CHAPTER 6: FINDINGS AND CONCLUSIONS

6.1 SUMMARY OF RESEARCH

Academic research in business process outsourcing has not kept pace with the growing importance and acceptance accorded to this management practice (Rouse and Corbitt 2004, Gewald et al. 2006, Whitaker et al. 2006). This study was an attempt to fill that lacuna by undertaking a study of business process outsourcing controls. The study builds on significant prior research in the area of inter-organizational control (Kirsch 1997, Kirsch et al. 2002, Henderson and Lee 1992) and extends it to the domain of business process outsourcing.

6.2 MAIN FINDINGS

The key findings of this study were:

1. Business process outsourcing relationships are governed by an array of control practices which may be divided into:
   
   - contractual measures
   - social measures
   - self-control measures of the vendor
2. Nature of the outsourced process (w.r.t. transaction attributes) is significantly related to degree and mode of control

3. Degree of control is significantly related to outsourcing success

4. An initial formulation of the construction process of business process outsourcing controls is proposed indicating
   - The ‘Service Contract’ as the key setter of control practices
   - Dynamism of control practices over the relationship lifetime
   - A multiplicity of controllers of the relationship

6.3. **CONTROL PORTFOLIOS IN BUSINESS PROCESS OUTSOURCING**

Control, in this research, refers to a range of mechanisms to monitor and execute operations to increase the probability of conformance to organizational (both client and vendor) requirements in the outsourcing relationship. At the onset of the analysis an attempt was made to define and describe these mechanisms as observed in the four case sites. Control mechanisms observed could be differentiated into (1) contractual measures; (2) measures which involved socialization of client and vendor executives and (3) measures the vendor undertakes wherein both the goals and the actions through which they should be achieved are determined by the vendor. Each mechanism was then associated with a mode of control viz, outcome, behavior, clan or self.
Contractual mechanisms formed a part of the contract variously referred to as ‘service level agreement (SLA)’ or ‘statement of work (SOW)’ and focused on four aspects: Process, People, Performance and Pricing.

Process controls were geared towards efficient provision of products and services to clients and end users as per their expectations on a consistent basis and included:

- Process work-flow documentation
- Task work-flow documentation
- Transaction monitoring
- Staffing and scheduling
- Data security measures

Process flows, task work-flow documentation, staffing/scheduling and data security measures were all mechanisms by which the client explicitly specified rules, procedures, or processes for the vendor to follow while transaction monitoring facilitated direct observation of the vendor’s behavior and thus were illustrations of behavior control.

People controls ensured that the vendor workforce was appropriately skilled and motivated enabling them to effectively and efficiently deliver quality products and services and included:

- Recruitment guidelines
- Training
- Staff testing

People controls explicitly specified procedures and processes for the vendor to follow while simultaneously effected selection of members who shared a common ideology and thus represented both behavior as well as clan control modes.

Performance control mechanism - 'metrics' were the key focus of outsourcing contracts. This mechanism explicitly specified desired outcomes and included information systems, to evaluate the quality and timing of outputs delivered by the vendor and thus illustrated the use of outcome controls.

Pricing based controls which served to align the incentives of the vendor more completely with those of the client created a shared goal for both parties thereby serving as a clan control mechanism. The explicit specification of desired outcomes in the pricing plans illustrated the usage of this mechanism as a form of outcome control as well.

Social mechanisms involved frequent interactions between the client and vendor and were aimed at generating shared values while at the same time monitoring / influencing the behavior of vendor employees thus illustrating the use of both clan and behavior modes of control. This included:
- Regular meetings
- Site visits
- Business reviews
- Gifts
- Special events

Besides the use of the above mentioned client initiated control practices; vendors themselves had put in place a number of governance mechanisms. These self – controls resembled those used for intra-organizational projects but differed from them as the usage of this mode of control is often assisted and promoted by the client. The client used mechanisms to encourage the vendor to exercise better self-control (e.g., by conveying to the vendor that it valued the process certifications held by the vendor), and helped enhance the vendor’s ability to exercise better internal control (e.g., by helping to design the vendor’s performance management systems). Although the client helped the vendor design these control processes, they were not examples of behavior control. The client neither dictated the use of the processes, nor monitored the vendor’s adherence to them. This is akin to the client training the vendor in certain techniques, which has earlier been classified as self-control (Brief and Aldag 1981). Illustrative mechanisms included:

- Staff performance management
- Process audits
- Shrinkage management
- Certifications

The array of control practices available for the governance of business process outsourcing relationships has been summarized in the Table 6.1.

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Table 6.1: Control Practices in Business process outsourcing
6.4. **Transaction Attributes as Antecedents of the Control Portfolio**

A substantial correlation was found between the degree of control and the four transaction attributes viz. asset specificity (physical), asset specificity (knowledge), task programmability and output measurability thus validating the initial three hypothesis of the study. Of these output measurability had the greatest influence followed by asset specificity (knowledge) on overall control. The direction of influence for all four was positive indicating that increases in levels of these characteristics are associated with higher levels of control.

Further, fine grained analysis regarding the relationship of transaction attributes with specific control modes revealed that increases in output measurability (the ability to assess the true quality of actually delivered performance); task programmability (the ability to define ex ante the outcome that may realistically be expected to result from the transaction) and investment in physical assets specific to the relationship are positively related to increases in degree of formal control and negatively to degree of informal control. Conversely increases in relation specific knowledge assets are related negatively to formal control and positively to informal control.

These results are consistent with earlier control literature. Prior theory and evidence suggest that the use of behaviour control (formal control) is a function
of the extent to which the process that transforms inputs to outputs is understood (task programmability) (Ouchi 1979, Snell 1992). Further, Spekle (2002) states that programmable activities permit a fairly comprehensive ex ante articulation of the characteristics of the contribution that is required from the members of the organization, and therefore, control can be prescriptive or authoritative in nature, featuring rules of behaviour, specific instructions, and relatively rigid performance targets, and focusing on assuring compliance to these pre-imposed norms. Outcome measurability has also been found to have a positive relationship with outcome (formal) control (Eisenhardt 1985, Snell 1992, Kirsch 1996).

Similarly, control theory argues that clan (informal) control will be implemented when it is not possible to implement formal modes of control (Ouchi 1980). There is evidence of a negative relationship between reliance on vendor self-control and outcome measurability: as it becomes more difficult for controllers to measure whether specific targets are achieved by the controllees, they might encourage the use of vendor self-control by the controllees (Kirsch 1996). Social controls are also indicated by van der Meer-Kooistra and Vosselman (2000) for transactions characterised by low levels of task programmability and low levels of output measurability.

The research results thus, suggest that the structure of the control portfolio in terms of comparative reliance on formal or contractual governance mechanisms
as against informal or relational governance mechanisms is influenced by the
transaction attributes. An examination of the nature of outsourced business
processes reveals that the nature of the work can be broadly classified into three
categories (Aron and Singh, 2002) viz.:

1) Data Transformation: Straightforward data digitization work which are
typically routine and repetitive and thus lend themselves easily to ex ante
programming and definition of quantifiable measures of outcome
assessment. These processes are also low on strategic importance and
hence investment in knowledge assets is also low. This research analysis
would suggest an appropriate control portfolio for such processes to be
largely dependent on formal control mechanisms.

2) Customer Interface Services: In this category, the vendor employee
handles tasks with varying levels of information structuring thus
requiring differing degrees of human intervention as opposed to routines
that can be run off computerized menus. In some instances the
information worker is no more than conduit for the transfer of highly
structured and pre-determined information types (telemarketing) and at
other times s/he may use the information contained in the user firm’s
systems to decide whether or not a course of action was in consonance
with the client’s policies (Aron and Singh, 2002). Thus dependant on
the formalization of the process structure the activity would be
amenable task programmability and output measurability. Further the strategic importances of these activities also vary influencing the clients' investments in relation specific assets. Consequently portfolios of control would be structured with increasing reliance on informal control and decreasing reliance on formal control as the nature of the process involves higher levels of vendor judgment and strategic importance.

3) Expert intervention: Here vendor employees use a combination of knowledge, information, analytical skills and some sets of rules (supplied by the client) to drive outcomes for the client’s customers (Aron and Singh, 2002). Thus, these processes are characterized by higher levels of uncertainty and lower intensity of ex post information symmetry leading to higher reliance on informal or relational governance mechanisms.

The above results are diagrammatically represented here (Fig. 6.1) using an adapted version of Aron and Singh’s diagram on ‘BPO types’.

Research results of the comparative analysis conducted using the means procedure and one-way ANOVA support the model of controls across business process outsourcing types presented above.
Figure 6.1: Model of Control Portfolios by business process outsourcing type
6.5. **Degree of Control and Outsourcing Success**

The final hypothesis stated that the degree of control and partnership quality would have a positive interactive association with outsourcing success. This was tested using hierarchical regression analysis and Median Split Analysis. Results of both indicated that while degree of control has a significant positive relationship with outsourcing success neither partnership quality nor its interaction with degree of control enjoyed any relationship of significance with outsourcing success.

Control as a significant predictor of success finds empirical support from research work done on other inter-organizational settings. Henderson and Lee's (1992) study on control behaviors that can affect the performance of an I/S design teams supported the proposition that increases in the total level of control behavior is positively correlated with performance.

Results on partnership quality are however in contradiction with what is most often suggested by earlier research. Lee and Kim's (1999) study stated partnership quality was a critical success factor of IS outsourcing. Further, primarily based on social exchange theory, many researchers argue that a partnership is the ideal type of relationship, in that it will result in a higher level of success (Dibbern et al., 2004).
Support for this result however comes from Lacity and Hirschheim (1993) who revealed that the trade literature presented an inaccurate view of outsourcing arrangements. The outsourcing relationship is often portrayed as a strategic partnership or alliance. This is at odds with the actual contractual relationship, which usually does not contain provisions for sharing risks and rewards associated with outsourcing. Lacity and Hirschheim go on to state that viewing a relationship as a partnership can be dangerous because it may lead to a loose or incomplete contract, in part because the client thinks of the outsourcing vendor as a partner when in fact it is not. Consequently, the possibility for "opportunistic behavior" by the vendor exists.

Even in the Indian context explored by this study, while outsourcing clients and vendors interviewed by us referred to the outsourcing relationship variously as ‘strategic partnership’, ‘thought partnership’ ‘enterprise extensions’ and in fact most had pricing models based on ‘gain share’ agreements which reflected the benefit –risk sharing component of partnership quality; the governance of the relationship was structured around formal control mechanisms which were explicitly guided by the contract or ‘statement of work’. This reality was well brought out by the Vice President (Operations) of the largest (in terms of revenue) business process outsourcing vendor of this study who referred to the ‘Statement of Work’ (formal contract) as the “bible” guiding the relationship.
An additional insight revealed by the case study component of the research study was an initial formulation of the construction process of business process outsourcing controls. An analysis of Table X showed that a common thread that emerged was that the portfolio of control was set up in the initial stage of the relationship most often during the ‘process transition’ stage and was documented in the contract. Thereafter changes were made to this portfolio based on specific encounters. How rigorously a mechanism was enforced depended largely on the kind of relationship between the vendor and client management team at a personal level.

At the initiation of the contract execution phase during the transition of the outsourced function certain control mechanisms were factored into the service design. Some of these controls were derived from those already existent in the process as executed in the client organization. Other contributors were norms generally followed in the Indian business process outsourcing sector as mandated by the dominant players and/or Nasscom (e.g. data security norms, pricing norms etc.) and vendor developed transaction engines. Transaction engines are process modules created around a back-office function or the vertical industry process and typically a collection of standard technology applications, codified best-practice modules, domain-specific proven business
processes, and people resources that can be duplicated with minimal customization for a specific function (Simonson, E. 2002).

An initial portfolio of controls was thus created from these sources depending on the cost of execution; attributes of the outsourced function such as task programmability, output measurability and asset specificity; vendor competencies, both actual and perceived; client’s relationship management skills and cultural attributes of the outsourcing organization.

This portfolio of control was however dynamic and underwent changes as the relationship progressed. These dynamics of control find explanation in the theory of 'episodes and encounters' (Newman and Robey 1992). Processes can be viewed in terms of stable periods, called episodes, and transitional events between episodes, called encounters. Encounters can change the nature of the process from one episode to the next. For this study, episodes were periods during which control mechanisms remain stable, while encounters were "punctuations" (Newman and Robey 1992) or "critical turning points" (Heiskanen et al. 1996), which produce significant changes in the way the relationship is controlled. Such encounters are most often incidents which neither party had anticipated while signing contract but now want to prevent the reoccurrence of. For instance in the V01-C03 relationship, one of the outsourced tasks was customer 'saves' or convincing a customer calling up to terminate his account to continue the same. Initial process metrics revolved
around the save rate. However as the relationship progressed the vendor in their value creation efforts discovered that the ‘upfront save rate’ was directly proportional to the ‘long-term (90 day) retention rate’ only up to a certain point after which it was inversely proportional. Hence the metrics were changed to reflect these findings.

Other factors which affected the evolution of the control portfolio were the learning curve and the quality of the partnership. As the two sides learnt from their interactions, they reassessed the alliance and made adjustments. Changes in the best practices followed by the vendor resultant from its learning experiences with other clients also affected a business process outsourcing relationship. Further changes resulted from inter-personnel relationships developing at an individual level. As one client manager mentioned “we had to refocus on the daily reporting metrics when <name withheld> left with his core team as we didn’t know the new lot and found it hard to work on pure trust with them”.

Thus, in this study, controllers constructed the initial portfolios of control based on their initial assessments of the influencing factors. Over time, as they went through sequences of negotiation, commitment, and execution controllers were sometimes forced to modify their perceptions of the influencing factors and incorporate additional or modified controls. Figure 6.2 represents a pictorial description of this process.
6.7. **Implications for Practice**

For practicing managers, this research underscored three factors: (1) the array of control mechanisms available to govern a business process outsourcing relationship; (2) linkages between attributes of the outsourced process with the
choice of control mode and (3) degree of control as a significant predictor of outsourcing success.

The array of available control practices point to the need for clients to cultivate a broad view of control which go beyond direct, constraining control mechanisms and incorporate indirect and particularly enabling controls to instill in their provider the incentive to deliver high performance.

The influence of transaction attributes on efficacy of control modes has direct implications for the scope and content of control portfolios. Dependant on the characteristics of the outsourced process the portfolio should be largely contractual or primarily relational. Also processes which show a mix of these characteristics lend themselves to a suboptimal structuring of the control portfolio. Thus the implication is for clients to break down these processes into sub-processes to create a homogeneous set of characteristics which lend themselves to a more optimal control structuring.

There is also the indication that the process of structuring outsourcing controls should in fact be initiated while the outsource decision itself is being considered. The client needs to assess the level of task programmability and measurability of outputs of the process as well as the investment requirements in physical and knowledge assets in the outsourced condition to be able to judge the feasibility of adequately governing the process after outsourcing. Differing
control structures also point to the need for differing vendor governance skills required by the client’s outsourcing management team dependant on the outsourced process.

The process of structuring the control portfolio underscores this need for clients to pay adequate attention to establishing a rigorous control structure at the very onset of the relationship. It is also equally important to build in the flexibility to accommodate experiential learning at later stages. The contract or ‘Statement of Work’ (SOW) is of paramount importance as it is the single most definitive guide to the governance of the relationship. Thus, it is important to be precise in specifying process, performance and people related requirements, install robust post-contract monitoring mechanisms, and to build in a pricing structure which involves the vendor in sharing the benefits and risks of the relationship.

For the vendor, this study underscores the point that in-spite of all the public pronouncements on ‘strategic alliances’ and ‘close partnerships’ the ground reality of the Indian BPO sector is that it is largely transactional in nature with the relationships being that of typical buyer-supplier nature. This is emphasized by the fact that this study is focussed on the dominant players of this sector. Earlier research has suggested vendor concerns such as inflexibility and traditional measurement approaches of clients as a barrier to service innovation (Quinn, 1999). This indicates the need for vendors to encourage and educate
clients to move towards a model of increasing partnership enabled governance as a remedy to their concerns.

Another observation in the case study was that the control portfolio faced changes dependant inter-personnel relationships developing at an individual level. This indicates the business imperatives of managing attrition in the leadership level of outsourcing service providers though empirical validation of the same is called for.

6.8. **Major Research Contributions**

This paper makes some significant contributions of interest to managers who enter outsourcing relationships, and to researchers who endeavor to understand the nature of control systems associated with inter-firm relationships.

The first contribution is support for the proposition that a control theories perspective may be helpful in explaining the relative success of business process outsourcing relationships. Second, is a detailed articulation of the mechanisms used by stakeholders to implement behavior, outcome and clan controls in business process outsourcing relationships. This has remained largely unexplored till now, though work on ‘BPO Metrics’ has appeared (see for example Niranjan et al, 2007). This articulation lays an integrative
groundwork for the understanding of BPO governance and speaks to the issue of how multiple mechanisms constitute a portfolio of control modes.

Application of the transaction cost perspective unifies the diverse control portfolios found in business process outsourcing under a single explanatory scheme by showing that they are in fact expressions of the same set of explaining factors (viz. transaction attributes). Previous research has specified composition of various archetypal control structures and the links to their antecedent conditions (Spekle 2002, Langfield-smith and Smith 2003) albeit without adequate empirical grounding. The empirical component of this study fills this lacuna and adds to the growing knowledge of the design of control systems in new organizational forms. This research develops valid measures that operationalizes the concepts of formal and informal control which would aid future research.

Another contribution is a proposed theory explaining why stakeholders construct portfolios with particular control mechanisms. Though an initial formulation of the construction process of business process outsourcing controls, it is meaningful due to a complete lack of available literature on the dynamics of BPO control.

The research also provides an understanding of the critical roles played by different stakeholders to control business process outsourcing relationships
indicating a multiplicity of controllers of the relationship. Not just are the clients and vendors involved in the structure, but also end-users (through user satisfaction measurement), external quality agencies (through provision of certification) and industry bodies (through insistence on particular levels of data protection done to maintain the image of the sector).

6.9. **LIMITATIONS OF THE STUDY**

This study had important limitations that imply caution in generalizing the findings. First, this study was limited geographically to outsourcing relationships being executed in India. This may have influenced the behavior of the companies and thus the results. Further, the broader institutions of nations and their cultural and legal systems are likely to alter the effectiveness of various control mechanisms as governance devices.

Second, research indicates that control in inter-organizational relationships would differ depending on the age of the relationship. An inter-organizational relationship evolves through sequences of negotiation, commitment, and execution as successful alliances undergo cycles of learning, re-evaluation, and readjustment. As clients and vendors learn from their interactions during the course of a project, their perceptions of the factors affecting the choice of control modes and mechanisms may also change, which in turn would motivate them to change the portfolio of control modes and mechanisms. Hence, for
justifiable comparison of the structuring of control portfolios the study was limited to one-to-three year lifetime relationships. Thus, the findings may not be applicable in entirety to partnerships of longer durations.

To fully test the dynamics of the complementarities between partnership quality and control structures, relationships need to be examined over time, noting the evolving nature of the institutions that embed these relationships and the pathways they pursue in seeking high performance. Thus longitudinal data which this study lacks is another limitation.

A major constraint faced by the researcher specific to the business process outsourcing context was the stringency of data security measures. Possibility of misuse of sensitive and proprietary data coupled with lack of confidence in the Indian regulatory framework for protection of intellectual property, are major client concerns. This has prompted vendors to put in place elaborate security measures which prohibit employees from sharing information without formal permission, restricted access to internet, cell phones, email, instant messaging, removable storage units such as pen drives, laptops etc. Further fears of backlash and stakeholder concerns in the home country have made clients extremely wary of revealing their outsourcing arrangements. All relationships studied by this researcher had ‘non-disclosure agreements’ as part of the contract prohibiting the vendor from disclosing any information which would publicly identify the client. As a precondition for allowing access to personnel
and information, this researcher was asked to refer any material collected for review by the vendor’s management prior to inclusion in this study. Further, any information identifying either the vendor or the client organization was strictly prohibited.

6.10. **FUTURE SCOPE**

Avenues for future research include seeking clarity on the sufficient amount of control needed and what decides the appropriateness of a particular mechanism. Secondly, business process outsourcing relationships face a complex, dynamic environment, and the multiplicity of controllers and control modes contributes to that complexity. Future work could examine how various stakeholders structure their control portfolios to manage this complexity. Empirical grounding to the initial formulation of the control portfolio structuring suggested in this research is also called for.
6.11. **CONCLUSION**

The research objectives were to study control practices in business process outsourcing as practiced at vendor sites in India.

The study was conducted as a two step process. First, an in-depth case study of four business process outsourcing relationships was conducted to provide a basis for understanding how control is operationalized in practice. Thereafter an empirical study of the relationships between antecedent conditions, control practices, relational governance practices and success of the relationship was conducted.

The research was able to decode and describe the portfolio of controls as practiced as well as link it to existing theories on control and outsourcing thereby providing an understanding on the antecedents and structuring of the control portfolio and its impact on outsourcing success. These results make a valuable contribution to the existing knowledge in the fields of business process outsourcing and inter-organizational control and lay a strong foundation for future research.
Endnotes:


2 ref: http://www.theblackbookofoutsourcing.com/endorsements.htm