

What Makes Companies Backsource IT Services? Exploring the Influence of Decision Makers' Preferences

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Abstract

This paper presents a research model to explore factors which influence a company's re-evaluation of its initial outsourcing decision. Thus, it aims to extend the research area of information technology (IT) back-sourcing by creating further insights into antecedents for back-sourcing decisions and implications for IT governance. The research is relevant because IT sourcing arrangements are increasingly changing towards selective sourcing and multi-sourcing approaches with more but smaller contracts. Companies will therefore have to re-evaluate their IT strategy and sourcing decisions more frequently. The proposed model examines the effect of service quality, relationship quality, and switching costs. Further, this paper extends existing research and introduces decision makers' sourcing preferences as a not yet examined moderator. This allows to incorporate the influence from beliefs of decision makers on the decision process. The paper further provides a perspective on the subsequent steps to pursue the presented research approach.

Keywords

Backsourcing, outsourcing, information technology, sourcing decisions, decision makers' preferences.

Introduction

The importance of information technology (IT) for companies has grown rapidly over recent years (Newman 2016). Companies from various industries strive for digitizing business models, agile forms of collaboration, and increasing automation (Heltzel 2017). This forces companies to review their IT sourcing strategies and IT governance models and to consider alternatives for currently existing outsourcing arrangements. One potential option could be to backsource IT services currently performed by external vendors (Veltri et al. 2008). The concept of IT back-sourcing was initially established by Hirschheim and Lacity (1998) and Lacity and Willcocks (2000). They defined back-sourcing as the repatriation of all previously outsourced assets, activities, and skills needed to perform IT services back in-house. Further, Nujen et al. (2015) emphasize the change in ownership back to the mother organization as distinctive characteristic. This distinguishes the term back-sourcing from similar terms, e.g., backshoring or reshoring, which rather focus on a change in location of the delivery (Bary and Westner 2018).

Several researchers have discussed motivators which trigger a company to question their IT outsourcing strategy and to initiate a decision whether to backsource, e.g., expectation gaps and organizational changes (Nagpal 2015; Veltri et al. 2008). Furthermore, researchers have analyzed back-sourcing cases to identify reasons why a company actually decided in favor of back-sourcing (Moe et al. 2014; Thakur-Wernz 2019). In contrast, Whitten and Leidner (2006) followed a different approach and empirically tested the effect of several factors on the decision to backsource or switch vendors. Similarly, Gorla and Lau (2010) tested the influence of risk factors during IT outsourcing. However, since those empirical studies were conducted, the field of IT has changed fundamentally, which impacted IT sourcing: over the last years, there has been a strong increase in cloud-based services and a shift towards deploying standardized, almost "industrialized" applications as services (Bommadevara et al. 2018; Heltzel 2017). The rise of cloud computing and standardization of service delivery led towards a decline in large outsourcing contracts and a growth of multi-sourcing from respective "best-in-breed" vendors (Könning et al. 2018). This leads to an increase of "second generation sourcing decisions" (Lacity et al. 2009), namely whether to continue outsourcing or to

backsource a respective service. In addition to the changes in the IT sourcing environment, the author observed during a recent series of qualitative, semi-structured interviews with multiple IT backourcing experts, that personal preferences of decision makers (e.g., the CIO or COO) were frequently stated as a further important factor influencing a backourcing decision (Bary et al. 2018). As this particular reason for backourcing has been less mentioned in previous academic literature, the author would like to further explore its influence on IT backourcing decisions to complement existing research. Consequently, the goal of this paper is to present a research model to a) explore the effect of decision makers' preferences in addition to previously examined factors and b) to furthermore re-visit previous research findings given the changes in the IT environment. The paper thus aims to answer the following research question (RQ):

(RQ): How does a decision maker's personal preference for internal IT influence a backourcing decision?

This RQ is of special interest, as it focuses on the drivers behind one of the central elements of a backourcing transition. When deciding for backourcing, decision makers ultimately accept that the current IT strategy must be changed and major foundations for the future IT delivery and enterprise architecture are defined. To reflect changed sourcing practices, and in contrast to previous contributions, focus is put on backourcing decisions for single, differentiable services, not necessarily on the termination of whole contracts. By adding personal preferences from decision makers as influence factor, this contribution will allow practitioners to gain insights into new factors influencing backourcing decisions. This could, for example, lead to more objective, less biased decisions or improved IT governance concepts.

The remainder of this paper is structured as follows. The subsequent section presents the research model and the included constructs and relationships. Then, hypotheses how these constructs influence a decision to backsource are proposed. The final section concludes and discusses further directions and limitations.

Research Model to Explain IT Backsourcing

The proposed model incorporates factors derived from prior research, namely service quality, relationship quality, and switching costs (Law 2018; Thakur-Wernz 2019; Whitten and Leidner 2006). An additional factor which could influence the decision process, a decision maker's preference for internal IT, was added based on prior own work (Bary et al. 2018) to extend existing research. Figure 1 displays the research model.

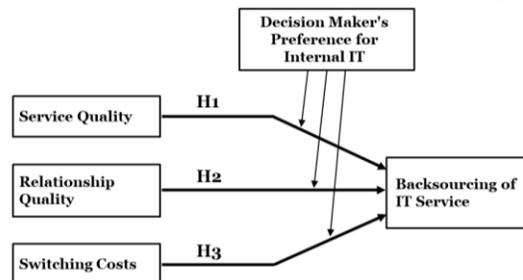


Figure 1. Research Model to Explain IT Backsourcing

To reflect the changes to the IT environment, the model puts a special focus on its applicability for decisions on single IT services instead of entire outsourcing contracts only. Therefore, the unit of analysis is a differentiable IT service (e.g., application development or data center services), since a company could partially backsource specific services out of a larger contract (Veltri et al. 2008). This allows a more granular consideration of the sourcing setup based on each particular service and its suitability for backourcing and is more relevant for future sourcing decisions, since recent studies show a growth in the number of separate outsourcing contracts, accompanied by a decrease in contract volumes and durations (Könning et al. 2018).

Factors from Prior Research Which Influence the Decision to Backsource

Service quality can be defined as the conformance to customer requirements based on the comparison between client expectations and service delivery (Parasuraman et al. 1988). Service quality has two dimensions, technical and functional quality (Grönroos 1984). Technical service quality, for example reliability and technical performance, evaluates the quality of the outcome of the delivered IT services (Parasuraman et al. 1988; Park et al. 2012). In contrast, functional service quality assesses the performance during the service delivery, for example, the vendor's responsiveness (Park et al. 2012).

The importance of service quality in outsourcing can also be seen in the transaction cost (TC) theory. High service quality decreases costs required for monitoring service levels and thus potentially the overall TC (Whitten and Leidner 2006). If the vendor would act opportunistically as predicted by TC theory, service quality would decrease and therefore increase TC (Whitten and Leidner 2006). Further, research has shown that high service quality influences customers' willingness to remain with the current vendor (Zeithaml et al. 1996). Additionally, high service quality has a positive impact on confidence and trust from the client in an IT outsourcing relationship (Eisingerich and Bell 2008). Consequently, it can be argued that companies which are unsatisfied with the delivered service quality rather consider to backsource the services in scope (Chakrabarty et al. 2008; Whitten and Leidner 2006). This leads to the following hypothesis:

H1: Service quality is negatively associated with the decision for back sourcing.

A high **relationship quality** between client and vendor is important to achieve project success (Lacity and Willcocks 2000), and influences the decision to backsource or to continue outsourcing (Whitten and Leidner 2006). Both involved parties should explicitly aim to maintain a well-functioning relationship to increase outsourcing success (Schroiff et al. 2011). The perceived quality of a relationship is influenced by different factors, for example trust, commitment, or communication quality (Jeong et al. 2018).

Trust exists when client and vendor have confidence in the reliability and integrity of each other (Park et al. 2012). Thus, trust decreases uncertainty of an outsourcing relationship and can positively impact its duration (Lee and Kim 1999). Besides trust, commitment also plays an important role on relationship quality. For the context of IT outsourcing, it reflects the highest level of a connection between client and vendor, and can be defined as the desire to maintain a relationship over a long term (Park et al. 2012). Thus, it can be concluded that a company is hesitant to terminate such a deep connection and even accepts certain limitations in the overall service quality (Rajamani et al. 2010). This leads to the following hypothesis:

H2: Relationship quality is negatively associated with the decision for back sourcing.

Switching costs can be defined as relationship-specific investments between client and vendor (Farrell and Shapiro 1988). Companies can be locked into an outsourcing relationship due to high degree of knowledge or asset specificity (Gorla and Lau 2010). During outsourcing, vendor employees will build up personal knowledge unique to a particular IT service (Salge 2015). Since this knowledge is not a commodity but relationship-specific, it cannot simply be redeveloped internally or from a different vendor and thus increases switching costs. Further switching costs can occur when a termination fee has to be paid as contractual penalty for early termination (Thakur-Wernz 2019).

Previous research shows that although customers are dissatisfied, they are willing to stay in the relationship if high switching costs are present (Whitten and Leidner 2006). Similarly, Law (2018) concluded that companies can feel captured into an IT outsourcing relationship, for example due to missing internal capabilities, and therefore do not terminate an outsourcing contract despite dissatisfaction with the services. Only a larger organizational crisis, e.g., resulting from the failure of large outsourced IT projects, led to a decision in favor of back sourcing (Law 2018). This leads to the following hypothesis:

H3: Switching costs are negatively associated with the decision for back sourcing.

Exploring the Influence of Decision Makers' Preferences

This paper considers a **decision maker's preference for internal IT** as the general belief that internal IT is preferable; independent of the respective service or outsourcing contract in scope. This preference could be, for example, based on previous sourcing experiences (Barney et al. 2010), which lead to a potential bias in future decisions (McLaughlin and Peppard 2006). One possibility is that the decision maker has had negative experiences with IT outsourcing (Barney et al. 2010), or previous experiences with an internal IT which had been mainly positive (Bary et al. 2018). Another cause would be if executives had already collected positive IT back sourcing experiences, thus reducing concerns about the transition or outcomes (Bary et al. 2018). Further, external advisors like consultants, peers or journalists could influence a decision maker towards favoring internal IT and thus having a more subjective evaluation of the other introduced factors. While the construct focusses on an individual's preference, this contribution does not aim to ignore that sourcing decisions are often made by multiple stakeholders in a structured process. However, it can be argued that preferences from executives can influence the decision-making process within organizations, and thus bias the organization to favor certain decisions (Hutzschenreuter and Kleindienst 2006).

If a decision maker has a strong belief in internal IT delivery, her/his perception of the other introduced factors could be influenced positively or negatively (Webster and Wind 1972). Therefore, the research model includes a decision maker's preference for internal IT as a construct interacting with the three other factors. It assumes a subjective perception of the other factors which changes their assessment and thus their influence on the decision. The paper therefore proposes a moderator design as the absence of preferences for internal IT was considered to be a condition for the other factors' influence rather than being causal (Kraemer et al. 2008). This inclusion of personal preferences represents a novel aspect and extends previous research focusing on the organizational level, for example by Whitten and Leidner (2006).

Summary and Outlook

This paper suggests a research model to explain IT back sourcing and to explore different influencing factors on a company's re-evaluation of its initial sourcing decision. By drawing upon the three factors service quality, relationship quality, and switching costs, the model relates to previous research. With the newly introduced moderator decision maker's preference for internal IT, this contribution suggests further explanations to extend the academic literature based on own prior research and aims to provide relevant insights into the IT back sourcing decision process. The research model considers the changing IT environment and specifically the impact of new sourcing strategies. Therefore, its unit of analysis is a differentiable IT services in scope of the back sourcing decision instead of an entire IT outsourcing contract.

The subsequent step for the presented emerging research will be the finalization of the operationalization of the constructs, especially the selection, adoption and development of applicable measurement scales based on existing literature and own work. In the following, the author aims to collect primary data to test the proposed hypotheses. The desired approach for the data collection phase is to set up an online survey among IT executives and consultants with insights in sourcing decisions to aggregate their experience on the back sourcing decision process and influence of the introduced factors. Potential limitations could arise from the challenge to receive an adequate number of responses from suitable candidates. Also, it might be difficult to truthfully determine the decision maker's preference for an internal IT delivery. However, in total, the approach is regarded as robust and appropriate to further explore IT back sourcing decisions.

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