Chapter 7.14
Analysis of a Large-Scale IT Outsourcing "Failure":
What Lessons Can We Learn?

Anne C. Rouse
Deakin University, Australia

Brian J. Corbitt
Shinawatra University, Thailand

ABSTRACT

Much of the research that has been carried out into outsourcing is based on relatively successful case studies. Yet drawing inferences from case studies when those with largely negative outcomes rarely see the light of day represents a significant problem. When negative cases are systematically unrepresented, there is less opportunity to subject theory to scrutiny. This chapter goes some way towards redressing this trend, by reporting on a large scale "selective" outsourcing arrangement that has been publicly described as a failure — the Australian Federal Government's "whole of government" IT infrastructure outsourcing initiative. This initiative, originally promoted as likely to lead to a billion dollar saving, was abandoned early in 2001, after a damning public report by the Australian Auditor General. However, a detailed study of the initiative suggests that the "failure" occurred despite the project adhering to many of the recommended guidelines for successful outsourcing that had been derived from earlier case analysis. The findings have important implications for decision makers confronted with outsourcing choices. The study suggests that the risks of outsourcing are often downplayed, or ignored in the rush to reap the expected benefits. The study also suggests that expectations of savings from outsourcing IT are often substantially higher than those that have been empirically confirmed in the field. Decision makers are advised that key assumptions about costs, savings, managerial effort, and the effects of outsourcing on operational performance might be incorrect, and to plan for their outsourcing activity accordingly. They should pay particular attention to coordination and transaction costs, as these tend to be overlooked in the business case. These costs will be magnified if "best in breed" multiple-vendor outsourcing is chosen, and if contracts are kept short. Decision-makers are also

warned of the difficulties they are likely to have at the end of an outsourcing contract if there is not a large and robust pool of alternative vendors willing to bid against the incumbent.

INTRODUCTION

This chapter describes the outcomes of a decision by the Australian Federal Government to outsource the provision of supposedly low-risk, IT (information technology) infrastructure services. The government initiative was an attempt to save up to $1 billion (AU) dollars. The decision caused substantial controversy within Australia, and therefore a large body of public documentation became available to researchers. This documentation, supplemented by anonymous interviews with key players, provided a unique opportunity to explore a "failed" outsourcing case study.

Most large-scale outsourcing arrangements are treated as highly confidential by all players, because both the purchaser and vendor do not wish potential competitors to have information about costings, and because outsourcing announcements tend to have positive impacts on share prices (Loh & Venkatraman, 1992). Any public announcement that the anticipated benefits of outsourcing were *not* achieved would lead to depressed share prices. In the circumstances, it is not surprising then that few announcements of this nature are made by commercial organizations. Consequently, the trade literature is saturated with positive announcements of attractive benefits that outsourcing is *expected* to bring, but very little evidence of actual experiences.

The case analyzed in this chapter provides an opportunity to explore a widely reported outsourcing failure, and so to reconsider the "evidence" that has been used to promote outsourcing. The chapter discusses the methodology and some of the key findings, and then considers the implications of these findings for practitioners.

BACKGROUND

There is a relative shortage of negative case studies in the outsourcing literature — with the notable exception of the early work of Lacity and Hirschheim (1993, 1995) and a handful of more recent cases reported by Kern and Blois (2002), Kern, Willcocks, and Van Heck (2002) and Dalcher (2005). This probably reflects the political realities of case study research — organizations that have unhappy experiences with their outsourcing do not tend to talk about it "outside" for fear of appearing badly managed. Moreover, university ethics committees tend to insist that research participants should be free to withdraw from research at any time, and this, combined with a reluctance to publish anonymous cases, acts to prevent the publication of negative organizational experiences. The result of a process that favors the positive over the negative is that decision makers can be lulled into perceiving outsourcing as more successful, and less risky than it really is. As a result, it has almost become an article of faith that outsourcing business services saves money and improves service quality, even though the quantitative empirical evidence does not necessarily support this.

When the IT outsourcing literature is examined, it is also clear that the majority of IT outsourcing cases reported in the academic and trade literature has involved private sector organizations (illustrated in Dibbern, Goles, Hirschheim, & Jayatilaka, 2004). Yet substantial proportions of IT investment within western economies are made by the "not for profit" and public sectors, and over the past two decades governments all around the world have been outsourcing IT services as a key part of public sector reforms.

This chapter attempts to address the imbalance in the literature by reporting on a large-scale public sector outsourcing exercise that was widely reported in the literature to be a "failure", or even, in some cases a "fiasco" (Rouse & Corbitt, 2003).

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