. We noted, from our research, the additional impact of internal factors of vision, business, and IT strategy on relationships, and also of external market, economic, legislative, competitive, and technological factors. Contract complexity was also highlighted as a significant factor affecting operability. The macro structure of the venture in terms of size, complexity, and stability also engendered risks, and required much greater relationship effort. Structure at the micro level also emerged as an area fraught with difficulty and unintended consequences, as we saw particularly in BPX and Xerox.

Our study has also highlighted the manifold risks in IT outsourcing, and in this chapter we have pointed out the dangers of a 'winner's curse' arising, affecting relationships and outcomes for both supplier and client. We also pointed to the additional importance of clarifying types of relationship and developing suitable relationship arrangements and supporting evaluation regimes across the six phases of any IT outsourcing venture. Finally, a provisional statement was offered for the key supplier capabilities needed to feed into making IT outsourcing arrangements productive.

In all this, it is clear that the relationship dimension, and what supports effective relationships, are critical to IT outsourcing success. Also clear is that, if, as we believe, IT outsourcing can be conceived as achieving a relationship advantage, then this presents profound management challenges for the ways in which IT outsourcing is more typically conducted. We started this study for two reasons: because practitioners told us that relationships were key in IT outsourcing, and because, paradoxically, there were so few studies that took a relationship perspective. The book has thus contributed by showing just how important relationships are, and by providing ways forward for practitioners and researchers alike.

In a piece of deliberate understatement, a manager we interviewed once told us that in IT outsourcing there was no such thing as an instant relationship. IT outsourcing can be understood in many ways but it is certainly well to operate on the assumption that managing it to success involves dealing with a fundamentally high-risk, relationship business.

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