Association for Information Systems
AIS Electronic Library (AISeL)

ECIS 2006 Proceedings

European Conference on Information Systems (ECIS)

2006

It backsourcing: from 'make or buy' to 'bringing it back in-house'

Des McLaughlin
des.mclaughlin@dcu.ie

Joe Peppard
Cranfield University, j.peppard@cranfield.ac.uk

Follow this and additional works at: http://aisel.aisnet.org/ecis2006

IT BACKSOURCING: FROM 'MAKE OR BUY' TO 'BRINGING IT BACK IN-HOUSE'

McLaughlin, Des, Dublin City University Business School, Dublin 9, Ireland.
des.mclaughlin@dcu.ie

Peppard, Joe, Cranfield School of Management, Bedford, MK43 0AL, UK.
j.peppard@cranfield.ac.uk

Abstract

Since the early 1990's, IT outsourcing has become a popular strategy with contracts valued at billions of Euro, and durations ranging from five to ten years. Stories in the computing and business press together with reports of analyses by consultants highlight that during the life-time of some contracts, organisations have reconsidered their original decision to outsource. With this rethink, the options available are to continue with the existing vendor and the existing contract, to re-negotiate some or all of that contract with the existing vendor; to re-tender the contract or part of the contract and seek new vendors; or to backsource, bringing some or all of the previously outsourced activities back in-house. This last option has major implications for the organisation yet there is little empirical research on this final part of the outsourcing process. This paper introduces backsourcing as a legitimate strategy in the outsourcing process. An exploratory study identifies some recent examples where companies have made the decision to backsource, surfacing the rationale behind those decisions. From an analysis of the data, an end-to-end model for the outsourcing process is presented. The paper concludes with an agenda for future research.

Keywords: IT outsourcing, strategy, outsourcing model, backsourcing

1 INTRODUCTION

While organisations have outsourced Information Technology and Information Services almost since the birth of information processing (Dibbern et al, 2004), the beginning of the current era of IT outsourcing is usually linked to the decision by Eastman Kodak in 1989 to outsource its IT services provision to a consortium led by IBM. A landmark paper by Loh and Venkatraman (1992) identified that outsourcing decision as an acknowledgement that total IT outsourcing had now become a serious strategic choice for companies. Since the Eastman Kodak decision, many other organisations have outsourced their IT functions, and, as a result, the value of the IT outsourcing industry has grown rapidly each year. The survey and analysis of the literature on Information Systems outsourcing by Dibbern et al. (2004) quotes various estimates of the value of the IS outsourcing market including a 2003 study by International Data Corporation which, using a narrow definition of IS outsourcing, estimated that actual global IS outsourcing spending was $40 billion in 1996 growing to $71 billion by 2003. Thus, both the scale of the IS outsourcing industry, and its growth rate are significant.

Lee et al (2003) described how issues relating to outsourcing have evolved over time, starting from the 'make or buy' decision, through the motivation for outsourcing; the scope of what was to be outsourced; measurement of performance of the outsourcing vendor; whether to insource or outsource; the increasing complexity of outsourcing contracts, and, most recently, a movement towards shared risks and benefits in a partnership arrangement. In the context of these IT outsourcing trends we offer evidence for another stage of evolution – the backsourcing of previously outsourced IT activities.

The practice of IT backsourcing has been fleetingly referred to number of times in the literature without significant elaboration (Hirschheim and Lacity, 2000; Hirschheim, 1998). There is some

evidence, particularly in the trade press and practitioner literature, to suggest that it is of sufficient scale to warrant further attention (Bushell, 2003; Overby, 2003; Buxbaum, 2002). The objectives of this exploratory study are to get an indication of the extent to which companies are backsourcing previously outsourced IT contracts so as to understand some of their reasons, and to develop an appropriate research agenda. The remainder of this paper is set out as follows: The next section addresses a definitional problem of backsourcing related to the other main terms in the discourse around outsourcing and insourcing. This is followed by a review of the literature identifying key references to backsourcing that are already published and also highlighting the literature relevant to issues in IT sourcing which may give rise to a decision to backsource. A number of instances of IT backsourcing are then introduced and discussed. Based on an analysis of patterns evident in the data, an end-to-end sourcing model is proposed which describes the sourcing process. We end with a research agenda for IT backsourcing to clarify the issues raised.

2   LITERATURE REVIEW

One of the challenges of discussing IT outsourcing is the lack of a common definition of the terms used. Willcocks et al. (1995) point out that the terms information technology (IT) and information systems (IS) are often used interchangeably, which can lead to confusion as to exactly what is being outsourced. They define IT as "the technical means available – equipment and attendant techniques, [which] is essentially activity-based, supply-oriented, and technology- and delivery-focused." IS, on the other hand, are "business applications, more or less IT-based." For the purposes of this paper we will consider that IT outsourcing includes both IT and IS.

Another issue is the inconsistent use of the terms 'insourcing' and 'backsourcing', particularly in the popular press, where most of the up-to-date references for IT backsourcing are to be found. Lacity and Hirschheim (1995, pg 1) define information systems outsourcing as "the use of a third party vendor to provide information products and services that were previously provided internally". Gilley and Rasheed (2000) clarify this further by asserting that outsourcing "represents the fundamental decision to reject the internalisation of an activity". That decision, in turn, is based on the organisation's capability to perform that activity if it wished or decided to do so. So, according to Gilley and Rasheed, a decision to outsource can only be made when "the internalisation of the good or service outsourced is within the firm's managerial and/or financial capabilities". Thus, organisations which have no choice but to acquire a service or an activity from an external supplier are not outsourcing – they never had the option to internalise it in the first place, so they are simply engaging in procurement. Hirschheim and Lacity (2000) define 'insourcing' in a similar way as "the practice of evaluating the outsourcing option, but confirming the continued use of internal IT resources to achieve the same objectives of outsourcing".

Hirschheim (1998) and Kern and Willcocks (2001) define 'backsourcing' as "pulling back in-house [previously outsourced] activities as outsourcing contracts expire or are terminated". This definition implies that there is an *active* decision to bring the activities back in-house, and that this decision is made having considered other options such as extending, renewing, or renegotiating the existing contract, or re-tendering to test the market and potentially find a new outsourcing vendor. Other authors (e.g. Overby, 2003; Buxbaum, 2002; Tiernan, 2002) have used the terms 're-insourcing' or 'reinsourcing' to describe this decision, or have made references to 'insourcing' in this context (e.g. Samuels, 2005; Verhoef, 2005). To avoid confusion, we use the term 'backsourcing' as defined above by Hirschheim, and by Kern and Willcocks.

The motivations of firms to outsource have been summarised by Mahnke as: Financial – reducing costs, obtaining immediate cash, replacing capital outlays with periodic payments; Technical – improving the quality of IT, gaining access to new and/or proprietary technology; Strategic – focus on core activities, facilitate merger and acquisition, access to new and/or proprietary technology, attracting skilled professionals; and, Political – dissatisfaction with internal IT department, regarding IT as a support function, pressure from vendors, or desire to follow trends or imitate.

Frameworks to assist outsourcing decision-making have been described by Clark et al. (1995) and Cronk and Sharp (1995), and a number of authors (e.g. Dibbern et al, 2004; Kern et al, 2002;   Gilley & Rasheed, 2000; Earl, 1996; Clark et al. 1995; and Jurison, 1995) identify the benefits and risks of IT outsourcing. In particular, Jurison (1995) compiled a list of benefits from a wide variety of publications, and concluded that economic considerations, in one form or another, have the primary role in IT outsourcing decisions. The expected benefits of outsourcing identified by Jurison are: cost savings through economies of scale; cash infusion; faster applications development; improved service and quality; access to IT expertise and competence; access to new technologies; flexibility in managing IT resources; and elimination of a troublesome function. Gilley and Rasheed (2000) add some other benefits to this list: avoiding lock-in to a specific type of technology by having an ability to switch outsourcing suppliers as new, more cost-effective technologies become available; and, an increased focus on the organisation's core competencies.

In practice, in a number of cases, these benefits have not always been achieved with a resulting effect on costs, performance and service levels. For example, Boonlert (2005) has observed that outsourcing does not always lead to competitive advantages and cost savings, and argues that the chances of success in outsourcing are at best 50:50. In their summary of the track record of IT outsourcing, one of the issues identified by Kern & Willcocks (2001, pg 5) is a number of organisations encountering 'severe/difficult' problems as a consequence of outsourcing IT. These are: Strategic (e.g. supplier does not understand our business, corporate strategy and IT are no longer aligned);   Cost (e.g. escalation due to loopholes); Managerial (poor supplier staffing, managerial skills shortage, in-house staff resistance);   Operational (defining service levels, lack of supplier responsiveness, getting suppliers to work together); Contractual / Legal (e.g. contract too loose, inadequate service level agreements); and, Technical (e.g. suppliers' IT skills shortage, failure to upgrade IT).   Mahnke et al. (2005) point out that while most IT outsourcing decisions are made based on economic and/or strategic analysis, they at times fail due to relational factors.

The 2005 Global IT Outsourcing Study on buyers and providers of IT outsourcing services by DiamondCluster[1], a Chicago-based management consulting firm, has found that the number of buyers that have abnormally terminated an outsourcing relationship in the past twelve months has more than doubled to 51% in 2004 versus 21% in the previous year. In support of this, a recent study by Deloitte Consulting (Landis et al 2005) on current outsourcing strategies, their impact on organisational performance, and nascent outsourcing trends has identified a number of issues. In particular, the rationale for outsourcing has not fared well with the experience of outsourcing – for example:

> 70% of firms mentioned cost savings as a major driver of their outsourcing decision, yet 37% paid additional / hidden costs for services they believed were included in their contracts

> 57% of firms expected to gain access to best practices / quality / innovation, yet 31% of those participants stated that vendors became complacent once contracts were in place

> 35% of firms expected increased flexibility / capacity / scalability, yet one of the findings of the study was that outsourcing adds a level of rigidity because contracts are binding

> 35% of firms expected a greater focus on core / strategic activities, yet 25% of those participants has mislabelled functions as non-strategic and ultimately backsourced those areas

Similarly, 74% of a sample of fifty 'problem deals' in the Deloitte study failed due to vendor under-performance and/or cost overruns, and 64% of firms in the study backsourced services. Earl (1996) discusses the risks of IT outsourcing and points out that even though none of the risks associated with IT outsourcing were esoteric or unusual, the uncertainties and complexities involved are such that he suggests rephrasing the IT sourcing question to 'why should we not insource IT services'?

---

[1] DiamondCluster 2005 Global IT Outsourcing Study, Spring 2005, in www.diamondcluster.com (accessed 19th Sept. 2005)

So, while there are many papers about different aspects of outsourcing and, in particular, about the motivations, risks, and benefits of outsourcing, together with frameworks to assist decision-making, there are also many reports of general dissatisfaction with the experience of IT outsourcing and that those expected benefits are not being achieved. While Willcocks and Lacity (2000) have described how the results of outsourcing are improving with greater experience of outsourcing, there is also some evidence that the level of dissatisfaction is still growing. In a search of LexisNexis for the period from 1999 through 2004, Landis et al. found a fourfold increase in the instances of sentiment against outsourcing in the final year of the study – 2004. Vendor under-performance is the key driver of outsourcing problems and 42% of the problem deals are related to IT infrastructure.

However, there is a gap in the literature as to what happens when organisations experience such difficulties with their IT outsourcing. While, the evidence would suggest that the majority of outsourcing deals are less than satisfactory, most companies try to work things out with their service providers rather than backsource (Overby, 2005). Still, it is clear from references in trade and practitioner journals and company news and that IT backsourcing is a real and current issue. Among the small number of academic references is Hirschheim (1998) who identified backsourcing as an emerging trend, and pointed out that companies were not achieving the flexibility and service levels that they had expected. Later, Hirschheim and Lacity (2000) used a backsourcing scenario as one of their archetype case studies to show how the senior IT managers achieved lower IT costs and improved service levels by terminating outsourcing contracts and rebuilding the internal IT organisation. In their IT outsourcing literature survey and analysis, Dibbern et al. (2004) suggest that backsourcing may become one of a number of key trends in outsourcing. Cullen et al. (2005) view outsourcing as a strategy with a life cycle rather than as a one-off transaction. From this viewpoint, backsourcing is one alternative to be considered in the final building block of the outsourcing life cycle model in which the final building block is 'refresh – towards the next generation'.

In contrast to the peer-reviewed literature, some practitioner magazines have had relatively extensive discussions about backsourcing. For example, Overby (2005) describes the 'whiplash' effect on JPMorgan Chase employees who were first transferred to IBM as part of an outsourcing deal, then subsequently backsourced when the contract was cancelled. Whiplash includes such issues as uncertainty about continued employment, diminished morale, decreased productivity, and loss of employee trust. The article further describes the cost in management time, attention, and productivity as the contract was outsourced and then backsourced, as well as the pent-up demand of IT projects stalled by the rigidity of the outsourcing contract. Samuels (2005) quotes the head of Deloitte's strategy practice who says that the high level of backsourcing can be partly attributed to poor management decisions with managers rushing headlong into long-term outsourcing contracts. One outcome of this is that over 80% of IT outsourcing contracts are renegotiated at some point during their lifespan. A study by the Performance Management and Benchmarking Practice of XMG[2], a leading global ICT research and advisory firm shows that almost 90 per cent of contract renegotiations in the Asia-Pacific region are at least considering either backsourcing, or select sourcing. The study points out that, until about early 2003, the subjects of backsourcing or select sourcing were almost unknown in the Asia-Pacific region. The XMG study identifies that this trend has been driven by dissatisfaction with service quality, problematical change processes, and lack of integration.

3   DATA COLLECTION

In order to explore this issue of backsourcing, stories published in the news media about backsourcing decisions were accessed via the online news service Factiva. We also searched for relevant articles in trade journals and magazines such as *Computer Weekly*, *CIO Magazine*, *Outsourcing Journal*, and

---

[2] XMG (2005) http://itmatters.com.ph/news/news_06272005a.htm. (accessed 13th July 2005)

Computer World. Instances of backsourcing identified from these sources were followed up by research in the 'Investor Relations' and 'Newsroom' sections on relevant company websites. SEC filings were also examined. While these sources are typically more subjective than peer-reviewed journals, they are however, independently compiled and a useful barometer of contemporary practice, and they report up-to-date information on what is actually happening in the marketplace. A summary of some of the more recent backsourcing decisions resulting from this search is shown in Table 1.

Client	Vendor	Scale & Scope of Contract	Start / End dates	Comment
JPMorgan Chase	IBM	7 year, $5 billion contract covering data centres, help desks, distributed computing, data and voice networks, and 4,000 staff and contractors.	Signed in December 2002. Terminated in 15 Sept 2004 – after 21 months in operation.	After the merger between JP Morgan Chase and Bank One, the new entity wishes to manage its own infrastructure
Sainsburys	Accenture	7 year, £Stg 1.7 billion contract covering design, building implementing and running all the retailers' IT systems and networks. Subsequently extended by 3 years in 2003 to end in 2010.	Contract signed on 1 Nov 2002 and terminated on 27th October 2005 – after 2 years.	IT and supply chain systems valued at £Stg 260 million were written off in the 2004 accounts with further expected material impact on 2005 results
Cable & Wireless	IBM	10-year contract, £Stg 1.8 billion covering all aspects of C&W's IT infrastructure except IT strategy and systems security	Signed in 1998, terminated in June 2003 – after 4.7 years.	Alleged overcharging by IBM. Legal action settled in Sept '03, terms not disclosed
Sears Roebuck (SR)	Computer Sciences Corp (CSC)	10 year, $1.6 billion covering servers, desktop PCs, systems that support Sears' websites, voice & data networks, and decision-support technology. Sears retained mainframes and core retail systems.	Signed in June 2004 and terminated with effect from 11 May 2005 – after less than a year.	SR alleges that CSC failed to live up to the agreement CSC alleges that SR terminated the agreement 'for convenience' as a result of its merger with KMart
Halifax Bank of Scotland (HBOS)	IBM	10-year, £700 million contract covering the provision of IT operational services	Signed on 29 June 2000 and terminated on 29 Aug 2002 – after 2.2 years.	Business requirements changed after a merger.
Gateway Computer Corp.	Affiliated Computer Services	7 year, $400 million contract for midrange, desktop, helpdesk, field services, network mgmt, application development, and maintenance	Signed in Sept 2003 and terminated on 17 May 2004 – after less than a year	Business changes, restructuring and staff reductions reduced the need for an outsourcing vendor.
Bedfordshire County Council (UK)	Hyder Business Services (HBS)	£Stg 267 million for provision and maintenance of a range of IT services including: IT, call centres, communications, HR, finance, education, business support 547 staff transferring to BCC from HBS.	12-year contract signed in 2001. Terminated in Sept 2005 – after 5.5 years.	BCC alleges contractor default HBS states that BCC accepts that HBS was never in breach of contract
Oxford Health Plans, USA	Computer Sciences Corporation (CSC)	5-year, $195 million contract for help-desk services, desktop systems, and network operations.	Signed on 1 Nov 2000, terminated on 10 May 2002 – after 1.5 years.	OHP wished to regain control of the IS function
West Berkshire County Council	Amey, UK	10-year, £Stg 168 million contract to provide a range of services including property, planning, HR, information & communication technology, legal, and administration	Signed on 6th June 2002, terminated on 22nd June 2005 – after 3 years.	Terminated by the contractor as they had been unable to grow other public services business to a sufficient level and could not realise the anticipated efficiencies.

Table 1.   A summary of some recent IT backsourcing decisions

Collected data were inserted into a research database. Inconsistencies were reconciled by triangulation through examining multiple sources of evidence. Company press releases frequently give a favourable 'spin' to the company's decision that was often at odds with the vendor's version, and vice versa. In these situations, commentator analysis in reported news stories was used to adjudicate, although the

arguments of both sides were recorded in the database. The collected data were analysed using content analysis and coded accordingly.

It is recognised that this method of data collection only identified those situations that made it into the public domain. It is possible that many other organisations, on reaching the end of their IT outsourcing contract, made the decision to backsource quietly and without the need to produce a press release or note it in their annual report, and so were not found in this process.

All the outsourcing contracts quoted in Table 1, relative to the scale of the originating organisations, can be considered as significant commitments of money, time, opportunity cost, and other resources on the part of the client company, and also for the outsourcing vendor   In each case, the later decision to backsource, for whatever reason, indicates at least a decision of similar scale.

4   FINDINGS

Evidence provided by the data indicates that backsourcing is clearly a legitimate sourcing option either at the end of a contract or during the lifetime of a contract.   While there is evidence of increasing dissatisfaction with the IT outsourcing experience, from the data it is impossible to say whether, as a practice, backsourcing is more prevalent today than it was ten years ago.   The data were analysed to ascertain the reason the decision to backsource was made.   Often it was difficult to characterise the *real* reasons why a particular contract was terminated. There may be a dispute between the parties, or reluctance to discuss in public the true factors leading to the decision, or legal action may be pending which will stifle statements by the opposing parties.

Problems arise during the Contract / Failure to achieve specific Objectives

Problems arising in the contract, or failure to achieve key business objectives can be a factor.   These problems can quickly lead to accusations, counter-accusations, and a legal dispute.   For example, Cable & Wireless signed an outsourcing contract with IBM in December 2000 for the bulk of its critical management systems including customer care and billing.   After a relatively short period, in February 2002, both parties engaged a consultant to review the benchmarking provisions in the agreement.   Based on the outcome of that review, Cable & Wireless (C&W) initiated legal action in June 2003 against IBM for alleged overcharging.   IBM disputed the allegation and stated that it would 'contest the case vigorously'.[3]   The outsourcing contract, which had been agreed in December 2000, was cancelled on 30 June 2003, just under half-way through its ten-year term. In September 2003 the legal action was settled and, in an agreed statement, both companies said that C&W would now take the outsourcing contract back in-house as a result of "business changes" within C&W. Settlement terms were confidential.

Bedfordshire County Council paid £7.7 million to terminate its 12 year £267 million contract with Hyder Business Systems (HBS) following problems with a SAP implementation which prevented the Council from filing its accounts for 2003/04 before its regulator's deadline.[4]   Each party cited contradictory reasons for the termination with the Council alleging 'contractor defaults' and HBS stating that 'Bedfordshire accepted that HBS was never in breach of contract.'   Rather then become embroiled in legal action, both sides settled on 14 August 2005.

Sainsburys terminated a ten year £1.7 billion outsourcing contract with Accenture signed just two years previously and backsourced its IT activities after a failure to modernise its supply chain had a significant business impact.[5]   This failure led to a £260 million charge against earnings in 2004 when

---

[3] 'Cable & Wireless: Lawsuit against IBM alleges overcharging for Tech Services'. *The Wall Street Journal*, 23 June 2003.
[4] 'Bedfordshire pays HBS £7.7m to terminate outsourcing contract', *Computer Weekly*, 13 September 2005.
[5] Separate Press Releases by Accenture, and by Sainsbury's, 27th October, 2005, and an article in *Information Week* - 'U.K. grocery chain terminates big outsourcing deal with Accenture', 28 October 2005.

it was forced to write off a number of IT systems that did not work as planned. In this case, both parties issued effectively identical press releases on the termination of the contract and neither side initiated legal action.

IT now seen as strategic – A Desire to regain Control

From the data, this arises in two main ways: with a realisation that the previous decision to outsource was based on the assumption that IT was a commodity whereas it is now realised to be core to business strategy; or, as a result of a merger where significant new or enhanced skills and capabilities are now available to the new entity.

For example, in April 2004, health care company Oxford Health Plans (OHP) terminated its five-year, $195 million outsourcing agreement with Computer Sciences Corporation (CSC) just 18 months into its five-year $US195 million contract as it wished to regain control of its IS function. CSC had been contracted to take responsibility for a variety of OHPs information systems, including its data centre operations, help desk, desktop systems and network management, with Oxford retaining many of the IS functions it viewed as important to its core businesses, including application development and maintenance, database administration, quality assurance, programme management and architecture. In a statement announcing the termination, president and COO of OHP Charles Berg said they believed that fully integrating the entire function would allow the company to deploy technology solutions in a more flexible, timely and cost-effective manner to meet its business goals.

Based in Seattle, Washington Mutual (WaMu) is a provider of financial services to consumers and small businesses across the USA. IBM Global Services had been awarded a ten-year, $533 million outsourcing contract in 1996 to provide desktop support, network services, help desk, network management, architecture, and strategy for the company. In 2001, the newly-appointed Chief Information Officer identified that the outsourcing arrangement was negatively affecting operational excellence and customer service and decided to backsource the activities into the WaMu information technology group citing the reason that "the functions involve such close interactions with customers."

The large Australian bank and insurer Suncorp undertook one of the biggest IT backsourcing projects in Australian corporate history after it acquired GIO Australia from AMP for $Aus 1.4 billion in mid-2001. GIO's infrastructure had been outsourced to Computer Sciences Corp. Suncorp decided to bring the IT operations of the newly acquired GIO back in-house as they both ran very similar platforms through mainframe, midrange and desktop and they saw the opportunity to get benefits from economies of scale. In the process they claim to have saved $Aus 120 million and created 80 jobs. Their reason for backsourcing was that the company believes that doing the bulk of its IT in-house is the best way to maintain its competitive edge. Suncorp Group Executive, IT Carmel Gray says that "IT is really integral to the quality of service customers receive from us and every interaction they have with us. It is very difficult to tell where technology ends and products and services begin these days, so our preference is to manage IT in-house on the basis that we can run it at least as well as or better than the best outsourcer" (Bushell, 2003).

Restructuring due to merger and acquisition activities can also lead to the reconsideration of the continued usefulness of an IT outsourcing deal when the entity resulting from the merger or acquisition has significantly greater economies of scale or IT skills. Following its merger with Bank One, JPMorgan Chase backsourced a $5 billion contract with IBM. [6] The reasons given by the CIO of JPMorgan Chase for this decision were that the merger created a new firm with significantly greater capacity to manage its own technology and infrastructure and had the significant scale, enhanced capabilities, tools and processes to build its own global infrastructure services organization. They believe that "managing their own technology infrastructure is best for the long-term growth and success of their company and shareholders and would give them competitive advantages, accelerate

---

[6] JPMorgan Chase Press Release 15th September, 2004

innovation, and enable them to become more streamlined and efficient." JP Morgan has determined that, with its Bank One merger, it now has "sufficient scale to do its own IT, as well as to justify a belief that IT can serve as a core competency from which it can derive a competitive advantage."

Similarly, after its merger with Halifax Building Society in 2001 to form Halifax Bank of Scotland (HBOS), Bank of Scotland decided to terminate its ten-year £700 million outsourcing arrangement with IBM. When the contract was signed in June 2000 it was seen as one of Europe's biggest outsourcing deals. The decision to terminate the contract cost HBOS tens of millions of pounds both in transition costs to backsource the activities and for penalties to IBM for terminating the contract early without sufficient cause[7]. HBOS also faced significant hurdles in rebuilding the management team and enticing the staff who had transferred to IBM to return to HBOS.

Changes in the Business Environment, Business Change and Evolution

The business environment changes continually. Many of the early outsourcing contracts were negotiated in the early 1990s when the economic climate was depressed. The upturn in business in the late 1990s obviated the need for those cost savings-oriented outsourcing deals. Extension into new product areas or new markets, or the reverse – contraction due to poor business performance can lead to a decision to outsource functions, or to cut back on existing outsourcing contracts when the need is no longer evident. For example, after they changed their CEO, contracted their operations by closing 188 retail outlets which eliminated about 2,500 positions, and bought eMachines Inc. to reposition their brands, Gateway, Inc. then backsourced a seven year $400 million services contract which it had signed with Affiliated Computer Services just seven months before.

Technology Change

The rapid and widespread adoption of internet-related technologies during the mid- to late 1990s is an example of a sea change that can take place in the technologies used by organisations. Technology change and the associated dramatic reductions in cost and improvements in performance washed out the cost advantages of those early IT outsourcing contracts. Overby (2005) quotes a JPMorgan systems engineer who had survived the outsourcing, and then backsourcing at Bank One, who said that "once they signed the [outsourcing] contract we didn't move at all beyond that date as far as picking up new technologies that would give us competitive advantage. Technology was not refreshed, and new projects were not rolled out."

Management Change

A new management team, or individual changes, particularly at CEO or CIO level have also led to a decision to reconsider the value being obtained from the IT outsourcing contract. Some new management teams have reconsidered the contribution of information technology in a strategic context – that which was previously considered commodity may, on reflection, be considered a core function. The attitudes and preferences of the new management team were clearly a factor in the decision by the newly-merged JPMorgan Chase / Bank One entity to backsource. The newly-appointed CIO of the merged entity had previously been CIO of Bank One and had backsourced their operations from IBM Global Services and AT&T in 2002.

Other Reasons

Sears Roebuck ended a $1.6 billion technology services contract with Computer Sciences Corp. (CSC) with effect from May 11, 2005 "for cause due to CSC's failure to perform certain of its obligations in accordance with the terms of the Agreement."[8] The ten-year contract was agreed in June 2004, under

---

[7] *Computer Weekly* 29th August 2002, http://www.computerweekly.com/Articles/2002/08/29/189257/Bankbins%c2%a3700mIBMdeal.htm (Accessed 19th October 2005)
[8] Public filing with the US Securities and Exchange Commission by Sears Holdings Corp. on 11th May 2005.

which CSC would provide IT infrastructure support services, including desktops, servers, systems to support Sears-related Web sites, voice and data networks and decision-support technology.   While Sears Roebuck alleges that Computer Sciences Corp failed to live up to their agreement, CSC, on the other hand, alleges that Sears terminated the agreement "for convenience due to change in control" as a result of its merger with Kmart Holding Corp.

First Consulting Group, Inc, also signed a seven-year outsourcing agreement in November 1999 with The New York and Presbyterian Hospital (NYP), New York, USA. In July 2005 NYP exercised its option to terminate the outsourcing agreement "for convenience" effective 31 December 2005, one year before the end of the contract[9].

In June 2005, Amey, UK terminated a ten year £168 million outsourcing agreement with its client, West Berkshire County Council after just three years because of its inability to grow other public sector business to a sufficient level. This is a refreshing contrast to expectations of poor performance which would arise from the Winner's Curse (Kern et al, 2002). Apparently, in this case, when Amey realised that it would be unable to grow its other public sector business to a sufficiently profitable level, it initiated a discussion which ended with both sides reaching an amicable and sensible arrangement to terminate the contract. Tony Barry, group director, strategic development for Amey said[10]: "Amey has made a major contribution to the development of council services. It has become clear, however, that the original objectives for the partnership, set by both the council and Amey, cannot easily be realised. The settlement is therefore in our collective best interests."

5   DISCUSSION AND OPPORTUNITIES FOR FURTHER RESEARCH

The decision to outsource is usually made in the context of corporate strategy.   A number of authors have discussed the strategic aspects of IT outsourcing (Quélin and Duhamel, 2003; Roy and Aubert, 2002; DiRomualdo and Gurbaxani, 1998; Willcocks et al, 1995; and Quinn and Hilmer, 1994). Several authors have written about frameworks for helping to make an IT outsourcing decision (deLooff, 1995; Cronk & Sharp, 1995), and Cullen et al (2005) have described a detailed process for client organisations to follow when considering an outsourcing contract to improve their likelihood of success while minimising their risk.   However, despite extensive literature on the risks of outsourcing and on frameworks for decision-making related to IT outsourcing, evidently it still goes wrong. We outline below what we believe would be areas for fruitful research.

After the contract is awarded to the successful vendor or multiple vendors, and after an initial transition period, the client begins to experience the services and deliverables of the outsourcing contract. The contract may proceed normally and reach the end of its term uneventfully. However, the Deloitte study has found that while 30% of companies have encountered 'normal growing pains' with the outsourcing contract, 70% have had 'significant negative experiences', and so, problems emerge with the contract. One could speculate that a potential driver of problems in the contract is the so-called 'winner's curse' (Kern et al, 2002), in which vendors make unrealistically low bids to win the contract, then try to recover using practices such as identifying areas in need of urgent attention, but which are not included explicitly in the contract – so earning extra fees. This, and other similar practices where a vendor focuses disproportionately on recovering costs, are likely to lead to trade-offs in performance or quality which are unfavourable to the client's expectations from the contract.

The outsourcing contract may proceed normally and uneventfully towards its natural end. Alternatively, several types of change can occur during the contract: A change in the management

---

[9] First Consulting Group Press Release, 18th July 2005.   URL http://investor.fcg.com/phoenix.zhtml?c=61499&p=irol-news (Accessed 19th October 2005)
[10] 'West Berkshire Council and Amey end partnership.' *Local Government Chronicle*, 22 June 2005. Accessed on Factiva 20 November 2005.

team, or changes in key individuals, or business change and evolution – either extension into new product areas or new markets, or the reverse – contraction due to poor business performance, can lead to a decision to re-evaluate the original decision to outsource. Technology and business-related innovations will also continue to evolve during the lifetime of the contract and may also trigger a re-evaluation of the outsourcing contract. At that point, the main options for this decision are:

1. To renew, extend, or renegotiate some or all of the IT outsourcing contract with the original outsourcing vendor for better terms in the light of experience and expected new needs;

2. To re-tender some or all of the IT outsourcing contract to the market to establish whether a different vendor can meet the needs of the organisation better;

3. To backsource some or all of the previously outsourced activities and carry them out in-house.

The model in Figure 1 is based on patterns observed in the data and illustrates a summary of the issues leading towards the re-evaluation of the outsourcing decision, and the main options available at that point.
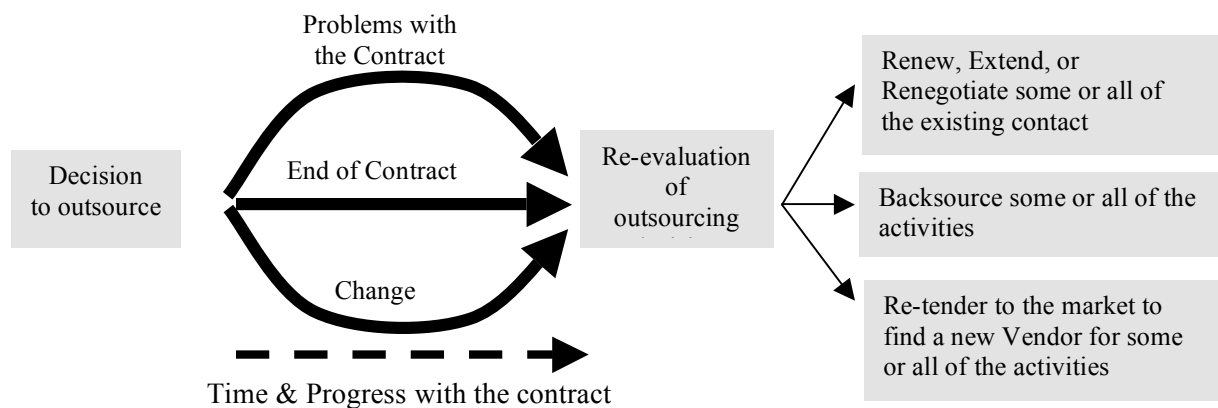

Figure 1.   *An end-to-end model of issues and options for evaluating the outsourcing decision*

Clearly, a good or poor experience with the vendors in the just-terminated contract will, to a large extent, determine the choice made. In the case of the first two of these options, firms opening or re-opening discussions with outsourcing vendors will start negotiations from a different starting point in the light of their learning and experience from their soon-to-be-terminated outsourcing contract. New requirements may be included at this stage, as well as the opportunity to include technology changes and other environmental changes since the last contract was negotiated. Also, in the case of the first two options, some firms may considering the formation of true alliances / partnerships involving the formation of new entities with synergistic skills aimed at specific markets, or equity holding deals with vendors and clients taking shareholdings in the other company (Dibbern et al, 2004).

The third option – backsourcing is the focus of this paper. We have used secondary research to get an indication as to the scale of IT backsourcing. We will continue with this research and also collect primary data to build a more comprehensive picture of the contemporary issue of backsourcing – in particular the motivations for, and implications of a decision to backsource, together with guidance as to the processes around backsourcing.

The motivation for backsourcing is just as relevant a topic as the motivation for outsourcing. To take just one example, it is interesting to note that, comparing quotes from the Vice Chairman of JPMorgan Chase in a company press release when the outsourcing contract was awarded to IBM in Dec 2002, with another quote by the CIO of the newly merged Chase / Bank One in another press release at the time of the backsourcing announcement in Sept 2004, Overby (2005) suggests that the reasons for backsourcing were basically the same reasons that were asserted for outsourcing in the first place. In

both cases technology was seen as key to competitive advantage, and the just-announced arrangement (whether outsourcing or backsourcing) would enable innovation and efficiency.

In our (albeit relatively small) sample of organisations that have backsourced it is interesting to note that, while saving cost has often been quoted as a main reason for outsourcing, a failure to achieve such cost savings, so far as we can ascertain from published statements, is not a main reason for backsourcing. While cost savings are clearly part of the decision, it appears that the main reasons for backsourcing in this sample have more to do with a desire to regain control and flexibility, a new recognition of the role of information systems, or strategy change following a change of management. Another revealing point is that all of the companies listed in Figure 1 appear to have totally bacsourced, that is, none of them backsourced selectively.

A number of large datasets have been quoted in the literature over the years (e.g. Lacity and Willcocks, 2000; Lacity and Willcocks, 1998) to establish some of the main issues in outsourcing practices – why outsource, what outsourcing option to use, and for which IT activities, among other questions. Recent research has focused on implementation issues such as how to outsource and on an evaluation of the outcomes of outsourcing. Although many of the organisations that were used in those analyses are anonymous, one interesting area for further research would be for the authors to re-examine their datasets and follow up to identify those organisations which have backsourced so as to build a picture as to their motivations, decision-making process and experiences.

What is remarkable about our data is the number of examples where the outsourcing contract was terminated within one or two years of signing the contract, in particular given the extensive analysis and negotiations that presumably took place beforehand, and the cost, possible penalties, legal action, management resources and complexity involved in re-absorbing or hiring staff, and re-integrating with business areas. With these potential problems and penalties raised by a decision to backsource, is it more desirable for some organisations to renegotiate an outsourcing contract with the existing vendor rather than go through the trauma and further disruption of backsourcing their IT function, or to begin the process of establishing a new outsourcing relationship with a new vendor? If so, this would be evidence of effective lock-in by a client to a vendor, an issue which has been identified as one of the risks of outsourcing but for which there does not appear to be any empirical evidence. Another area for research would be in regard to the decision-making process. Was the backsourcing the result of a flawed decision – that is, was the decision to outsource a good decision in the first place? Or, was backsourcing the result of a flawed process – the decision was correct, but was poorly implemented by the firm, or was the result of poor performance by the vendor? Or, was the decision to outsource correct at the time, but important aspects of the business and its environment changed, or technology developments obviated the need to outsource in the first place? Finally, questions around effective backsourcing and how best to re-integrate while maintaining / restoring IT value merit some research.

6   CONCLUSION

In this paper, we have shown a number of instances to indicate that backsourcing is significant in scale. Its implications are also significant, either when it is being implemented, with the attendant issues of acquiring, rebuilding and re-integrating knowledge, resources, and capabilities back in-house or, perhaps more significantly, when managers decide not to backsource because it would be so disruptive to business and to the organisation, and too difficult to achieve. We have identified areas where we believe further research would usefully elaborate on these issues.

7   REFERENCES

Boonlert, W. (2005). Determinants of IS sourcing decisions: A comparative study of transaction cost theory versus the resource-based view. Journal of Strategic Information Systems, 14, 389-415
Bushell, S. (2003). Inside Moves. CIO Australia Magazine, Issue of 11 April.

Buxbaum, P. (2002). Bringing IT back home. Computerworld, Issue of 29 July, 36 (31).

Clark, T.D., Zmud, R.W. and McCray, G.E. (1995). The outsourcing of information services: Transforming the nature of business in the information industry. Journal of Information Technology, 10, 221-237.

Cronk, J. and Sharp, J. (1995). A framework for deciding what to outsource in information technology. Journal of Information Technology, 10, 259-267.

Cullen, S., Seddon, P. and Willcocks, L. (2005). Managing Outsourcing: The Lifecycle Imperative. MIS Quarterly Executive, 4 (1), 229-246

DeLooff, L.A. (1995). Information Outsourcing decision making: A framework, organisational theories, and case studies. Journal of Information Technology, 10, 281-297.

Dibbern, J. Goles, T. Hirschheim, R. and Jayatilaka, B. (2004). Information systems outsourcing: A survey and analysis of the literature. The DATA BASE for Advances in Information Systems, 35 (4), 6-102.

Earl, M. (1996). The risks of outsourcing IT. The Sloan Management Review, 37 (3), 26-32.

Gilley, K.M. and Rasheed, A. (2000). Making more by doing less: An analysis of outsourcing and its effects on firm performance. Journal of Management, 26 (4), 763-790.

Hirschheim, R. (1998). Backsourcing: An emerging trend? Outsourcing Journal, September.

Hirschheim, R. and Lacity, M. (2000). The myths and realities of information technology insourcing. Communications of the ACM, 43 (2), 99-107.

Jurison, J. (1995). The role of risk and return in information technology outsourcing decisions. Journal of Information Technology, 10, 239-247.

Kern, T. and Willcocks, L.P. (2001). The Relationship Advantage: Information Technologies, Sourcing, and Management. Oxford University Press, Oxford.

Kern, T., Willcocks, L.P., and van Heck, E. (2002). The Winner's Curse in IT outsourcing. Strategies for avoiding relational trauma. California Management Review, 22 (2), 47-69.

Lacity, M.C. and Hirschheim, R. (1995). Beyond the Information Systems Outsourcing Bandwagon: The Insourcing Response. Wiley, Chichester.

Lacity, M.C. and Willcocks, R. (2000), Survey of IT Outsourcing experiences in US and UK organisations. Journal of Global Information Management, Apr-June, 5-13.

Lacity, M.C. and Willcocks, R. (1998). An empirical investigation of information technology sourcing practices: Lessons from experience. MIS Quarterly, 22 (3), 363-408

Landis, K, Mishra, S. and Porrello, K. (2005). Calling a Change in the Outsourcing Market: The realities for the world's largest organisations. Deloitte Consulting.

Lee, J.N., Huynh, M.Q., Kwok Ron Chi-Wai, and Pi, S.M. (2003). IT outsourcing evolution: Past, present, and future. Communications of the ACM, 46 (5), 84-89.

Loh, L.V., and Venkatraman, N. (1992). Diffusion of information technology outsourcing: Influence sources and the Kodak effect. Information Systems Research, 3 (4), 334-358.

Mahnke, V. Overby, M.L. and Vang, J. (2005). Strategic Outsourcing of IT services; Theoretical Stocktaking and Empirical Challenges. Industry and Innovation, June.

Overby, S. (2003). Bringing I.T. back home. CIO Magazine, 1 March.

Overby, S. (2005). Backsourcing Pain. CIO Magazine, 1 September.

Quélin, B. and Duhamel, F. (2003). Bringing together strategic outsourcing and corporate strategy: outsourcing motives and risks. European Management Journal, 21 (5), 647-661.

Quinn, J.B. and Hilmer, F.G. (1994). Strategic Outsourcing. Sloan Management Review, Summer.

Roy, V. and Aubert, B.A. (2002). A resource-basaed analysis of IT outsourcing. The DATA BASE for Advances in Information Systems, 33 (2), 29-40.

Samuels, M. (2005). The insourcing trend is bringing it all back home. IT Week, Issue of 12 May.

Tiernan, C. (2002). The three 'R's – Renegotiating, Retendering, Reinsourcing. IMIS Journal, October, 21-22.

Verhoef, C. (2005). Quantitative aspects of outsourcing deals. Science of Computer Programming, 56, 275-313.

Willcocks, L.P., Fitzgerald, G., and Feeny, D. (1995). Outsourcing IT: The Strategic Implications. Long Range Planning, 28 (5), 59-70.