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Understanding the Cosourcing Decision: 
A Case Study of Credit Unions in Australia

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ABSTRACT
In a variation on outsourcing, organisations are increasingly seeking opportunities where services can be provided jointly. This paper outlines an approach that combines resource based and resource dependency theories to assist in assessing and structuring such cosourcing initiatives. Based on a case study of credit unions in Australia, it is concluded that the approach may provide organisations with an improved understanding of the cosourcing decision. The case study also suggests that one of the most difficult requirements is to balance the differing needs of participants and reveals the complexity of an outsourcing milieu which is both layered and modular.

Keywords
Cosourcing, economies of scale, core capability, resource dependency

INTRODUCTION
Organisations are increasingly seeking opportunities where services can be provided jointly. In the UK, for example, three banks and Unisys formed a joint cheque processing venture (Roberts, 2004). While Gallivan and Oh (1999) recognise a class of outsourcing – cosourcing – where a group of organisations come together to obtain a common service, a review of the literature suggests that little research has been conducted on the phenomenon. It is likely though that not all cosourcing initiatives will be appropriate and it would be useful for organisations to have an understanding of the factors that will contribute to a successful initiative. Seddon (2001) for example provides an account of the Australian Federal Government’s failed attempt to introduce IT outsourcing by “grouping government agencies (mainly departments) into clusters” (p5).

In focusing on cosourcing, this paper reflects the starting point of much of the research in IT outsourcing by seeking to address the question of what activities should be cosourced. While research examining the motivation for outsourcing draws from many theoretical perspectives, two are particularly relevant with regard to determining what to outsource from a strategic perspective: resource based theory and resource dependency theory (Dibbern et al, 2004) and form the core of the current research.

The remainder of the paper comprises two sections, The first outlines the proposed approach to understanding the cosourcing decision. The second assesses that approach through an empirical study of credit unions in Australia.

THE COSOURCING DECISION
The resource based and resource dependency theories both view a firm’s resources as being the foundation for its strategy and do not inherently conflict with each other but rather can be seen as complementary (Duncan, 2002). Here they are synthesised so that the decision regarding what areas to enter into cosourcing arrangements for takes into account both the strategic contribution of an activity to an organisation and the relationship with the ultimate supplier. Transfer of the field of investigation from organisations outsourcing individually to cosourcing also requires the addition of an additional consideration – that cosourcing offers advantages over acting individually. As Figure 1 illustrates it is proposed that economies of scale can provide such an advantage.

Economies of scale
Economies of scale refer to production and distribution efficiencies which come with larger size (Chandler, 1990), and it has long been recognised that they can be a motivation for outsourcing (Venkatesan, 1992). However from the perspective of this paper it is not just the existence of economies of scale that are of importance but also the extent to which the benefits can be appropriated by customers rather than be retained by the supplier. The literature suggests that one successful approach
adopted has been for organisations to form cooperative agreements to achieve the necessary bargaining power (Scherer and Ross, 1990).

![Figure 1. Shapers of the cosourcing decision](image)

**Resource based theory**

Resource based theory suggests that firms secure success by utilising their unique resources comprised of intangible and tangible assets that are tied semi-permanently to the firm (Wernerfelt, 1984). However such resources provide a sustained competitive advantage only when competitors are unable to acquire and deploy similar resources (Mata et al., 1995). Furthermore, according to Coyne (1986), to provide an advantage the resources must contribute to “a consistent difference in important attributes between the producer’s product and those of his competitors” (p51). From the resource based perspective, success is maximised where organisations focus their attention on those areas where their distinctive capabilities lie (Hagel and Seely Brown, 2001) and rely on others for the provision of ancillary activities.

**Resource dependency theory**

Resource dependency theory states that organisations are dependent upon their environment and are faced with choices regarding how they manage that dependency (Thompson, 1967). Kotter (1979) suggests that organisations need to adopt strategies to manage their dependency on external parties and ensure access to the resources they supply is stable and secure. There appears to be limited research in an outsourcing context though regarding the management of dependency. For example, Ang and Cummings (1997) considered the influence of the number of potential suppliers but did not consider whether and how that number could be modified.

Combining the three theories leads to the perspective of organizations outsourcing non-core activities jointly to realise economies of scale while ensuring that they, not the supplier, are the beneficiaries.

**METHODOLOGY**

The empirical focus was on credit unions which are non-bank financial institutions, owned and operated by the people who save and borrow with them. Around 180 credit union brands operate in Australia with more than $29 billion in assets and 3.6 million members. The specific area of interest was the IT services used to support a credit union's core banking system. These were typically outsourced to computer bureaus known as Independent Data Processing Centres (IDPCs).

The case study method was employed as it is seen as particularly appropriate where research and theory are at a formative stage and a phenomenon is not well understood (Benbasat et al., 1987). The case work presented here is primarily explanatory and draws upon the work of Dubé and Paré (2003) with regard to the approach followed. A multi-case research design was adopted with a purposeful selection of cases to cover the full range of credit unions. The primary unit of analysis was the set of activities outsourced to an IDPC. A degree of triangulation was achieved by interviewing credit unions that shared the same IDPC and reinforced by reviewing documentation and reports for each credit union.

A total of 14 interviews were conducted. Interviews were between one and two hours in duration and a semi-structured interview protocol was followed with questions across two principal themes: What influenced the decision to cosource and how was the resultant initiative structured. While the underlying rationale was purposeful, to collect data pertinent to the underlying research themes it was deliberately non-directive so as not to preclude the emergence of concepts not previously considered (Patton, 2002). As such it is in line with the methodology presented by Eisenhardt (1989). With regard to analysis, data was first reviewed and coded in line with the principal dimensions of each theoretical lens. Descriptive codes were used...
and interview transcripts coded in sentence or multi-sentence chunks. Such an approach is in accord with the recommendations of Miles and Huberman (1994) who suggest that the level of coding detail should be aligned with the objectives of the research. Where interview data did not code to the concepts identified a priori as of interest it was further assessed to determine if additional concepts could be formed.

RESULTS AND DISCUSSION

The interviews suggest that in this case economies of scale were the principal motivator for cosourcing and that credit unions do not see the use of IDPCs as impinging upon their core capabilities. While attempts have also been made to actively manage and mitigate dependency it is possible that they have not always been entirely successful. In addition to starting to confirm that adopting a multi-perspective approach to the decision may be useful the cases also revealed the complexity associated both with managing cosourcing and of the outsourcing milieu per se.

Motivation

In terms of the motivation for cosourcing the primary driver was seen to be economies of scale.

“If I was to negotiate Australia wide with whoever head up [Company1], number one they’d say well who are you? How big are you.. and they’d basically put me on the bottom of the pile. Or they would charge some astronomical fee for our members to transact” CU6

In addition there were seen to be benefits in being aligned with larger credit unions in that with new innovations they would tend to go first enabling the other credit unions to learn from their experiences. It was recognised though that cosourcing is not a perfect substitute to having scale in your own right.

“you can get a lot of the benefits by doing things as a group .. but we're still never going to have the full flow on like the larger institutions” CU1

Constraints

Resource based

Credit unions identified a variety of core competences ranging from personal service to having the best savings and loans products available in the market. While IT was seen as an important contributor to the business, in no cases was use of an IDPC seen as inhibiting a credit union’s ability to differentiate itself.

“What we basically said is, as an organisation, we didn't have the competencies to bring it in house nor did we want to bring it in house because it was not part of our core direction” CU13

“Our core we develop internally ourselves, which is our deposit and loan products” CU14

Resource dependency

Prima facie dependency is managed as there are a number of different IDPCs and core banking systems are available for credit unions providing alternatives

“They’re negotiating agreements and if we don’t like it we can find another bureau” CU14

“because of the relative ease of this migration, if we had to do it again in five years it wouldn’t bother me” CU12

Furthermore the IDPCs are actually owned by the credit unions. However dependency – on the IDPC or other credit unions – can be reintroduced as a result of the nature of the contracts struck or the membership structure.

“[IDPC1 has] the largest credit union on Australia and from what we understand 40% of their transactions will go [if that credit union leaves]. Now that’s a lot. One of the beauties of IDPC2 is that all of our institutions are relatively small, so we don’t carry bulk risk as such” CU1

A further dependency risk identified was that the ownership structure of the IDPCs inhibited the development of effective service level agreements

“The unique thing though about our own cooperative entities is that we never sue each other ..[and we’ve] all agreed that if a service level agreement is all about penalties and suing, then the cost goes back to the company which we all share in” CU4
“Sometimes I think that familiarity breeds contempt is one way of putting it. The funny thing is that because of that I think we take liberties that you wouldn’t want a pure commercial basis” CU14

Achieving and maintaining balance

In structuring cosourcing arrangements interviewees suggested that one of the most difficult tasks was managing the balance between the individual credit union and the group as a whole.

“There is inherent compromise in all of these systems... “CU4

Such factors are likely to limit the membership of any particular IDPC

“[Issues with a previous credit union sector wide initiative] one being it was cooperatively owned and it was slow to move and while we compromise a bit in IDPC1, there’s only ten of us, when it was 250 users you got rooted.” CU4

“we see extra customers of IDPC3 as being good, it reduces costs but not necessarily extra shareholders. What we have works well” CU5

Rebalancing appears also to be constantly required as a result of changes in the competitive environment, the resources required and changes both in the capabilities of IT and its contribution to a credit union.

“With the cost of technology I know some institutions, credit unions, that have been using IDPCs and because of the cost of IT they’re bringing it back in-house” CU1

“we actually created our own switching company, which we ended up selling to First Data .. so the reason it was sold to First Data, like everything, the resources and investment that would be required in the worldwide network, which is becoming a significant number” CU4

The complex milieu of outsourcing

With regard to the IDPCs themselves, a variety of options have been taken with regard, for example, to whether the IDPC and the core banking system constitute an inseparable bundle, whether other activities will be provided and even whether the technical operations themselves will be further outsourced out. However what was also made clear from the interviews was that the IDPC is only one component of a complex outsourcing milieu that, even within the domain of transactional services, is both layered and modular (see Figure 2).

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**Figure 2. Simplified map of transaction processing – all elements of which may be outsourced**
REFERENCES