IT managers commiserate over the challenges of convincing senior executives that, contrary to popular belief, outsourcing isn’t always a money-saving option.

Information technology outsourcing—the practice of transferring IT assets, leases, staff, and management responsibility for delivery of services from internal IT functions to third-party vendors—has become an undeniable trend ever since Kodak’s 1989 landmark decision. In recent years, private and public sector organizations worldwide have outsourced significant portions of their IT functions, among them British Aerospace, British Petroleum, Canadian Post Office, Chase Manhattan Bank, Continental Airlines, Continental Bank, Enron, First City, General Dynamics, Inland Revenue, JP Morgan, Kodak, Lufthansa, McDonnell Douglas, South Australian Government, Swiss Bank, Xerox, and Commonwealth Bank of Australia. The IT outsourcing market, which was worth $76 billion in 1995, grew to over $120 billion in 1997 [5].

As the market evolves, a number of important aspects of these IT outsourcing decisions have been explored. These studies can be categorized as descriptive case studies and surveys of the current outsourcing practices, surveys of practitioners’ perceptions of risks
and benefits of outsourcing, studies of determinants of outsourcing, and identification of best practices that distinguish success from failure [1–4, 6, 9, 11]. In general, the current research indicates selective sourcing is still the norm but that outsourcing options are becoming more complex. There are many perceived benefits and risks of outsourcing, but these studies are based on respondents’ perceptions rather than actual outcomes. The determinants of outsourcing research generally show that companies most likely to outsource on a large scale are in poor financial situations, have poor IT functions, or have IT functions with little status within their organizations [7, 8]. There is still considerable debate on best practices that distinguish successes from failures.

The current IT sourcing research covers the motivations and consequences of outsourcing and has neglected another important option—insourcing. Insourcing is the practice of evaluating the outsourcing option, but confirming the continued use of internal IT resources to achieve the same objectives of outsourcing. We believe that insourcing must be fully explored to complement the growing body of outsourcing research. Only by understanding the processes and outcomes of both outsourcing and insourcing can a comprehensive understanding of IT sourcing result. This unexplored insourcing option provided the motivation behind our research. Can internal IT departments achieve the same results as outsourcing vendors? If so, why have they not done so in the past? Do IT departments actually reduce costs or improve service after winning an insourcing bid? If so, how did IT departments achieve the results? We conducted 14 insourcing case studies to research these issues. The experiences of case study participants are examined and analyzed. The resulting picture is a rich and varied one involving a number of key decision makers, alternative reasons for choosing insourcing, contrasting outcomes, and varying perceptions of its success or failure. But we also identified a number of common experiences. These similarities and differences across the cases are the focus of this article.

This research contributes to the IT sourcing research base by providing evidence that companies need not necessarily turn to outsourcing to improve IT performance. While outsourcing may be a preferred option for some organizations for various reasons, such as returning to core competencies or focusing IT staff on more business-oriented IT activities, our cases show that if cost reduction is the major objective, IT managers can oftentimes replicate a vendor’s cost reduction tactics. Insourcing success, however, is predicated on a number of key issues, including aligning the perceptions of and agendas for IT, senior level sponsorship of the decision, and a fair and rigorous evaluation process.

In order to develop an in-depth understanding of IT insourcing decisions and outcomes, we adopted a multiple case study approach. Our aim was to interview various stakeholders within organizations who were likely to have different views of the insourcing decision, who could provide longitudinal accounts of the decision-making process, who could explain how decisions were embedded, as well as the outcomes of the decision (see sidebar for methodology).

Four Archetypes of Insourcing
The issues associated with the choice of an IT sourcing strategy are often murky, hidden behind euphemisms, perceived differently by different stakeholder groups, and generally not easily analyzed. Nevertheless, in trying to explain what we found in our research about these issues we noted certain similarities and differences in patterns and these coalesced around four loosely connected alternatives in the way organizations approach IT insourcing. We describe these four alternative approaches in terms of archetypes, discussing each one through an individual case study. It should be noted that these approaches are neither as clear cut nor as animated as they seem. There is overlap and their differences are overstated for the purpose of effect. They are highly simplified but powerful conceptions of an ideal or character type. The archetypes play an important role in conveying the essential differences that exist in alternative ways organizations approach IT insourcing.

Archetype 1. Senior executives enable internal IT managers to cut costs.
Six of our cases—PETRO2, UNIVERSITY, FOOD, TCOM, ENERGY, and RETAIL1—reflect this archetype. It begins when external pressures threaten the organization causing senior management to search for ways to reduce costs, including IT costs. Under this scrutiny, senior executives question the value of rising IT expenditures and mandate that IT managers cut costs. IT managers counter that costs are high because users resist their cost reduction tactics. Senior management despairs at the gridlock and formally invites outsourcing vendors to submit bids. IT managers rally, requesting they be allowed to compete with vendor bids. They argue that senior management’s outsourcing threat serves to empower IT managers because they can convince users that costs will be cut—either by them or by an external vendor. By replicating a vendor’s cost reduction tactics, internal IT managers prepared internal bids that beat vendor
bids. Once these bids were awarded to the internal IT managers, they succeeded in meeting—or in some case exceeding—their bid proposals, resulting in a successful financial outcome. A description of one of the cases—PETRO2—serves to demonstrate this theoretical archetype.

PETRO2 is a Fortune 100 conglomerate of petroleum, natural gas, and chemical companies that ran into severe financial difficulties in the late 1980s. Senior management responded by cutting costs through the sale of assets, reduced headcount, and budget cuts. In this climate, senior management began to scrutinize the rising costs of IT—where was the value from these IT expenditures? The corporate manager of IT planning explains: "All they (senior management) see is this amount of money that they have to write a check for every year—year after year after year. Where is the benefit? MIS says, 'Well, we process data faster than we did last year.' They say, 'So what?' MIS says, 'Well, we can close the ledger faster.' And they say, 'So what? Where have you increased revenue? All you do is increase costs, year after year after year and I am sick of it.' All I get are these esoteric benefits and a bunch of baloney on how much technology has advanced. Show me where you put one more dollar on the income statement.'"

Internal IT managers tried repeatedly to reduce costs by consolidating their three data centers, but business unit managers refused, figuring the new consolidated center would not effectively cater to their needs. For example, one of the business unit leaders declared: "If it cost $5 million more to have this in my business unit and be able to control it and make it responsive to my needs, it's worth $5 million to me."

Only after senior management initiated an outsourcing evaluation did IT managers convince senior managers and users that they could match a vendor's offer: "The IT management said there is no reason we should be excluded from the party. You cannot assume, that we'll just do what we've been doing. We ought to have the same freedom to make decisions that outsourcers are making. So IT management in each of the divisions caucused. We put together a team."—Corporate technology manager.

The team prepared an internal bid based on severe cost reductions, including data center consolidation. This bid beat two external bids. The internal IT department was awarded the bid and subsequently consolidated the data centers, installed automation in the tape libraries, reorganized the work flows, standardized software, and instituted a new chargeback system that curtailed excessive user demands. These tactics reduced headcount by 51% resulting in a 43% cost reduction, thus deeming the insourcing project a financial success. The corporate manager of technology attributes the success to senior management's empowerment of the IT staff.

Archetype 2. IT managers terminate failing outsourcing contracts.

Our second archetype—exemplified by CHEM2 and RUBBER—also results in a financial insourcing success, but the route to success is very different. In these two companies, senior managers had previously outsourced over 80% of the IT budget and engaged in long-term contracts.

Due to poorly negotiated contracts, however, IT costs rose and service levels dropped. The senior IT managers assembled a case to terminate the outsourcing contract and rebuilt the internal IT organization. Senior executives and users supported the IT managers' proposals. After an initial investment, IT costs dropped and service levels improved as a result of insourcing.

At CHEM2, senior executives decided to outsource the entire IT department in 1984 after a leveraged buyout left the company debt-ridden. After analyzing three vendor bids, senior executives signed a seven-year, fixed-price contract with the only vendor they perceived as capable of handling their information needs. The contract stipulated the vendor would provide the same level of service that CHEM2 received from the internal IT department in 1984. The first month into the contract, the vendor charged CHEM2 for many services senior executives assumed were covered in the contract. Excess charges were not the only problem. The IT manager noted the vendor's goal was to maximize profits, therefore, the vendor failed to introduce new technology (without a stiff excess fee), the vendor reduced staff and over-worked remaining employees, and the vendor siphoned the best talent to woo other customers.

"One of the questions I asked was, 'How do you view IT, Mr. President, particularly in the operational center, as an asset to your corporation? Of potential value? For the most part, business people don't see it that way. They see it as cost.'"—The IT Manager at TCOM describing the President's view of IT.
"I think you find with outsourcing that any innovation in technology comes from your own people, requirements from users on your staff. But basically the [outsourcing vendors] just crank it. And so we were operating old software...You pay for them to learn your business, then they move those people to court other companies in your industry. They transfer skills to get new business, now the learning curve is yours to pay for again," said one IT manager.

The IT manager accumulated the evidence of rising IT costs and decreased service levels to convince senior management and users to terminate the contract. Senior management bought into the proposal, even though the vendor tried to keep the contract. Recalls the IT manager: "I opened up negotiations early, to renegotiate the contract to get me out...It's like when you were a little kid. Two weeks before Christmas, you suddenly cleaned up your act and behaved a whole lot better...But I think they [senior management] had an awful lot of feedback from the users that they didn't like the systems. Also the issues of quality came up, customer service, no new technology."

The IT manager put together a plan to rebuild the internal IT department, which included purchasing a new machine, buying packaged software, and hiring back 40 analyst programmers from the outsourcing vendor. After an initial investment, the IT manager conveyed that users are happier with the service and that his current IT budget is less than the fixed price contract, indicating a successful financial outcome.

Archetype 3. IT managers defend insourcing.

This archetype is the first time in which insourcing results in a financial failure in that no cost savings (or service improvements) occur. In these cases, exemplified by CHEM3, DIVERSE1, PETRO3, and DIVERSE2, IT managers took charge of the outsourcing evaluation for a number of political reasons, such as proving efficiency, justifying new resources, or trying to enhance their reputation as a business person. They used the outsourcing evaluations to confirm to senior management the legitimacy of continued sourcing through the internal IT departments. In three cases, these cursory evaluations eventually backfired, senior managers firing IT managers or eventually outsourcing.

The Director of Information Services at PETRO3 initiated an outsourcing investigation after users complained consistently to senior management about the lack of service in the applications area. The IS director explained that user demands far exceeded his current resources, leading to a large applications backlog.

His investigation consisted of inviting several vendor bids—not for applications, but for the data center, a function he knew was performing well. After the bids were analyzed, the IS director drafted a letter to the chairman of the board explaining that continued insourcing cost less than outsourcing. The IS director explains the outcome: "I had their attention now. And so some of the people who were bashing us backed off. Their group executives now tell their users, 'Back off, they are doing the best that they can.' So did it help? Since then, I've been to two officer meetings, so I guess it did."

Although a political victory, there was no change in IT costs: "As a result of having done this study, there is no difference now than if we had not done the study...It really came down to an exercise. We did not try to make outsourcing work. What we were really trying to do was to come up with the justification for why we shouldn't outsource."—Technical support manager.

Archetype 4. Senior executives confirm the value of IT.

This archetype indicates the case where the insourcing decisions did not result in significant reduction in IT costs, but the insourcing decisions were still considered a success because companies revaluated and further legitimized internal sourcing. Senior IT executives at PETRO1 and INTL-BANK—two companies that exemplify this approach—had full support from senior management. Each has implemented organizational structures and processes to demonstrate the cost effectiveness of its IT departments.

In the mid 1980s, PETRO1, one of the world's largest petroleum companies, suffered severe financial difficulties that forced senior management to find ways to cut costs. An outsourcing vendor, cognizant of the situation, called the CEO and offered to purchase his IT assets, hire his IT staff, and reduce his current IT costs while still maintaining service levels. The CEO called his direct subordinate, the VP of IT, and told him to draft a letter to the vendor, declining the offer. The VP of IT conveys this conversation with the CEO: "'[The CEO] said, 'I'm not interested in letting other people have access to our data. I don't have to go..."
outside for use of our data, so prepare a letter back to the chairman of [the outsourcing vendor] and say we appreciate your offer but at this time we consider our information technology as part of the strategic work that we have."

When the VP of IT was asked how the CEO could readily dismiss the vendor's offer without further analysis, he explained how he had spent 30 years educating and demonstrating to senior managers the value of IT. For example, he convinced the CEO to invite all new general managers to attend a week-long executive computer class which focused on IT-enabled business achievement. He abandoned the general allocation chargeback system in favor of unit pricing and compared these prices with vendor offerings to demonstrate his cost-efficiency.

His IT department even became an outsourcing vendor by providing IT services to external customers. Although external customers represent only 10% of the IT budget, the VP explains that this creates a marketing mentality among his staff to be both cost-efficient and service-oriented. The VP also participated in two top executive committees that set corporate strategy and allocate large amounts of resources. His high profile contributed to the quick dismissal of the vendor's outsourcing proposal: "So I think the concept of your IT person being part of the management of the company—not just a technician sitting on the sidelines—is something that keeps us from outsourcing."

Table 1 offers a summary of the 4 archetypes and classifies the 14 cases.

### Discussion

Prior to our data collection, our conception of insourcing success and failure was equivalent to financial outcomes of the process, that is, insourcing successes were companies that achieved dramatic cost savings of at least 20%, while insourcing failures were companies that achieved little or no cost savings. In our research design, we selected successes and failures to ascertain: After outsourcing evaluations reconfirmed insourcing as the preferred sourcing strategy—why did some companies achieve dramatic savings (and thus success) while others merely continued as-is?

Based on our analysis—which led to the four archetypes—we reconceptualized our notions of success and failure along stakeholder lines. In the majority of cases, our original conception of cost-savings as the primary criterion for success only captured the perceptions of senior executives, whom we concluded perceived IT as a cost to be minimized. In cases of extreme cost-cutting—up to 54% in one company—senior executives deemed the insourcing decision as a success, but users perceive it as a failure. Unlike senior executives who focus on cost, users primary criterion for success is service excellence. Because service degradation accompanies severe costs due to the cost/service trade-off, users were most displeased with the insourcing outcomes in the majority of cases. And IT managers' perceptions of insourcing success and failure are even more complex—many IT managers hoped the insourcing projects would raise the status of IT in the eyes of senior management, but remain disappointed on this front.

Thus, we assume a stakeholder interpretation of success and failure. We have categorized these stakeholders into three main groups: senior management, business unit managers and users, and IT managers. Each stakeholder group sets a different expectation for IT performance, and as such, holds different perceptions of IT performance and the effects of insourcing.

**Senior management's expectations of IT performance: Minimize costs.** In all but two of the participating companies—PETRO1 and INTL-BANK—senior executives focused on one dimension of IT performance: cost efficiency. These senior executives were frustrated with the rising costs of IT and questioned the value of IT expenditures. Because of the questionable value of IT, many senior executives viewed IT as a commodity—a necessary cost of doing business. As such, the
We interviewed 41 participants at 14 companies (see accompanying table). The choice of the case studies was based on the desire to have a variety of sourcing experiences in terms of degree of financial success claimed, primarily assessed a priori through the trade press and personal contacts. We sought to generate insights into best sourcing practices by comparing successes and failures. The organizations also represented a wide spectrum of industries. In order to facilitate the discussion, the 14 companies are referred to by pseudonyms based on their industry type—CHEM1, CHEM2, FOOD1, and so on.

At each case site, we conducted face-to-face interviews with individuals directly involved in sourcing decisions. Interviewees included senior business executives and IT managers who sponsored the sourcing evaluations, consultants hired to assist contract negotiations, and IT personnel responsible for gathering technical and financial information pertaining to the sourcing decision. All interviews were conducted in person at the company site. All participants were assured anonymity so as to promote open discussions.

Interviews followed the same protocol, proceeding from an unstructured to a structured format. During the unstructured portion, participants were asked to tell their sourcing story, which allowed them to convey their interpretations freely. We then asked semistructured questions designed to solicit information on specific sourcing issues that may have been absent from their previous recollections. These issues included coverage of the scope of the sourcing decision, sponsors of the decision, the sourcing evaluation process, and implementation process. All participants were also asked to assess the decision outcome in terms of their perceptions of “success” or “failure” and why they felt the way they did about the outcome. When participants expressed a viewpoint, they were prompted to provide specific supporting evidence. The evidence consisted of anecdotes as well as documentation such as benchmarking reports, IT budgets, internal bids, outsourcing bids, and bid analysis criteria. In cases where opinions of participants at the same organization differed, we conducted follow-up telephone calls to clarify their positions.

Participants were also asked specific questions about their company and IT department. Pertaining to their company, participants described the organizational structure, the major products and services produced, competition in the industry, financial situation, corporate goals, business successes and failures. Pertaining to IT, participants described IT activity in terms of headcount, budget, chargeback system, size of data centers, user satisfaction, challenges, goals, and reputation.

Data Analysis
The transcribed interviews were analyzed using a data analysis process involving the following steps:

1. Create individual case descriptions. Detailed cases were written up based on each interview. Each case included the historical details in which insourcing was considered; the key participants in the decision process; their pre-understanding of the sourcing options and apparent values and assumptions; how these values and beliefs were manifest in the actual decision to insource; the implementation of the decision; and the consequences (results) of insourcing.

2. Analyze six decision factors across the cases. Once we had a feel for each individual case, we then scanned across the 14 cases to see what similarities and differences existed. We analyzed six factors across the cases—decision scope, decision sponsor, evaluation process, year of the decision, size of the organization, and decision outcome. These factors were derived from our previous research on outsourcing [7].

3. Employ a rhetorical device to generalize common themes among the cases. The use of archetypes is employed to condense and simplify a complex subject matter. We are not using archetypes necessarily as an analytical tool, rather as a rhetorical device to convey the themes extracted from our analysis of the textual data collected in the case studies.

4. Identify common lessons across the cases. While these archetypes capture the differences among insourcing approaches, we also sought to characterize common elements, or lessons to be learned from the body of research. These common lessons describe stakeholder attitudes, perceptions, and behaviors based on implicit assumptions about IT sourcing.
<table>
<thead>
<tr>
<th>COMPANY PSEUDONYM AND INDUSTRY</th>
<th>PARTICIPANTS</th>
<th>SOURCING DECISION(S) SCOPE</th>
<th>DECISION SPONSOR</th>
<th>DECISION YEAR</th>
<th>EVALUATION PROCESS</th>
<th>SIZE OF COMPANY/ANNUAL REVENUES/ANNUAL IT BUDGET AT TIME OF DECISION</th>
<th>SIZE: IT HEAD COUNT</th>
<th>EXPECTED COST SAVINGS</th>
<th>COST SAVINGS ACHIEVED</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. CHEM1 Chemicals</td>
<td>1. Manager of IS</td>
<td>Entire IT function outsourced</td>
<td>IT Manager</td>
<td>1991</td>
<td>3 external bids</td>
<td>$5 billion/$17 million</td>
<td>60</td>
<td>No cost savings estimated</td>
<td>No cost savings achieved</td>
</tr>
<tr>
<td>2. DIVERSE1 Diversified</td>
<td>4. Director of Advanced Technology</td>
<td>(a) Entire IT function outsourced, (b) Apps development outsourced</td>
<td>(a) IT Manager, (b) Senior Manager</td>
<td>1991</td>
<td>(a) no formal bid process</td>
<td>(a) $3 billion/$30 million</td>
<td>184</td>
<td>(a) No cost savings estimated</td>
<td>(a) No cost savings achieved</td>
</tr>
<tr>
<td>Product Management</td>
<td>5. VP of IS</td>
<td>Senior Manager</td>
<td>1998</td>
<td>no formal bid process, approached by vendor</td>
<td>$35 billion/$240 million</td>
<td>1800</td>
<td>No cost savings estimated</td>
<td>No cost savings achieved</td>
<td></td>
</tr>
<tr>
<td>3. PETRO1 Petroleum</td>
<td>9. Corporate Mgr. Planning</td>
<td>Entire IT function outsourced</td>
<td>Senior Manager</td>
<td>1991</td>
<td>Internal bid and 2 external bids</td>
<td>$10 billion/$32 million</td>
<td>134</td>
<td>43%</td>
<td>Yes, achieved within 5 years</td>
</tr>
<tr>
<td>Refining</td>
<td>10. Division Manager</td>
<td></td>
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<tr>
<td>4. PETRO2 Petroleum</td>
<td>14. Assistant Treasurer</td>
<td>Entire IT function outsourced</td>
<td>IT Manager</td>
<td>1990</td>
<td>2 external bids</td>
<td>$3 billion/$6 million</td>
<td>25</td>
<td>No cost savings estimated</td>
<td>No cost savings achieved</td>
</tr>
<tr>
<td>Refining</td>
<td>15. Director of IS</td>
<td></td>
<td></td>
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<td></td>
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<td></td>
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</tr>
<tr>
<td>5. PETRO3 Petroleum</td>
<td>17. Manager of IS</td>
<td>(a) Entire IT function outsourced, (b) Entire IT function outsourced</td>
<td>(a) IT Manager, (b) Senior Manager</td>
<td>1988</td>
<td>(a) no formal bid process (b) informal external bid</td>
<td>$6 billion/$100 million</td>
<td>530</td>
<td>(a) 0% (b) 20%</td>
<td>No cost savings achieved</td>
</tr>
<tr>
<td>Refining</td>
<td>18. VP Operations</td>
<td></td>
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<tr>
<td>6. DIVERSE2 Natural gas,</td>
<td>20. VP of Computer Utility</td>
<td>(a) Entire IT function outsourced</td>
<td>(a) IT Manager</td>
<td>1984</td>
<td>(a) 1 external bid (b) no formal bid process</td>
<td>$7 billion/$4 million</td>
<td>40</td>
<td>(a &amp; b) Savings anticipated but not quantified</td>
<td>(a) No, terminating contract due to excess fees &amp; poor service (b) Savings achieved</td>
</tr>
<tr>
<td>and other services</td>
<td>21. Outsourcing Consultant</td>
<td></td>
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<td></td>
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<tr>
<td>7. CHEM2 Chemicals</td>
<td>22. Manager of DP</td>
<td>(a) Entire IT function outsourced, (b) Entire IT function outsourced</td>
<td>(a) Senior Manager, (b) IT Manager</td>
<td>1988</td>
<td>(a) No formal bid process, (b) no formal bid process</td>
<td>$6 billion/$240 million</td>
<td>1,000</td>
<td>(a &amp; b) Savings rose to 4% of sales (b) Yes, costs fell to 1% of sales</td>
<td></td>
</tr>
<tr>
<td>8. RUBBER Rubber and Plastics</td>
<td>23. VP of IS</td>
<td>(a) Entire IT function outsourced, (b) Entire IT function outsourced</td>
<td>(a) Senior Manager, (b) IT Manager</td>
<td>1987</td>
<td>(a) No formal bid process, (b) no formal bid process</td>
<td>$6 billion/$240 million</td>
<td>1,000</td>
<td>(a &amp; b) Savings rose to 4% of sales (b) Yes, costs fell to 1% of sales</td>
<td></td>
</tr>
<tr>
<td>9. RETAIL1 Apparel</td>
<td>24. VP of IS</td>
<td>Entire IT function outsourced</td>
<td>IT Manager</td>
<td>1988</td>
<td>No formal bid process</td>
<td>$2 billion/$27 million</td>
<td>125</td>
<td>54%</td>
<td>Yes, achieved within 4 years</td>
</tr>
<tr>
<td>Manufacturer &amp; Retailer</td>
<td>25. Director of IS Administration</td>
<td></td>
<td></td>
<td></td>
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<td></td>
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<td></td>
</tr>
<tr>
<td>10. UNIVERSITY</td>
<td>26. CIO</td>
<td>Entire IT function outsourced</td>
<td>Senior Manager</td>
<td>1992</td>
<td>Compare 1 external bid with 1 internal bid</td>
<td>$250 million/$7 million IT</td>
<td>110</td>
<td>20%</td>
<td>Yes, achieved within 1 year</td>
</tr>
<tr>
<td>11. FOOD Food Manufacturer</td>
<td>28. Data Center Director</td>
<td>Entire IT function outsourced</td>
<td>Senior Manager</td>
<td>1988</td>
<td>Compare 1 external bid with internal bid</td>
<td>$7 billion/$18 million</td>
<td>80</td>
<td>45%</td>
<td>Yes, achieved within 3 years</td>
</tr>
<tr>
<td>12. TCOM Telecommunications</td>
<td>39. Manager of IS</td>
<td>Entire IT function outsourced</td>
<td>Senior Manager</td>
<td>1991</td>
<td>Compare 2 external bids with internal bid</td>
<td>$5 billion/$7 million</td>
<td>39</td>
<td>46%</td>
<td>Yes, achieved within 2 years</td>
</tr>
<tr>
<td>13. ENERGY Energy Company</td>
<td>36. Director of IS Planning</td>
<td>Entire IT function outsourced</td>
<td>Senior Manager</td>
<td>1989</td>
<td>Compare 3 external bids with internal bid</td>
<td>$6 billion/$60 million</td>
<td>180</td>
<td>25%</td>
<td>Yes, achieved within 2 years</td>
</tr>
<tr>
<td>14. INTL-BANK International Bank</td>
<td>38. Executive VP</td>
<td>Entire IT function outsourced</td>
<td>Senior Manager</td>
<td>1989</td>
<td>Never really considered outsourcing</td>
<td>DMS57 billion in assets</td>
<td>1800</td>
<td>20% cost savings through adoption of best practices</td>
<td>Yes</td>
</tr>
</tbody>
</table>
performance expectations of these senior executives focused on cost minimization, that is, provide the commodity function as inexpensively as possible.

We conclude that senior management in all but two of the participating companies—PETRO2 and INTL-BANK—viewed IT as a cost to be minimized. Furthermore, these senior executives perceived their current sourcing strategies had failed to meet this major objective, as evidenced by the rising costs of IT. In the six companies illustrating Archetype 1, senior managers were pleased that the outsourcing evaluation served to mobilize internal IT managers to cut costs. In Archetype 2, senior management cancelled outsourcing contracts and brought the function back inside when costs for IT increased through outsourcing. In Archetype 3, IT costs did not decrease and led to senior management questioning the value of IT.

We believe that senior management’s perceptions of IT as a cost to be minimized are tied, in large part, by accounting for IT as an overhead, which only serves to highlight the costs, and not the value of IT investments. For example, one VP of IT noted his CEO kept asking him why IT budgets were rising when budgets in all the other functional units were falling. The VP of IT responded that marketing costs dropped 10% partly because IT implemented a new credit card system and that transportation costs dropped because IT automated 16 truck-refueling systems. Prior to the outsourcing evaluations, all but two participating companies—PETRO1 and INTL-BANK—accounted for IT in this way, thus contributing to our understanding of why these senior executives sent the mandate to IT managers to cut IT costs.

**Users’ view of IT: Service excellence.** Unlike senior management, users did not view IT as a commodity. Indeed, IT is not a lack of cement, but it must be custom-tailored to meet their idiosyncratic business requirements. As such, users set service excellence as their major expectation for IT performance. For example, users generally demanded customized software, a local staff of dedicated analysts and programmers, excess IT resources in case they are needed, subsecond response time all the time, 24-hour help, information centers, training, and so on. At PETRO2, for example, users demanded their own local data centers and did not want to consolidate to save money at the corporate level.

At FOOD, users in each business unit demanded custom-tailored software—even when standard packages were more cost efficient. For example, different business units chose different packages for word processing, email, fourth-generation languages, and spreadsheets. From the business unit perspective, it made more business sense to use packages users were familiar with rather than incur the inconvenience and expense of learning a standard package. In summary, participants consistently reported users set service excellence as the primary expectation for IT performance.

**IT manager’s view: Caught in the middle.** Juxtaposed to senior management’s cost reduction mandates were users pleas for service excellence. This leads to a cost/service dilemma, which can be depicted as a matrix highlighting realistic versus unrealistic IT performance expectations. Because of the cost/service trade-off, IT can be realistically expected to perform in one of two boxes at a given point in time: IT can provide a premium service for a premium cost or IT can provide a minimal service for a minimal price. If organizations perceive that a given IT function is a critical contributor, then we can realistically expect its performance to be in the differentiator quadrant. As a differentiator, service excellence supersedes cost efficiency. If organizations perceive that a given IT function is merely a utility, IT can be realistically expected to perform in the commodity or low-cost

"They are always telling us our processing for payroll is too damn expensive. Then when you say, 'Will have you looked outside?' 'Oh yes, we beat the heck out of them.' So our costs are too high but they can't get it any cheaper."  — **Director of IT Administration at RETAIL1**

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producer quadrant. As a commodity, IT can be expected to deliver a standard service at a minimal cost.

But in our case companies, senior executives were demanding cost cuts while users were demanding service excellence. IT managers were expected to perform the near impossible: provide a Rolls Royce service at a Chevrolet price in order to be superstars. IT managers could not simultaneously satisfy both stakeholder groups because the best practices associated with one objective are in direct conflict with the best practices prescribed for the other objective. In general, the differentiator quadrant calls for decentralization, customization, and encouraged user demand. The commodity quadrant calls for centralization, standardization, and curtailed user demand. The result: neither stakeholder group was satisfied and began to perceive that IT provided poor service that cost too much. IT was a Black Hole (see Table 2).

Implications for Practice

We contend that outsourcing evaluations often result from the frustrations caused by different stakeholder expectations and perceptions of IT performance. This belief is based on an analysis of what IT managers can realistically achieve versus what senior executives and users expect them to achieve. Different stakeholder perspectives set unrealistic performance expectations for IT managers, leading to frustration, loss of faith in internal IT management, and hopes that outsourcing vendors will provide the solutions. While outsourcing can lead to a reduction in IT costs, this reduction often comes at a price: reduced service. Moreover, since it is known that most of the cost savings come from the implementation of key cost reduction strategies such as data center consolidation, unit-cost chargeback systems, and standardized software, rather than economies of scale, internal IT departments should be able to reduce costs on their own. And indeed they did.

However, while IT managers can theoretically implement cost-reduction strategies, internal politics often prevent them from doing so. This is why senior executives need to allow IT managers the ability to submit internal bids in competition with external vendors. The outsourcing threat may overcome political obstacles and allow IT managers the freedom and power to propose and implement drastic cost cuts. If senior executives merely compare external bids with current costs, they may allow the vendors to "pick the low-lying fruit." That is, vendors may make drastic cost cuts but absorb most of the savings themselves, merely passing some benefit to customers in the form of modest price cuts. Users, on the other hand, who have been used to service excellence from IT must now realize that such premium service comes at a price—it is not a free good. Implementing outsourcing or insourcing helps focus users' attention on the cost/service trade-off. IT managers, for their part, need to make visible the cost/service trade-off and work for a consensus on what level of service IT should provide for a given cost.

In conclusion, we wish to offer this sobering thought: even if insourcing is chosen over outsourcing, and the expected cost savings are realized, there is no guarantee it will be perceived as successful due to the very different expectations held by the various stakeholders. Success is related to who is doing the evaluating.

REFERENCES


RUDY HIRSCHHEIM is the Tenneco/Chase International Professor of Information Systems and past Director of the Information Systems Research Center in the College of Business Administration, University of Houston.

MARY LACITY is an associate professor of management information systems at the University of Missouri, St. Louis. She is also a research associate at Templeton College, Oxford, U.K.

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