Conflicts in IS Outsourcing: Developing a Research Model

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Conflicts in IS Outsourcing: Developing a Research Model

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ABSTRACT
Conflicts among client and vendor in IS outsourcing can negatively affect their relationship and outsourcing project success. However, there is little research done on the antecedents of conflicts and conflict resolution. In this research study, we utilize concepts from marketing, operations management, and management fields to develop a comprehensive research model for studying conflict.

Keywords
Outsourcing, Conflicts, Conflict Resolution.

INTRODUCTION
Conflicts in outsourcing are a result of differences of interests in client and vendors (Lacity and Hirschheim 1995; Vining and Globerman 1999). One of the major risks in IS outsourcing is contractual conflicts, which start creeping in right after the contract is signed. They arise because of: differences in objectives of the client and vendor; incomplete contract, not covering all future contingencies; different interpretations of the contract; change in the business needs and requirements of the client; or technological changes. In case of large contracts, multiple vendors may be involved. Presence of conflict among the vendors also affects the client-vendor relationship (Choi et. al 2002).

If conflicts are not resolved amicably, the hostility and bitterness resulting from them can lead to negative consequences including relationship dissolution (Morgan and Hunt 1994). As outsourcing relationships evolve from arm’s length, transaction-based relationships to strategic relationships, resolving conflicts becomes particularly important.

Organizational literature has studied conflicts in alliances, joint ventures and partnerships, but very few studies have examined conflicts in IS outsourcing. Kern and Silva (1998) investigated the issue of power to map the areas of potential conflicts in outsourcing. Sun et al. (2002) found conflict mediated the impact of trust on partnership satisfaction. While these studies provide important insights about conflicts, there is a need to identify key antecedents of conflicts in IS outsourcing.

In this study, we develop a comprehensive framework for conflicts and conflict resolution through a synthesis and application of well developed concepts and theories. We investigate a two-dimensional representation of conflict, frequency and intensity. The objective is to identify sources of conflict and factors that may lead to conflict resolution in order to develop more co-operative and performance enhancing relationships and increase the likelihood of outsourcing project success.

THEORETICAL FOUNDATION
Relationship Marketing

The concept of relationship marketing emphasizes relationship building in buyer-seller interactions. Here, conflict is treated as a two-sided construct. If conflicts are not resolved, they can lead to relationship termination. If conflicts are resolved, they may increase productivity in relationship marketing (Morgan and Hunt 1994). This holistic view of conflict centers on the presence of commitment and trust in building a successful relationship.

Relational Exchange
This theory suggests that the governance structure of a relationship can be arranged on a continuum of market and hierarchy as the two extremes. IS outsourcing arrangements are becoming long-term, hybrid relationships. Firms participate in relational exchanges in expectation of perceived benefits or in anticipation of outcomes that are greater than those possible from other business alternatives (Mohr and Spekman 1994).

Psychological Contract
Psychological contract theory focuses on people’s mental beliefs and expectations about their mutual obligations in a contractual relation (Rousseau 1995). An outsourcing contract involves bilateral obligations which are beyond mutual expectations and based upon perceived promises of a reciprocal exchange. A failure to meet obligations is likely to lead to erosion of the trust and relationship between the client and vendor, and this will impact vendor’s satisfaction (Koh et al. 2004).

Social Exchange
According to Fischer and Bristor (1994), social exchange theory explicitly predicts that social relationships are formed on the basis of partner’s motivational investment and anticipated social benefits that would not be achievable on their own. When these benefits are not fulfilled for the participants in outsourcing, it can potentially lead to a strain in the relationship and conflict may arise.

Transaction Cost
Transaction cost theory (Williamson 1976) is used to determine appropriate governance structures in buyer-seller transactions. The theory suggests that high level of uncertainty, exchange frequency, and asset specificity can increase termination costs for both the client and vendor. Opportunism and threats of switching by a party can deter other party’s potential gains from making relationship specific investments (such as dedicated staffing and specialized equipment/software).

Expectation Confirmation
Expectation confirmation theory states that customer satisfaction develops from a customer’s comparison of post-purchase evaluation of a product or service with pre-purchase expectations. In outsourcing, vendors expect benefits such as building industry reputation, winning future contracts, and augmenting their competencies (Levina and Ross 2003) while clients expect economic and strategic benefits. When the expectations of benefit (economic or non-economic) for the outsourcing participants are not met, it leads to dissatisfaction.

RESEARCH MODEL
Building upon the theoretical foundation, we propose a conceptual framework (Figure 1). The framework hypothesizes a number of factors likely to impact conflicts and conflict resolution in IS outsourcing. Conflict resolution is the endogenous construct and communication, fulfilment of obligations, termination cost, and confirmation of expected benefits are exogenous constructs. Their relationship is mediated by trust, commitment and number of conflicts in an outsourcing relationship.
Factors and Related Literature

<table>
<thead>
<tr>
<th>Factors</th>
<th>Operational Definition</th>
<th>Related Literature</th>
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<tbody>
<tr>
<td>Communication with the Partner</td>
<td>The formal and informal sharing of information or meaning between client and vendor</td>
<td>(Anderson and Narus 1990; Sun et. al 2002)</td>
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<td>Fulfilment of Obligation by the Partner</td>
<td>A partner’s perception that the other partner will implement its mutual obligations (based upon the partner’s beliefs).</td>
<td>(Rousseau, 1989 79; Koh et.al 2004)</td>
</tr>
<tr>
<td>Trust in the Partner</td>
<td>A partner’s belief that the other partner will perform actions that will result in positive outcomes for the partner as well as not take unexpected actions that result in negative outcomes.</td>
<td>(Anderson and Narus 1990; Morgan and Hunt 1994)</td>
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<tr>
<td>Relationship Commitment</td>
<td>Degree of the pledge of relationship continuity of the partner</td>
<td>(Morgan and Hunt 1994)</td>
</tr>
<tr>
<td>Relationship Termination Cost</td>
<td>A partner’s perception of the costs associated with terminating a current relationship and establishing a relationship with another partner.</td>
<td>(Liu and Leach 2003; Morgan and Hunt 1994)</td>
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<tr>
<td>Confirmation of expected benefits</td>
<td>A partner’s perception of conformity between expectations of benefit from IS outsourcing and actual benefits received.</td>
<td>(Olshavsky and Miller 1972; Mohr and Spekman 1994 Levina and Ross 2003)</td>
</tr>
<tr>
<td>Conflict</td>
<td>The frequency and intensity of disagreement between client and vendor</td>
<td>(Robey et. al 1989; Barki, and Hartwick 2001; Morgan and Hunt 1994)</td>
</tr>
<tr>
<td>Conflict Resolution</td>
<td>The lessening or elimination of the disagreement between IS outsourcing client and vendor</td>
<td>(Robey et. al 1989; Barki and Hartwick 2001)</td>
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Table 1. Factors and Related Literature

According to relationship marketing, communication is one of the important antecedents of a successful relationship (Morgan and Hunt 1994). Past communication, from both supplier-customer perspectives, is positively related to trust (Anderson and Narus 1990). IS outsourcing involves communication between client and vendor in all stages of the project. A direct
manifestation of either partner’s involvement in the outsourcing project is in the communication with the other partner. Thus, we hypothesize,

**H1:** The degree of communication between two partners will positively affect their trust in each other.

A fulfilment of unwritten (psychological contract) and written (contract document) obligations by client and vendor will result in an expansion of their relational trust leading to positive beliefs. The unwritten obligations especially in outsourcing involving multimillion dollar deals assume greater importance, since the legal contract is usually so long and complex that it is impractical to disseminate it to all involved individuals (Koh et. al 2004). Even though Rousseau (1989) argued that concept of unwritten obligations does not apply to organizations, Koh et. al (2004) demonstrated that psychological contracts played an important role in the development of the outsourcing relationships. Hence,

**H2:** The mutual fulfilment of the obligations by the partners will positively affect their trust in each other.

Trust is one of the most desired qualities in any close relationship (Anderson and Narus 1990; Sabherwal 1999). Trust exists when one party has confidence in an exchange partner’s reliability and integrity (Morgan and Hunt 1994). Outsourcing relationships based on a formal contract and rooted in mutual trust give rise to stronger bonds between clients and their service providers (Sabherwal 1999). Several empirical studies have already shown that trust in a partner has a positive impact on relationship commitment. Hence,

**H3:** The degree of trust between two partners will positively affect commitment in each other.

In outsourcing relationship, both partners develop interdependency through their mutual complimentarity (Levina and Ross, 2003). The degree of interdependency depends on the level of economic and relationship investments made by the partners in the relationship. The partners risk losing these investments, when the relationship terminates. However, if such investments are low, the termination cost is low and a partner will feel less committed to the relationship. Hence,

**H4:** The termination cost for each partner will positively affect their commitment to each other.

Firms enter into relationship with a goal of deriving mutual benefits (Mohr and Spekman 1994). These expectations would enforce partner’s commitment to outsourcing success. A continuation of the relationship over the long term would encourage increased cooperation among the partners. When partners achieve expected benefits, it vindicates their motive of entering into outsourcing relationship and increases relationship commitment. We extend expectation-confirmation theory to hypothesize that when expectations of benefit are not met, it decreases the commitment among the partners. Hence,

**H5:** The confirmation of expected benefits for each partner will positively affect their trust in each other.

Kemp and Ghauri (1999) suggest that trust and norms, which are results of long-term relationship development, reduce the potential for conflict. Prior literature has shown that trust lead to higher levels of inter-organizational cooperative behaviours such as shared planning and flexibility. Trust developed through past experience in working with the same partner influences stability in future projects. Hence,

**H6:** The degree of trust between two partners will negatively affect the conflict between them.

Social exchange theory argues that an exchange partner is likely to remain in the relationship if its perceived reward is less than the cost. Firms understand that the costs of retaining current partners are far less than the costs associated with terminating existing relationships and finding new partners, therefore mechanisms for resolving conflicts are critical to building and maintaining relationships. Committed partners balance short-term problems with long term goal achievement (Mohr and Spekman 1994). In outsourcing relationships, both contractual commitment and relationship commitment are recognized as crucial preconditions for the outsourcing partners to be proactive beyond what the contract suggests (Kern and Willcocks 2002). Therefore,
**H7:** The degree of commitment between two partners will positively affect the conflict resolution.

Conflict resolution is the extent to which the client and vendor are able to replace objections by agreement and consensus between them. In conflict resolution, we distinguish between two facets of conflict: intensity and frequency (Robey et. al 1989). A “frequency” interpretation of conflict suggests that the more numerous the conflicts that client and vendors are engaged in, the less likely it is that they will resolve each and every one of them to their satisfaction, possibly due to insufficient time or energy. An “intensity” interpretation suggests that the greater the intensity of a conflict that vendor and client are engaged in, the less likely it is that they will resolve it to their satisfaction, possibly due to the greater importance of the issue or greater differences between them (Robey et. al 1989; Barki, and Hartwick 2001). Hence our hypothesis,

**H8:** The number of conflicts between two partners will negatively affect conflict resolution.

**THE RESEARCH PLAN**

The aim of this research is to build a model and test its veracity through an empirical evaluation. The unit of analysis would be an outsourcing project. We aim to utilize qualitative and quantitative techniques to develop the survey. The participants are expected to be senior management, IT/business unit managers, and project/contract managers who are responsible for managing the outsourcing arrangement. The participants will be initially interviewed to determine the broad factors which contribute to conflict. Survey measures would be developed on the basis of the interview results. The questionnaire would measure project details such as cost, number of vendors involved, length of relationship, financial and strategic importance etc.

**REFERENCES**