Chapter 16
Outsourcing Contract Success:
A Quality Management Perspective

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ABSTRACT

Despite the phenomenal growth in outsourcing of various business functions like Enterprise Systems outsourcing, IT outsourcing, and Business Process outsourcing, there has been relatively less attention given to the high-risk area of outsourcing contracts. In this regard, contract has been the conventional medium for governing outsourcing relationships. This study aims to bring forward the importance of quality in the entire contracting process, involving contract planning, pre-contract negotiation, contract formulation, and post-contract management. Specifically, the objective of this paper is to posit a quality framework for planning and analyzing outsourcing contracts that will in turn help in achieving outsourcing success. The framework proposed can be a useful guiding lens for practitioners and researchers associated with outsourcing work.

INTRODUCTION

Businesses today have grown in complexity and it is becoming increasingly difficult to do everything in-house. As a result, organizations are outsourcing their processes ranging from non-core operations to mission-critical operations (Yadav & Jaiswal, 2006; Quelin & Duhamel, 2003). Outsourcing is now being seen less and less tactical, cost-saving drive and more and more as a strategic direction that organizations follow (Johnson, 1997). There is a growing body of literature in management that highlights the globalization phenomenon and global corporations' need to plan for such work environments (Yadav, Gupta, & Saxena, 2007).

Contracts have been the traditional vehicle through which the outsourcing relationships have been governed (Clark, Zmud, & McCray, 1995).

The role of contracts is to prevent opportunism by stipulating an acceptable behavior at the outset of the outsourcing project. Contracts come at a price for both the client and the service provider. Proving violation of a contract is costly, thereby potentially limiting the usefulness of contracts (Clark, Zmud, & McCray, 1995). Further complicating the use of contracts is the difficulty of verifying what the outsourcing vendor is doing and determining on an ongoing basis whether the goals of the vendor are consistent with those of the client (Eisenhardt, 1989).

Despite the abundant literature available on outsourcing (Yadav & Gupta 2008; Dibbern, Goles, Hirschheim, & Jayatilaka, 2004), there are very few studies addressing the 'high risk' area of outsourcing contracts. The objective of this paper is twofold. Firstly, the paper offers to bridge the gap in outsourcing research literature by bringing forward the importance of quality in the entire contracting process. This research suggests that contracting quality is the prerequisite for outsourcing success. Secondly, the paper proposes a quality framework for planning and analyzing outsourcing contracts.

The paper proceeds as follows. The next section reviews the background literature on outsourcing, contracts and quality. Subsequently, the conceptual model is presented. The paper concludes with potential contributions and future research directions that this study offers to theory and practice.

LITERATURE REVIEW

Outsourcing

Outsourcing is one of the fastest growing phenomenons of the business world today. Outsourcing is defined as the procurement of products and services from sources that are external to the organization (Lankford & Parsa, 1999). Outsourcing involves contracting with an external provider for the provision of a service which may have been provided using in-house staff (Domberger, Fernandez, & Fiebig, 2000). A wrong sourcing decision can result in lost capabilities and exposure to risks that can result in business failure (Loh & Venkatraman, 1992; Ngwenyama & Bryson, 1999). It is therefore essential to ensure that the entire outsourcing plan is in place before the organization steps into an outsourcing relationship.

Academic and practitioner literature categorizes various kinds of outsourcing like Enterprise Systems outsourcing, IT outsourcing (Dibbern, Goles, Hirschheim, & Jayatilaka, 2004) and Business Process outsourcing (Yadav and Gupta 2008). The intent of this paper is not to distinguish or add to the growing taxonomy of different kinds of outsourcing rather the objective is to focus on 'outsourcing contracts' in general that can be applied to a whole gamut of outsourcing activities.

Contracts

Contract is the defining document of the outsourcing relationships (Walden, 2005). All the outsourcing customers researched by Lacity and Hirschheim (1993) agreed that contract was the number one key issue to a successful outsourcing relationship. Outsourcing contracts involve complicated business and legal issues, and are fraught with risks for both the outsourcing customer and the outsourcing vendor (Lee, 1996).

In outsourcing, the client organization and the vendor organization engage in a relationship. The two organizations draft a contract to define the parameters of the relationship (Walden, 2005). The contract is split up into sections that address the various aspects of a client-vendor relationship, for instance, assets, human resources, payment, performance measurement, intellectual property etc.

Quality

Quality is defined in terms of product or service features and freedom from deficiencies (Juran, 1997). Service quality refers to the degree and direction

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