Enterprise Systems Outsourcing "Behind the Curtain":
A Case Study Showing How Rational and Institutional Explanations Coexist and Complement Each Other

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ABSTRACT

Outsourcing is now a feasible means for enterprise systems (ES) cost savings, but does however increase the complexity of coordination substantially when many organizations are involved. We set out to study ES outsourcing in a large Scandinavian high-tech organization, SCANDI, a case setting with many inter-organizational partners, trying to answer the question: Why does SCANDI engage in these very complex outsourcing arrangements? To answer this question we have analyzed documents, observed meetings and gathered data from interviews in four parts of SCANDI. The first data analysis found just the rational front stage cost-saving explanation; but then, with a more careful analysis focusing on institutional factors, other backstage explanations "behind the curtain" were uncovered, such as management consultants with a "best practice" agenda, people promoting outsourcing, thereby being promoted themselves, and a belief in outsourcing as a "silver bullet": a recipe to success, solving everything.

Keywords: *Case Study, Enterprise Resource Planning (ERP) Systems, Enterprise Systems, Institutional Theory, Organization, Outsourcing*

INTRODUCTION

The development of Enterprise Systems (ES) has been a major trend within both the private and public sectors over the past decade. They often trigger major organizational changes and at the same time, introduce high-risks with potential high rewards (Chae & Lanzara, 2006, p. 100; Markus, 2004). ES can be defined as

large-scale organizational systems, built around packaged ES software, and composed of people, processes, and information technology (Seddon, Willcocks, & Shanks, 2003).

Outsourcing of ES is becoming increasingly important in today's global business environment in order to gain cost savings (Olson, 2007). Gartner valued the application outsourcing market at $76.9 billion in 2009 and forecasted that it would increase to $97.9 billion in 2012 (Young et al., 2008), which is

a high growth rate in these turbulent economic times, indicating that an outsourcing trend is in progress.

ES outsourcing is the practice whereby the organization "purchases goods or services that were previously provided internally" (Lacity & Hirschheim, 1993, p. 74). In this paper, we interpret this further, defining it as *any* type of outsourcing involving ES and Information Technology (IT). This includes application development on top of the ES, operation of a data centre running ES, business processes enabled by the ES, or the entire IS function (inspired by Dibbern, Goles, Hirschheim, & Jayatilaka, 2004). Thus, outsourcing in this context means aggregating specific tasks or entire processes and moving them to one or more outsourcing vendors (McFarlan & DeLacey, 2004).

Organizations have claimed that ES/IS outsourcing reduces cost and time, increases quality and reliability of product and services, improves business performance, and releases organizations to concentrate on core competencies (McFarlan & DeLacey, 2004; Vitharana & Dharwadkar, 2007).

The reasons why organizations outsource are dominated by rational explanations related to bounded rationality and opportunism (Williamson, 1981), and cost savings seem to be a prevailing explanation, which is repeated in the literature (Dibbern et al., 2004; Olson, 2007).

However, though a majority of extant literature finds mainly rational explanations for engaging in ES/IS outsourcing, our own experience from many companies and from many outsourcing arrangements made us speculate whether there was more to it. Using a theatrical metaphor we ask, could it be that there were both "front stage" explanations as well as other, different, "back stage" explanations hidden "behind the curtain"?

To address this curiosity, we set out to study ES outsourcing in a large Scandinavian high-tech organization, SCANDI, which has many inter-organizational partners. Our research question was: *Why does SCANDI engage in very complex ES/IS outsourcing arrangements?*

The paper is organized as follows. First we introduce the Transaction Cost Theory and the Institutional Theory. Then we explain our research methodology based on the interpretive paradigm. The section that follows outlines the SCANDI case study. The analysis of front stage and back stage explanations is then presented and is followed by a discussion and implications. Finally, we present some concluding remarks and sum up significant new insights, both from a theoretical point of view and from a practitioner perspective.

RATIONAL AND INSTITUTIONAL EXPLANATIONS

The theories used in this study have evolved over time in reaction to our progressive understanding of data collected during field work. Rational explanations were easily identifiable, and institutional explanations resulted from searching for "behind the curtain" explanations while interpreting the field data and IS literature. Two alternative theories were then adopted for this research: (1) Transaction Cost Theory (TCT), and (2) Institutional Theory (INT).

Both theories can be applied with an interpretive approach, where they are viewed as alternative "lenses" for interpreting outsourcing decisions, and not as the objective deterministic truth about outsourcing decisions (Lacity & Hirschheim, 1993). TCT was adopted because it has the widely accepted view that organizational actors make outsourcing decisions based on the economic rationale used in a majority of outsourcing literature, embedding an understanding about bounded rationality and opportunism (Scott & Davis, 2007, pp. 53-56). We adopted INT to explain outsourcing decisions in line with Vitharana and Dharwadkar (2007), because the theoretical constructs in INT are recognizable in our empirical data. The two theoretical lenses are presented in the conceptual framework in Figure 1, which is used to answer the research question.

Figure 1 shows that both rational and institutional factors impact the decision-making

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