Emphasis on Accounting Controls:
Asset specificity and the use of accounting and non-accounting information within IT outsourcing engagements

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Abstract

This study observes the nature of asset specificity in different Information Technology (IT) outsourcing typologies, and investigates the relevance of accounting and non-accounting numbers in relation to these outsourcing typologies, with consideration to the findings of literatures concerning Transaction Cost Economics Theory and Social Capital Theory. It represents a response to the lack of research on relationships of IT outsourcing engagements. A case study research method is used to analyse the effect of asset specificity on the nature of relationship, and the use of accounting and non-accounting information in supporting the decision making processes of the Outsourcing Service Provider. Contrary to the findings of many researchers, the outsourcing-service provider adopted an integrative approach to its relationships as opposed to a distributive approach even in engagements that were highly asset specific, and short-term in duration. Additionally, the nature of asset specificity for IT outsourcing engagements is not static, but dynamic and in continual flux. Overall, this study suggests that large IT outsourcing-service providers value non-accounting factors in decision-making processes, in addition to accounting information, thus reflecting the Integrative Outsourcing Typology. This further validated the fact that factors advocated by Social Capital Theory such as corporate reputation, trust and collaborative interactions are crucial in IT outsourcing relationships.

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Introduction

This study observes the nature of asset specificity in Information Technology (IT) Outsourcing typologies, and evaluates the relevance of accounting and non-accounting numbers in relation to these outsourcing typologies (Figure 1). The increased importance of outsourcing has received much attention in the literature (Kohler, 2000), largely due to the fact that it remains one of the most sustained trends within business over the last couple of decades. Resources spent in developing, maintaining and upgrading in-house IT functions arguably affects the resources that firms direct towards their core activities. To avoid such sub-optimal allocation of resources, many firms resort to outsourcing their IT functions to specialist service providers, who are able to provide specialised IT services at a lower cost. IT outsourcing allows businesses to seek higher levels of efficiency and effectiveness (Ngwenyama and Bryson, 1999). Given the nature of this competitive market, successful and established outsourcing-service providers are able to provide effective services at a fraction of the in-house cost (Harris, Giunipero and Hult, 1998; Klopack, 2000).

In line with previous research, this study uses the term ‘outsourcer’ in reference to the firm that opts to outsource its internal IT function to an external party, and the term ‘outsourcing-service provider’ in reference to the specialist organisation that provides the IT outsourcing service to outsourcers.

Motivation & Contribution

This study makes a threefold contribution to the IT outsourcing literature. First, the study focuses on outsourcing-service providers rather than outsourcers. Past research has predominantly focused on outsourcers and the benefits derived and/or costs incurred from their decision to outsource (Grover et al., 1996; Harris et al., 1998; Klopack, 2000), but little research has focused on the outsourcing-service provider. A possible explanation for this lack of research is the difficulty in obtaining information from outsourcing-service providers. This study benefits from the availability of confidential information from the Commercial Director of a multinational Outsourcing-Service Provider in charge of new businesses in South East Asia, Australia and New Zealand, who has committed to contribute to this study under a confidentiality clause.

Second, while the majority of outsourcing research investigates the management of outsourcing projects, this study investigates the initial bidding stage of an outsourcing contract. How accounting and non-accounting factors play a role in assisting outsourcing service providers to either accept or reject outsourcing contracts is not sufficiently discussed in the literatures. Finally, this study investigates the possibility that asset specificity changes over time. Although asset specificity has frequently been cited as a key factor that affects the nature of outsourcing relationships (Grover et al., 1996; Roodhooft and Warlop, 1999; Arnold, 2000), little research has documented the nature of asset specificity in relation to IT outsourcing engagements. Extant literature describes certain engagements as highly asset specific, but have not analysed whether this highly asset specific nature changes over time. It is important to note that these findings are limited to large IT outsourcing engagements, and cannot be generalised to smaller outsourcing engagements of smaller or different industries without further research.

The remainder of the paper is organised as follows. A literature review and theory development of key concepts and their relationships is conducted in the next section. Subsequently, insights gained from the relationships posited are used to form propositions. Finally, the results pertaining to the propositions are discussed, with concluding comments and suggestions for further research recommended.

Literature Review & Theory Development

Klepper (1995, pp. 257) states, “in the future an effort should be made to combine elements of several theories to obtain a better understanding of the mechanisms by which partnerships evolve...” (Kern and Willcocks, 2000, pp. 323). In line with this, various theories are used to explain the rationale for the
outsourcing decision and to analyse IT outsourcing relationships. Gilley and Rasheed (2000) define an outsourcing relationship as, “an activity that is less common, representing the fundamental decision to reject the internalisation of an organisational function...a highly strategic decision that has the potential to cause ripple effects throughout the entire organisation”. This definition emphasises the fact that organisations forced to purchase products or services externally due to the absence of the option to generate them internally do not fall under the definition of outsourcing. The option to conduct that activity in-house should be present for an outsourcing organisation.

Nature of Outsourcing Relationships

A common pitfall in most industries is a poorly implemented outsourcing strategy (Klopack, 2000). Outsourcing relationships have been perceived to be similar to arm’s-length transactions on one extreme, and akin to strategic alliances on the other (Kern and Willcocks, 2000; Grover, et. al. 1996). The goal of both buyer and seller in outsourcing negotiations is to obtain the best possible outcome for their firm (Clopton, 1984). Interestingly, and paradoxically, a traditional buyer-seller relationship sees transacting parties trying to make gains at the expense of one another. From this perspective, parties transact for a short period of time and hence are focused on maximising one’s own gains from the transaction without considering the other party (Schurr and Ozanne, 1985). Grover et al., 1996 find that it is important for firms to go much further than the transient buyer-seller association in order to achieve strategic, economic and technological benefits from IT outsourcing overall, for all parties involved in the process.

An outsourcing venture may thus achieve cost savings, increased service levels and other objectives stipulated in the contract, via both parties looking beyond the traditional arm’s-length buyer-seller type relationship, and forging an increasingly cooperative and collaborative partnership operating within the ‘spirit of the contract’ (Kern and Willcocks, 2000). Collaborative engagements are at the other extreme of the relationship spectrum. An example of a collaborative alliance is a partnership. Henderson (1990) defines partnerships as “working relationships that reflect a long-term commitment, a sense of mutual cooperation, shared risks and benefits, and other qualities consistent with concepts and theories of participatory decision making”.

In a partnership the parties involved are able to achieve key organisational objectives and build competitive advantage in their respective industries (Grover et al., 1996). Good partnerships are proposed as the key for successful outsourcing engagements (Livingston, 1992; Grover et al., 1996; Arnold, 2000;). In their study, Grover et al. (1996) find a strong positive relationship between IT outsourcing success and the partnership between outsourcing service-provider and outsourcer. The paper concludes that it is imperative for firms to go much further than a buyer-seller association in order to achieve strategic, economic, and technological benefits from outsourcing. They also state that it is important to cultivate a partnership with the outsourcing-service provider at the outset of the engagement. At its best, collaborative efforts benefit from a healthy cross fertilisation of corporate cultures, skills, and resources that often lead to speedier and more effective outputs (Bello, Lohtia and Dant, 1999). Klopack (2000) supports these arguments by contending that the most effective relationships for outsourcing parties are long-term partnerships, because building strategic relationships takes time and investment and changing those relationships can be difficult and costly. A short-term focus places stress on the outsourcing-service provider, resulting in poor performance because of inadequate time for the service provider to adjust to demand swings, to learn operation expectations and to establish a performance history (Klopack, 2000). Opportunism is a key behavioural assumption that drives transaction cost economic analysis (Meer-Kooistra and Vosselman, 2000). This concept refers to situations where entities behave in a manner that maximises their own perceived outcomes at the expense of others. Decision-makers are expected to act in the best interests of the entities they represent. However, under the umbrella of opportunism, the focus is on cost minimisation and profit maximisation at the expense of the other party in the engagement. Therefore, the decisions they make in determining the best direction for their respective entities are based on mainly available accounting information. Opportunistic behaviour is intensified in outsourcing relationships that are asset specific (Lonsdale, 2001). Asset specificity is discussed in the next section.

Outsourcing Typology

An integrative-distributive outsourcing typology is proposed in describing the nature of outsourcing relationships (Grover et al., 1996). This is a behavioural typology sourced from the Network/Interaction Industrial Marketing Theory investigating organisational motivations for inter-organisational interaction. This theory models the behavioural aspect of buyer-seller interactions along two principal dimensions (Schurr and Ozanne, 1985). First of the two typologies is the integrative-outsourcing typology. Extant literature associates higher levels of trust with the integrative interaction typology and lower trust levels with the distributive
interaction typology (Schurr and Ozanne, 1985; Grover et al., 1996). Integrative relationships are characterised by cooperative behaviour directed towards finding methods of satisfying the objectives of both the buyer and seller (in this case, the outsourcing-service provider and outsourcer) (Grover et al., 1996). These relationships rely on factors like trust and openness in extended buyer and supplier dyadic exchange relationships (Lonsdale, 2001). Here, the parties involved give more importance to the factors like the reputation and the trustworthiness of their respective partner(s). Due to the fact that they are formed with a view of achieving mutual goals, integrative relationships form the base for relationships that are long-term in nature (Grover et al., 1996). The network/interaction theory emphasises the importance of forming long-term engagements to establish a smooth working relationship (Grover et al., 1996). With regards to long-term relationships, McKenna (1985) states that it is necessary to “gain understanding of the market structure, then develop strategic relationships with other key companies and people in the markets. They must build relationships with suppliers and distributors, investors and customers. Change in the market can alter prices and technologies, but close relationships can last a lifetime, if not longer” (as quoted in Grover et al., 1996). The strong relationship between partnership and IT outsourcing success as observed by Grover et al. (1996) indicates that fostering a long-term integrative relationship based on social capital factors is critical to achieving the greatest benefits from outsourcing.

The second of the two extremities is the distributive-outsourcing typology. Distributive relationships are characterised by parties being mainly concerned with their self-gain, even at the expense of the other party (Schurr and Ozanne, 1985; Grover et al., 1996). The main factors that are focused on in these relationships are cost and profitability. These relationships are usually short term in nature. A prudent deduction from the aforementioned arguments would see outsourcers and outsourcing-service providers being more concerned with the cost factors when dealing with highly specific outsourcing activities. Hence, it would be safe to conclude that the decisions made with respect to highly specific outsourcing activities will predominantly rely on As the accounting system is able to measure this risk, it is considered important. Although, accounting numbers are important and used in virtually all pre-contractual business evaluations, it is posited that evaluations that solely rely on accounting numbers are mainly concerned with the costs factors associated with the potential engagement and profitability of the potential alliance partner. Hence, parties tend to work in a competitive fashion where they are opportunistically trying to maximise their share of the profits from the engagement at the expense of the partner. As mentioned earlier, this mannerism is reflective of the distributive typology of outsourcing relationships.

Asset Specificity

Transaction cost economics emphasises the importance of asset specificity in considering outsourcing decisions (Grover et al., 1996; Roodhooft and Warlop, 1999; Arnold, 2000). Asset specificity is defined as being “the extent to which the investments made to support a particular transaction have a higher value to that transaction than it would have if they were redeployed for any other purpose (McGuinness, 1994 as quoted by Lonsdale, 2001). Asset specificity refers to the uniqueness of the product or service exchanged between the two parties involved in the outsourcing engagement (Grover et al., 1996) and this includes physical asset specificity, human capital specificity and site specificity (Aubert et al., 1996; Arnold, 2000). Physical assets consist of the apparatus required for the transaction completion, human capital specificity represents the learning and the knowledge parties need to acquire to participate in the exchange, and site specificity refers to the need for a party to be physically located near the other party to participate in the transaction. An outsourcing activity that is highly asset specific sees the outsourcing-service provider incurring additional costs in providing services to the outsourcer. The increase in cost is attributable to the fact that goods and services provided by the outsourcing-service provider are customised and are not readily transferable or useable in other transactions without huge additional costs (Grover et al., 1996; Arnold, 2000). In such cases, the service provider does not benefit from the usual economies of scale received from low asset specific outsourcing relationships. Maintaining low charge-out rates becomes a strain on the service provider because only activities with low specificity enable the service providers to bundle demand and exploit economies of scale (Arnold, 2000). Due to the uniqueness of a highly specific activity, the outsourcing-service provider needs to invest more in the provision of goods and services. Therefore, the additional costs incurred are passed on to the outsourcer in the form of higher service fees. Grover et al. (1996) found that the asset-specific nature of many application projects could increase coordination costs significantly, reducing economies of scale and scope for the outsourcing-service provider, thereby making it difficult to realise the strategic, economic and technological benefits from outsourcing. Arnold (2000) states that it is sensible to avoid outsourcing highly specific activities by conducting them internally, in order to avoid extremely high market transaction costs.

Roodhooft and Warlop (1999) found outsourcers to be more reluctant to enter an outsourcing contract that involved high asset specific investments due to imminent cost issues. The high asset specificity of an outsourcing activity demands substantial amounts of investment by the outsourcer at the outset of the
relationship and are forced to incur these costs if conducting the activity in-house is more expensive. This initial outlay is treated as a sunk cost. If an outsourcing firm decides to terminate the activity with one outsourcing-service provider and pursue a new outsourcing contract with another, the initial investment would have to be written-off and incurred again in the wake of the new relationship. Outsourcers generally try to avoid the termination of a highly asset specific activity. This hesitance can result in post-contractual dependency where the outsourcers are locked in the relationship to their service provider to avoid the additional costs involved in seeking a different service provider for the activity (Lonsdale, 2001). The arguments presented above suggest that the outsourcing of a highly specific activity cause a perceived disadvantage rather than an advantage to the parties involved and hence is regarded unfavourably.

Due to the divergence in profit motives and the presence of factors like opportunism in a highly asset specific engagement, Kole (1983) emphasises the importance of hard contractual relationships (as quoted in Grover et al., 1996). Ellram and Billington (2001) also emphasise the importance of contracts in governing relationships.

Bidding & Negotiating

A phase of contracting that is critical to the success of the endeavour is the bidding process (Nam, et al. 1995). The selection of an appropriate outsourcing-service provider is also an important step in outsourcing that involves various issues. There are various service providers in the outsourcing marketplace, each possessing different strategies and service offerings. This creates an increasingly competitive environment amongst outsourcing-service providers who constantly bid and negotiate to win outsourcing contracts. Firms attempt to employ effective bidding and negotiating strategies because the outsourcer is in a position to take advantage of the competition amongst outsourcing-service providers (Nam, et al. 1995). It is usually the norm for outsourcing-service providers to have asymmetric expertise and cost structures. This is the by-product of one service provider possessing more information and expertise about the outsourcer than other service providers (Nam et al., 1995). Therefore, the process of contracting between entities will also involve costs. These cost are caused by information asymmetry, bounded rationality and opportunism (Arnold, 2000). Nam et al. (1995) found that a policy of giving incentives in the form of subsidies and forcing penalties in the form of discriminatory policies on to outsourcing-service providers allows an outsourcer to reduce contracting costs. They conclude that truth revelation strategies generally do better than and always at least as well as the blind strategy of picking the lowest bid.

Nevertheless, there is a degree of uncertainty and risk that even a well-drafted contract cannot mitigate (Nam et al., 1995). To minimise these risks, the outsourcing-service provider and the outsourcer must be aware of both, the benefits and risks of outsourcing and the specific factors that could lead to conflict (Vining and Globerman, 1998). To address these issues that arise during the process of contracting, the parties involved seek information regarding their prospective partners to assist them in the bargaining and contracting process. The findings of Nam et al. (1995) highlight the fact that it is important for an outsourcing-service provider to be equipped with as much information as possible about the outsourcer to gain a competitive advantage in the bidding and negotiation processes. They may rely on two different types of information which are quantitative criteria based on accounting numbers and/or qualitative criteria based on intangible factors (Agarwal, Tanniru and Dacruz, 1992).

The literature has documented the importance of accounting information to decision making. This study however, explores the role of accounting and non-accounting information in the decision-making processes of IT outsourcing-service providers and observes the changes to the role of accounting and non-accounting information in decision making in the presence of certain factors believed to influence the nature of IT outsourcing relationships. The two information types are analysed in the following section.

Types of Information

A strong assumption of classical economic theory is that information is constant in availability for decision-makers and that transacting parties possess the ability to measure the value of the elements exchanged. In outsourcing however, this is often proven false due to the existence of uncertainty measurement problems (Aubert, Rivard and Patry, 1996). ‘Uncertainty’ refers to the lack of information measurement ability and is observed through the difficulties encountered in the evaluation of an element of exchange (Aubert et al., 1996). Agarwal et al. (1992) state that of particular salience to the problem of project selection decision is the consideration of both the quantitative and qualitative aspects of the project. With regards to outsourcing-service providers, each outsourcing engagement is treated as an individual project, and as mentioned earlier, it is important for them to equip themselves with as much information about the outsourcer as possible. More information enables them to structure more competitive bids for outsourcing projects (Agarwal et al., 1992; Nam et al., 1995; Aubert et al., 1996).
The information relied upon in decision-making may be quantitative or qualitative in nature. Quantitative information refers to mainly accounting data (Nguyen and Leblanc, 2001). Qualitative information refers to other factors such as trust and corporate reputation that are affected by mediums like advertising and word-of-mouth (Nguyen and Leblanc, 2001).

**Accounting Information**

Past research has found that disclosure of accounting data is valuable in bargaining situations because it informs bargainers about the other party’s position thus reducing costly conflict (Luft, Haka and Ballou, 1998). Properties of accounting information can increase or decrease the uncertainty associated with accounting-based payoffs (Haka, Luft and Ballou, 2000). In evaluating possible business relationships, transacting organisations rely on accounting information to ascertain the risk associated with the venture. The information content present in the accounting numbers assists these parties to avoid or limit each other’s exposure to high risk (Luft et al., 1998; Agarwal et al., 2000; Haka et al., 2000). It is posited that uncertainties in the accounting system offer opportunities for bargainers to act strategically (Luft et al., 1998). Therefore, the higher the risk associated to a transaction, the higher the reliance of transacting parties on accounting information.

Notwithstanding the aforementioned, it is important to note that decision-makers cannot rely solely on quantitative accounting information to assist them in their decision-making processes. This view sources from the Social Capital Theory (Ireland, Hitt and Vaidyanath, 2002). Typically, in a situation where all aspects of a system are considered simultaneously, there can be a tendency for decision-makers to weigh the quantitative or concrete criteria more heavily than qualitative and abstract criteria (Agarwal et al., 1992), simply due to the objectiveness of measurement. A possible consequence of such biased decisions is that prospective outsourcing projects are judged merely on the financial merit of the outsourcer rather various intangible factors that are not reflected in the financial statements. Qualitative information plays a vital role in decision-making processes associated with outsourcing engagements.

**Non - Accounting Information**

Social Capital Theory refers to organisational relationships where other important resources are also strongly considered in addition to accounting numbers (Ireland et al., 2002). These resources mostly refer to non-accounting factors that can be acquired from information sources such as advertising, firm trustworthiness and reputation (Nguyen and Leblanc, 2001). Decision-makers have a perception about their prospective partners and rely on those perceptions to form their decisions (Ireland et al., 2002). Many outsourcing-service providers do not just restrict themselves to the mere provision of services for their clients, but also take on a certain degree of risk, which is shared with the outsourcers (Gilley and Rasheed, 2000; Meer-Kooistra and Vosselman, 2000; Langfield-Smith and Smith, 2001).

The two key attributes of Social Capital Theory are Corporate Reputation and Trust (Nguyen and Leblanc, 2001; Ireland et al., 2002). Based on this theory, reciprocal trust and cooperation are perceived as mitigating factors of mere legal or financial types of control. Corporate reputation has received increased attention in strategic management literatures, as it is perceived to be an intangible resource providing sustained competitive advantage to organisations (Deephouse, 2000). Viewed as a mirror of a firm’s history (Nguyen and Leblanc, 2001), corporate reputation is formed as a process that accumulates the judgements of the various groups who interact with the firm over time (Milewicz, 1993). A firm’s reputation is constructed through its credible actions (Nguyen and Leblanc, 2001). Credibility is determined by contrasting what a firm says it will do and what it actually does (Nguyen and Leblanc, 2001). Therefore, a firm with a high-perceived credibility enjoys a favourable reputation, unlike a firm with low-perceived credibility. Good corporate reputations have been found to be very important in establishing and maintaining loyal relationships (Robertson, 1993 and Nguyen and Leblanc, 2001), subsequently allowing for lower costs (Deephouse, 2000).

Trust is believed to be an important element in the formation of alliances. The presence of trust creates the optimal basis for a mutually beneficial relationship (Carayannis, Sulaiman and Radosевич, 2000). Trust is a variable that can be brought into play by parties taking the right actions and it may stem from previous contractual relationships between the parties or grow during a certain transactional relationship (Meer-Kooistra and Vosselman, 2000). The presence of trust between cooperating parties is especially important in situations characterised by uncertainty and strong dependencies between parties owing to specific investments (Meer-Kooistra and Vosselman, 2000), as it leads to constructive dialogue and cooperative problem solving (Pruitt, 1981 as quoted in Schurr and Ozanne, 1985). As stated in Luft et al. (1998), accounting numbers have the potential to cause uncertainty, thus creating a higher probability for the implementation of poor decisions...
by decision-makers. Therefore, the presence of non-accounting factors are seen as a complement to accounting information.

Research Propositions

The first and second propositions explore the alignment of asset specificity of outsourcing engagements with the two extreme relationship typologies of outsourcing. These propositions seek to establish the connection between asset specificity and the outsourcing typologies as suggested by Transaction Cost and Network/Interaction Theories. Asset specificity has been cited as one of the most important factors to be considered before parties venture into outsourcing engagements (Aubert et al., 1996; Arnold, 2000). High asset specific outsourcing activities make it difficult for service providers to maintain low costs. The absence of economies of scale escalates the investment outlay of the service provider to operationalise the outsourced activity. Due to the fact that it is important for service providers to ensure a profitable result from the outsourcing engagement (like any other profit-making organisation), the additional investments made are transferred onto the outsourcers in the form of service fees. Aware of this, the outsourcer also tries to minimise losses by seeking the service provider capable of charging the lowest fees. This creates a setting where both parties are focused on costs associated to the project. Each party tries to make opportunistic gains at the expense of the other. This circumstance makes it very difficult for the outsourcer and the outsourcing-service provider to work as a partnership and attain mutual goals. Rather, the parties involved are more likely to transact at arm’s-length, akin to buyer-seller relationships where each party is only concerned about its own interests. There is very little room for the factors advocated by the Social Capital Theory to exist here. Based on the Network/Interaction Theory, such opportunism-induced characteristics are indicative of the Distributive Outsourcing Typology. Therefore, the first proposition suggests that High Asset Specificity IT outsourcing engagements will reflect the Distributive Outsourcing Typology.

P1: High Asset Specific IT outsourcing engagements reflect the Distributive Outsourcing Typology.

The second proposition associates Low Asset Specificity IT outsourcing engagements with the Integrative Outsourcing Typology. Based on arguments similar to those discussed earlier, a low asset specific activity reduces the pressure to maintain low costs for both the parties involved in the outsourcing engagement. This is attributed to the fact that outsourcing-service providers can replicate the services provided for low asset specificity activities and benefit from economies of scale because large numbers of clients have similar requirements. The reduced costs attributed to low asset specific activities are passed on as cost savings onto the outsourcer. In such circumstances, the parties are more likely to pursue partnership-type strategies where both, outsourcing-service provider and outsourcer work together towards achieving mutual goals. Although the economic consequence of the transaction is always the primary focus for any business dealing, factors like trust and corporate reputation in line with the Social Capital Theory are expected to play a more important role in a partnership as opposed to an arm’s-length relationship. Therefore, as suggested by Network/Interactions Theory, Low Asset Specific IT outsourcing engagements can be aligned with the Integrative Outsourcing Typology. Hence, the second proposition:

P2: Low Asset Specific IT outsourcing engagements reflect the Integrative Outsourcing Typology.

The third and fourth propositions explore the alignment of the duration of outsourcing engagements to the two extreme outsourcing typologies. In accordance with the Network/Interaction theory, these propositions connect the perceived length of a project to one of the outsourcing typologies. Long-term interactions are formed with a focus on working together for a prolonged period of time. To sustain successful operations throughout a long-term commitment, past research has emphasised the importance of considering non-qualitative factors in addition to quantitative accounting factors. The greater duration of a long-term engagement causes an increase in the uncertainty associated to the project. As mentioned before, during the contracting phase, it is unrealistic to expect the parties involved to foresee all possible problems that could arise in the future. Moreover, an attempt to incorporate all possible issues that could arise in the future at the contracting stage would employ a lot of resources into research about the parties involved and their respective industries. These factors will cause the contracting costs associated with the outsourcing project to escalate. To avoid incurring the additional costs during the contracting stage, parties opt to implement flexible contracts (Nam et al. 1995). These contracts provide for making changes to the terms and conditions of the contract in the future with the consent of the parties involved. Proponents of the Social Capital Theory contend that such contracts require the presence of trust. The outsourcing-service provider would have to place a degree of trust on the outsourcer, vice versa, for them to commit to a flexible contract. In this case, to a degree, each party assumes that the other would not act deviously or abuse the trust. This assumption is in line with the Integrative Typology. It suggests that the outsourcing-service provider is not only focused on the profits derivable from the outsourcer, but also the long-term sustainability of their engagement, which
demands the presence of trust. Hence, the outsourcing-service provider is expected to act based on perceived
totality of the outsourcer. Behaviours like opportunism are not expected to be present. The interacting
are expected to work towards attaining mutual goals. Therefore, the third proposition suggests:

**P3:** Outsourcing service providers consider non-accounting factors in evaluating the decision to
accept an Integrative outsourcing contract.

The fourth proposition associates the use of accounting numbers with the Distributive Outsourcing Typology.
Distributive engagements are predominantly of a short duration and engaging parties are expected to be
focused on making quick gains within a limited time frame. Unlike long-term engagements, parties in short-
term engagements to an extent are able to anticipate problems that may arise in the future, at the initial
contracting stage. Provisions are included in the contract to control for undesired developments in the future.
Like most business ventures, IT outsourcing engagements require investments at the outset and parties expect
to receive returns on invested amounts within the course of the engagement. In short-term engagements, the
time frame within which the outsourcing-service provider and the outsourcer can receive their returns is
small. As a result, they are expected to focus solely on quantitative data and accounting numbers. Accounting
information assists decision-makers in calculating the level of risk associated to an outsourcing project.
Hence, factors advocated by Social Capital Theory are not as prevalent in a short-term outsourcing
relationship as compared to a long-term outsourcing relationship. Opportunistic behaviour is also expected to
be more rampant in these relationships as the parties are driven by the short time frame to make quick gains.
In line with suggestion of Network/Interaction Theory, such engagements would be described as being akin to
the Distributive Outsourcing Typology. Therefore, the fourth proposition suggests:

**P4:** Outsourcing service providers consider accounting numbers in evaluating the decision to
accept a Distributive outsourcing contract.

The fifth and sixth propositions focus on outsourcing engagements after the outsourcing-service provider and
outsourcer have formed the relationship, thus exploring the post contractual nature of IT outsourcing
engagements. Past literature has consistently categorised outsourcing activities as high asset specificity and
low asset specificity. The literature suggests that the level of asset specificity has to do with the complexity
and the uniqueness of the outsourced activity. A highly asset specific activity is unique in nature and thus
requires additional investments by the outsourcing-service provider. Moreover, the uniqueness of the activity
does not allow the outsourcing-service provider to apply the same resources to other outsourcers. As a result,
the outsourcing-service provider is deprived of the opportunity to exploit the economies of scale that is
usually present with low asset specificity outsourcing projects. However, nothing to the knowledge of the
author has been documented in IT outsourcing literature about the nature of asset specific projects. It is
assumed that the asset specificity of an outsourcing project remains static throughout the duration of the
engagement. As an extension to the main frame of research in this study, the nature of highly asset specific
relationships overtime is also analysed. This study posits that, due to an exposure to the uniqueness of a new
engagement, outsourcing-service providers are initially required to outlay large investments that render the
engagement as highly asset specific, but this situation reverses once the outsourcing engagement is in
operation. This view is based on the findings that IT outsourcing-service providers are technologically more
superior and hence given time, would be able to devise a cheaper alternative to conducting the outsourced
activity at high costs. If supported, this would imply that high asset specific outsourcing engagements could
possibly reduce in specificity over time, due to the competence of the outsourcing-service provider. By
tapping into technological developments to lower investments in a project, the outsourcing-service provider is
expected to move high asset specific projects towards lower specificity. Therefore, the fifth proposition
suggests that the nature of Highly Asset Specific outsourcing relationships are not static and can change over
the course of familiarisation between the two parties.

**P5:** The nature of Highly Asset Specific outsourcing relationships is not static.

The final proposition aims to test whether in the long-term, all IT outsourcing relationships will progress
towards the Integrative Outsourcing Typology. The rationale behind this suggestion is that over the course of
a prolonged time frame, i.e. in a long-term engagement, the transacting parties would be able to minimise
costs efficiently and build a strong relationship based on the factors advocated by Social Capital Theory.
Therefore, the sixth proposition suggests that in the long-term, all IT outsourcing relationships will reflect the
Integrative Outsourcing Typology irrespective of the nature of the relationship at the outset of the
engagement.

**P6:** In the long-term, IT outsourcing relationships will progress towards the Integrative
Outsourcing Typology.
Research Method

This study was conducted in the format of a single exploratory case study. Yin (1989) defines a case study as, “an empirical enquiry that investigates a contemporary phenomenon within its real life context when the boundaries between the phenomenon and its context are unclear, and where multiple sources of evidence are used”. A case study is the favoured method of research for studies that need to make sure that the phenomena explored is not divorced from its context (Brownell, 1995), and its unique strength is the ability to deal with a full variety of evidence – documents, artefacts, interviews, and observations (Yin, 1989). Case studies enjoy a comparative advantage over experimental research because of the premium focus placed on intimate appreciation of the context of the phenomena (Brownell, 1995). Otley and Berry (1994) state, “the case study provides a vehicle by which theories can be generated and modified in the light of data”. Case studies are said to be particularly valuable where existing theories are inadequate or incomplete. This applies to the IT outsourcing literature because as is widely accepted by most researchers, the IT outsourcing literature is not well developed (Hendry, 1995; Grover et al., 1996; Willcocks et al., 1999; Kern and Willcocks, 2000). These factors justify the case study approach used to conduct this study. Schramm (1977) provides support to this study’s choice of research design by referring to case studies as a strategy that “tries to illuminate a decision or set of decisions: why they were taken, how they were implemented, and with what results” (Yin, 1989). This study also explores the decision-making processes of an IT outsourcing-service provider. Therefore, Schramm’s explanation further affirms the appropriateness this study’s design to the research issue.

Respondents

The identities of the outsourcing-service provider and the respondents are kept confidential in line with the confidentiality stipulation agreed at the outset of conducting this study. Therefore, extreme care has been taken in describing the outsourcing-service provider (OSP). In the same vein, the Director participating in the interviews is referred to as Mr. X. OSP is a global services company providing strategy, implementation and hosting for clients managing the business and technological complexities of the digital economy. OSP provides consulting through to business process management and develops business solutions from concept to implementation and operation. The products and services offered through this line of business enable manufacturers to digitise their product lifecycles as a way to increase margins and grow revenues. OSP is one of the largest, best equipped and most advanced information technology services organisations in Australia and the Asia Pacific.

As the Commercial Director of OSP, Mr. X is in charge of businesses for South East Asia, Australia and New Zealand. He leads a team that engages in all new business pursuits across South East Asia, Australia and New Zealand. This team is responsible for handling the financial diligence on new contracts, getting involved in the negotiations of outsourcing contracts, and the structuring of deals. Apart from the long-term outsourcing contracts, this group also manages other operations such as divestitures and acquisitions. The team is used to solve specific problems on specific accounts and clients. The team also is in charge of renegotiating contracts that are under performing. Mr. X is the primary source of information for this study. The two managers who participated in the surveys to corroborate or contradict the information provided by Mr. X are also high-ranking personnel of the organisation. The first is the Commercial Manager South East Asia. The second is the Commercial Manager of Australia and New Zealand. These respondents are managers of sub-groups that are part of Mr. X’s group.

Within the organisation, responses were obtained from three key individuals. The first was a series of interviews with Mr. X. The second stage of data collection was the questioning of Mr. X’s two senior operational managers via a survey, to gauge their perceptions of the relationships discussed and investigate their consistency with Mr. X’s responses.

Interviews are one of the most important sources of case study information (Yin, 1989). Through interviews, well-informed respondents are in a position to provide important insights into a situation. In this study, the key respondent, Mr. X, was interviewed with mostly open-ended questions. It would be more appropriate to refer to Mr. X as the key informant rather than key respondent. This is because in answering the questions, Mr. X proposed his own insights into certain occurrences that were then used to make further inquiries. Such informants are critical to the success of a case study (Yin, 1989). However, extreme care was exercised in structuring the questions that were to be asked in the interview. In addition, a survey was carried out to increase the rigour of this study. The survey method is discussed in the next section.

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1 Here after, the outsourcing-service provider is referred to as OSP.
The survey was conducted to increase the reliability of the findings in this study. The questionnaires were answered by two managers in the organisation. A survey method is advantageous when the research goal is to describe the incidence or prevalence of a phenomenon or when it is predictive about certain outcomes (Brownell, 1995). Given this, it was opined that the use of a survey approach to complement the case approach reinforced the results obtained. The questionnaires were designed with a focus on individual outsourcing engagements that the managers have been in charge of. The rationale for this was to analyse how well the answers provided by Mr. X reflected the outsourcing engagements of the outsourcing-service provider and also to seek the viewpoint of the actual managers of the outsourcing engagements. Most questions required answers over a 7-point Likert scale. The reason for selecting a 7-point Likert scale as opposed to the usual 5-point scale was to allow more variance in the results. A larger scale provides for more effective incremental observations. It is important to note, however, that both the case study and survey methods of research can be disadvantageous if not conducted properly. These pitfalls relate to biases during the interview process and the inappropriate or inaccurate completion of surveys by respondents. Notwithstanding this, it is noted that measures were taken in the administration of the interviews and surveys in this study to minimise the lack of reliability of data from the respondents.

First, a consistent interpretation of the responses from the interviews and survey was facilitated via the use of simple instructions and questions that were worded to minimise difficulties associated with respondent interpretation. The respondents were high-level personnel who possess complete knowledge of the different activities and procedures within the organisation. Second, use of an alternate source of information (survey questionnaires), allowed a broader range of historical, attitudinal, and observational issues to be addressed. Most important is the development of converging lines of inquiry that allows any finding or conclusion in this case study to be much more convincing and accurate as it is based on different sources of information (Yin, 1989). Third, a case study database was created in to ensure that all the sources of information that assisted in the deduction of results in this study were preserved. This prevents the researcher from resorting to making false claims that are unfounded. The presence of a database in the form of notes, study documents, tabular materials, narratives, and tape recordings as evidence further authenticates the results and findings of this study (Yin, 1989).

Results

The first proposition attempts to relate highly assets specific IT outsourcing engagements to the Distributive Outsourcing Typology. The interviews conducted with Mr. X revealed that although the financial position of the outsourcer was important, OSP also focused on non-accounting qualitative factors advocated by the Social Capital Theory. The following statement suggests this: “We prefer large clients; enterprise clients who have market leadership or a significant base of operation; we target the top 200 corporations in Australia...size is an important factor.” This statement shows that corporate reputation is an important factor influencing OSP’s decision making with regards to outsourcing engagements. Moreover, Mr. X revealed that OSP shares the risks attributable to the outsourcing project with the outsourcer: “We prefer all of IT; so we like to take-over the whole environment and manage the whole thing for the client (complete outsourcing), which will include hardware, software, people and all future application development requirements.”

When the outsourcing-service provider takes over the whole of the environment for the client, there is a high degree of risk that it shares with the outsourcer. An organisation that bears a degree of risk along with its partner(s) characterises the Integrative Outsourcing Typology. Moreover, the following statement provided conclusive evidence that OSP’s relationships with its highly asset specific outsourcing engagements are reflective of the Integrative Outsourcing Typology: “We basically transfer any of the people who are in the in-house operation of the outsourcer into our organisation. Then, part of the process is to train them in the methodology of our organisation. We give them access to our experience and database and bring them up to speed with the operations. They then become resources that we can use on other accounts that we are going to win.” This statement suggests that OSP maintains a collaborative relationship with its outsourcing partners. Mr. X stated that OSP gives its clients’ staff access to its database and also to details of its key operations. This evidently indicates OSP’s openness towards its clients and also affirms its willingness to work towards attaining mutual goals. The results from the interview thus do not support Proposition 1.

As mentioned before, surveys were conducted to corroborate or contradict the information obtained from the interviews. The survey data were separated into two groups. The first comprised high asset specific engagements and the second, low asset specific engagements. The questions were structured to observe the factors that influenced the decisions of the outsourcing-service provider at the bidding, negotiation and management stages of specific outsourcing engagements. These results were collected from the two managers to increase the variety of the data sample and to collect evidence that either corroborates or contradicts the answers from Mr. X.
With respect to Proposition 1, the data obtained from the survey supported the results from the interview. Tables 1, 2 and 3 (see Appendix A), show the factors taken into consideration during the three stages with highly asset specific engagements and the evidence suggest that the relationships this IT outsourcing-service provider with its highly asset specific outsourcing engagements do not reflect the Distributive Outsourcing Typology.

The mean values for the non-accounting factors during the Bidding Stage (Corporate Reputation and Previous Typology. provider with its highly asset specific outsourcing engagements do not reflect the Distributive Outsourcing Typology.

The mean values for the non-accounting factors during the Bidding Stage (Corporate Reputation and Previous Dealings) showed significant results. On a scale of 1 (Not Important) to 7 (Very Important), the Corporate Reputation variable had a mean of 5 and the Previous Dealings variable had a mean of 4.57, both above point 4 (Moderately Variable). This suggests that non-accounting factors were considered important at the bidding stage of outsourcing engagements. The mean values for the non-accounting factors during the Negotiation Stage (Corporate Reputation, Previous Dealings, and Forging Long Term Relationships) also showed significant results. On a scale of 1 (Not Important) to 7 (Very Important), the Corporate Reputation variable had a mean of 4.86, the Previous Dealings variable had a mean of 4.57 and the Forging Long Term Relationships variable had a mean of 6.29. Again, the three variables had values above point 4 (Moderately Variable). This suggests that non-accounting factors were also considered important during the negotiation stage of outsourcing engagements. The mean values for the non-accounting factors during the Management Stage (Forging Long Term Relationships, Attaining Mutual Goals and Providing Saving to the Outsourcer) also unanimously show figures that are significantly above the Moderately Important point. The Forging Long Term Relationships variable had a mean of 6.71, the Attaining Mutual Goals variable had a mean of 6.58 and finally, the Providing Savings to the Outsourcer variable had a mean of 6.58.

Together, the importance of non-accounting factors in the three stages strongly supported the opinions of Mr. X. The importance shown for these non-accounting factors suggests that the relationships maintained by OSP with its highly asset specific outsourcing engagements were reflective of the Integrative rather than the Distributive Outsourcing Typology. Hence, Proposition 1 was not supported. It is important to note that the mean values for accounting factors were also above the Moderately Important level, indicating that accounting factors are significant regardless of the role of non-accounting factors.

The second proposition relates low assets specific IT outsourcing engagements to the Integrative Outsourcing Typology. This proposition follows the argument that, when an outsourcing engagement is of low asset specificity, the outsourcing-service provider does not place too much of a focus on accounting numbers, as there is no high initial investments involved. Hence, the outsourcing-service provider was expected to place more emphasis on non-accounting factors in low asset specific engagements as opposed to high asset specific engagements. The answers given by Mr. X support this proposition. Mr. X claims the following: “We are certainly more relaxed when dealing with clients from industries that we have the expertise in simply because we know the investment required is not much, although there is still the focus on the Top firms in the industry, and the similar services apply.” This suggests that as expected, OSP considers factors advocated by Social Capital Theory with low asset specific engagements. It also suggests that OSP maintains similar standards of service to both types of outsourcing engagements. These findings support Proposition 2. To ensure that these deductions from the interview are accurate, the data from the survey is analysed. Here, the data set representing all low asset specificity engagements is observed.

The evidence provided in Tables 4, 5 and 6 (not shown in this paper), show the factors taken into consideration during the three stages with low asset specific engagements and the evidence suggest that outsourcing engagements that are highly asset specific result in the firms behaving in a manner that reflects the Integrative Outsourcing Typology.

The mean values for the non-accounting factors during the Bidding Stage (Corporate Reputation and Previous Dealings) supported Proposition 2. On a scale of 1 (Not Important) to 7 (Very Important), the Corporate Reputation variable had a mean of 5.11 and the Previous Dealings variable had a mean of 5.78, both above point 4 (Moderately Variable). This suggests that non-accounting factors were considered important at the bidding stage of outsourcing engagements.

The mean values for the non-accounting factors during the Negotiation Stage (Corporate Reputation, Previous Dealings, and Forging Long Term Relationships) also showed significant results. On a scale of 1 (Not Important) to 7 (Very Important), the Corporate Reputation variable had a mean of 4.67, the Previous Dealings variable had a mean of 5.11 and the Forging Long Term Relationships variable had a mean of 6.29. Again, the three variables had values above point 4 (Moderately Variable). These results suggest that non-accounting factors were also considered important during the negotiation stage of outsourcing engagements.

The mean values for the non-accounting factors during the Management Stage (Forging Long Term Relationships, Attaining Mutual Goals and Providing Saving to the Outsourcer) also unanimously show
figures that are significantly above the Moderately Important point. The Forging Long Term Relationships variable had a mean of 6.67, the Attaining Mutual Goals variable had a mean of 6.78 and finally, the Providing Savings to the Outsourcer variable had a mean of 7.

Together, the importance of non-accounting factors in the three stages strongly support the answers from Mr. X. The importance shown for these non-accounting factors suggests that the relationships maintained by OSP with its low asset specific outsourcing engagements were reflective of the Integrative Outsourcing Typology as expected. Confirming a concept introduced earlier in this study, accounting factors never lose their importance as is reflected by high mean figures for certain accounting factors as is shown in Tables 4, 5 and 6. Nevertheless, the significance of non-accounting factors suggests that the relationships maintained by OSP with its low asset specific outsourcing engagements are also reflective of the Integrative Outsourcing Typology as was proposed in the second proposition. Therefore, the evidence obtained supports Proposition 2.

The third proposition relates long-term IT outsourcing engagements to the Integrative Outsourcing Typology. In this proposition, the argument is based on the notion that in a long-term engagement, the parties involved are aware of the prolonged commitment and see the importance of focusing on factors that can ensure a successful engagement. Thus, the outsourcing-service provider is expected to strongly consider non-accounting factors advocated by the Social Capital Theory in addition to accounting factors. The interviews with Mr. X provide evidence supporting these claims. Mr. X claims the following: “The IT outsourcing contract that our organisation prefers is long term. This is because of the governance and monitoring that are required in contracts. Governance increases the overheads for a contract, so we prefer long-term contracts to ensure that clients will take a relationship based approach and you have more time to recover initial investments. That way, you can give savings to the client as well.” From this statement, it is evident that the outsourcing-service provider gives importance to fostering long-term relationships with its clients in which both parties will interact in a collaborative fashion. The focus on factors advocated by the Social Capital Theory for long-term outsourcing engagements is therefore significant. These findings support Proposition 3. Again, to ensure that the deductions from the interview were accurate, the survey data was analysed. As was done with the sample to observe the effects of asset specificity, the sample is divided into two groups; Short-term and Long-term to test propositions 3 and 4. Mr. X identified 3 years as the average duration of the contracts. Therefore, any engagement that lasted for more than 3 years was regarded long-term and any engagement lesser than 3 years was regarded short-term.

Tables 7, 8 and 9 (not shown in this paper), like the previous tables present the factors taken into consideration during the three stages of long-term outsourcing engagements. The results corroborate the answers provided by Mr. X. It is evident from the results that in long-term engagements the relationships of the outsourcing-service provider reflect the Integrative Outsourcing Typology. The mean values for the non-accounting factors during the Bidding Stage (Corporate Reputation and Previous Dealings) supported Proposition 2. On a scale of 1 (Not Important) to 7 (Very Important), the Corporate Reputation variable had a mean of 4.92 and the Previous Dealings variable had a mean of 4.67, both above point 4 (Moderately Variable). This suggests that non-accounting factors were considered important at the bidding stage of outsourcing engagements. The mean values for the non-accounting factors during the Negotiation Stage (Corporate Reputation, Previous Dealings, and Forging Long Term Relationships) also showed significant results. On a scale of 1 (Not Important) to 7 (Very Important), the Corporate Reputation variable had a mean of 4.67, the Previous Dealings variable had a mean of 4.75 and the Forging Long Term Relationships variable had a mean of 6.33. The three variables had values above point 4 (Moderately Variable). These results also suggest that non-accounting factors were considered important during the negotiation stage of outsourcing engagements. The mean values for the non-accounting factors during the Management Stage (Forging Long Term Relationships, Attaining Mutual Goals and Providing Saving to the Outsourcer) also unanimously show figures that are significantly above the Moderately Important point. The Forging Long Term Relationships variable had a mean of 6.67, the Attaining Mutual Goals variable also had a mean of 6.67 and finally, the Providing Savings to the Outsourcer variable had a mean of 6.75.

The results therefore suggest that, again OSP considers non-accounting factors in addition to accounting information for its long-term outsourcing relationships. This is reflective the Integrative Outsourcing Typology. It is interesting to note that the mean values for the other accounting factors remain significant, reaffirming the fact that accounting information is never compromised in the decision-making processes of the outsourcing-service provider. Based on the evidence received from the surveys, Proposition 3 is supported.

The fourth proposition relates short-term IT outsourcing engagements to the Distributive Outsourcing Typology. This proposition was based on the notion that in short-term outsourcing engagements, the parties are aware of the shorter period of commitment and see the necessity to make gains within the limited time
frame. Such behaviour is akin to an arm’s-length buyer-seller relationship that sees each party trying to make opportunistic gains at the expense of the other party. Thus, the relationship between the outsourcing-service provider and the outsourcer is expected to be tense and non-collaborative reflecting the Distributive Outsourcing Typology. Quite surprisingly however, both, the interviews and the surveys produced results that did not support this proposition. In the interview, Mr. X said the following about short-term engagements: “They are more tactical; you sign a short-term contract if you know that a client is going to move on to a larger outsourcing deal down the track and you want to establish the relationship and credentials so that you would have an inside running (working relationship with the outsourcer). This is because you know that the outsourcer has a huge IT spend and that one day you could capture a large chunk of that and that is a huge incentive. Even though we already have large long-term contracts with some banks, if the other banks even want a short-term contract, you always think that you could ultimately win a larger contract. Short-term is not the preferred model but it is considered as a tactic.” Interestingly, the statement shows that contrary to the proposition, a short-term engagement is actually perceived as the means by which OSP can win larger outsourcing engagements. Therefore, the short-term engagement is selected with as much care as a long-term engagement because it is treated as the platform that the outsourcing-service provider uses to establish a rapport with the outsourcer. This paves an opportunity for the outsourcing-service provider to forge a long-term relationship in the future. This behaviour is reflective of the Integrative Outsourcing Typology.

The survey results were analysed to find either corroborating or contradicting evidence from the managers with regards to short-term contracts. The results are shown in Tables 10, 11 and 12 (see Appendix A). The evidence from the surveys once again support the answers provided by Mr. X. The results show that in short-term engagements the focus of the outsourcing-service provider very strongly reflects the Integrative Outsourcing Typology. The mean values for the non-accounting factors during the Bidding Stage (Corporate Reputation and Previous Dealings) supported Proposition 2. On a scale of 1 (Not Important) to 7 (Very Important), the Corporate Reputation variable had a mean of 5.5 and the Previous Dealings variable had a mean of 7, both very much above point 4 (Moderately Variable). This suggests that non-accounting factors were strongly considered important at the bidding stage of outsourcing engagements. The mean values for the non-accounting factors during the Negotiation Stage (Corporate Reputation, Previous Dealings, and Forging Long Term Relationships) also showed significant results. On a scale of 1 (Not Important) to 7 (Very Important), the Corporate Reputation variable had a mean of 5, the Previous Dealings variable had a mean of 7 and the Forging Long Term Relationships variable had a mean of 6.5. The three variables had values above point 4 (Moderately Variable). These results also suggest that non-accounting factors were considered important during the negotiation stage of outsourcing engagements. The mean values for the non-accounting factors during the Management Stage (Forging Long Term Relationships, Attaining Mutual Goals and Providing Saving to the Outsourcer) also unanimously show figures that are significantly above the Moderately Important point. The Forging Long Term Relationships variable had a mean of 6.75, the Attaining Mutual Goals variable also had a mean of 6.75 and finally, the Providing Savings to the Outsourcer variable had a mean of 7. The results received from the surveys with respect to short-term outsourcing engagements had the strongest mean values for non-accounting factors indicating the significance of these factors. This also supported the views of Mr. X and suggests that the relationships maintained by OSP with its short-term outsourcing engagements strongly reflect the Integrative Outsourcing Typology. This finding is contrary to the fourth proposition. Therefore, Proposition 4 is not supported.

The fifth proposition suggests that highly asset specific IT outsourcing engagements are not static in nature. Support for this proposition was found in the interview with Mr. X. The following statements provide evidence to the fact that an outsourcing engagement can start off as something that is highly asset specific, but over time, measures are taken by the outsourcing-service provider to ensure that it reduces in specificity. Mr. X states that the initial investments are high with highly asset specific engagements because of the outsourcing-service provider’s exposure to a new industry or activity. He states that OSP uses the resources of the outsourcer to gain new contracts thus reducing the specificity of the engagement. From the point of view of the outsourcing-service provider, this is one way by which the asset specificity associated to an engagement is reduced. The use of the outsourcer’s employees on other outsourcing engagements to increase revenues, balances off OSP’s high initial investments for the highly asset specific engagement. “We transfer the people who are in the in-house operation of the outsourcer from the new industry…. train that we are going to win them……….they then become resources that we can use on other accounts” The next statement suggests that large IT outsourcing-service providers have the technology and know-how to overcome asset specificity issues quickly. Mr. X states that OSP has the technological competence to reduce the asset specificity of engagements. “However, we have enough technology and know-how to ensure that the asset specificity issue that we face is overcome as soon as possible to make the dealings between our clients and us better. So far, it has had positive results.” This shows that high asset specificity projects reduce in specificity over time due to the initiatives taken by the outsourcing-service provider. Therefore, Proposition 5 is supported.
Thus additional investments deprive the service provider of the usual gains and as a result, these additional investments therefore have to make large investments to acquire the technological know-how to conduct the operations. Activities, they do not possess the expertise to conduct those operations at low cost. The service provider is equipped with the expertise to handle the technical requirements of low asset specific IT outsourcing engagements to the Integrative Outsourcing Typology. As mentioned before, the outsourcing-service provider is focused on factors advocated by Social Capital Theory in highly asset specific outsourcing engagements. The results show that the IT outsourcing-service provider favours and focuses on maintaining long-term collaborative relationships with its outsourcers, regardless of the asset specificity associated to the engagement.

Overall, the statements provide evidence that outsourcing engagements need to also focus on the factors advocated by Social Capital Theory in order to remain successful in the long-term. It is also clear that engagements that are unsuccessful in cultivating a collaborative relationship should be terminated to avoid undesired outcomes. These findings suggest that to survive in the long-term, IT outsourcing engagements should progress towards the Integrative Outsourcing Typology. Therefore, Proposition 6 is supported. This section presented the results upon testing each of the propositions presented earlier in this study. The results were discussed briefly with the presentation of evidence from the interviews and survey. The next section analyses and discusses these results and their implications in greater detail.

**Discussion of Results**

Propositions 1 and 2 explore the level of asset specificity associated with IT outsourcing engagements and its effect on the nature of the relationship between the outsourcing-service provider and the outsourcer. In accordance with theories and findings by previous research, Proposition 1 suggested that a highly asset specific outsourcing project will reflect the Distributive Outsourcing Typology. The rationale for this was that outsourcing-service providers do not benefit from economies of scale with highly asset specific projects. This is because, when the outsourcing-service providers are newly exposed to particular industries and/or activities, they do not possess the expertise to conduct those operations at low cost. The service provider therefore has to make large investments to acquire the technological know-how to conduct the operations. These additional investments deprive the service provider of the usual gains and as a result, these additional costs are passed on to the outsourcer. The outsourcer on the other hand reacts to the increases in expenditure by trying to reduce costs as much as possible. The two parties are thus expected to focus on cost reduction measures and try to make gains opportunistically out of the engagement at the expense of each other. Hence, their focus is proposed to be solely on accounting information about one another and not on factors advocated by the Social Capital Theory. This is reflective of the Distributive Outsourcing Typology. The results however, do not support this proposition. Interestingly, it was found that outsourcing-service providers were focused on factors advocated by Social Capital Theory in highly asset specific outsourcing engagements. The results show that the IT outsourcing-service provider favours and focuses on maintaining long-term collaborative relationships with its outsourcers, regardless of the asset specificity associated to the engagement.

Proposition 2 is also supported by these findings. This proposition relates low asset specific IT outsourcing engagements to the Integrative Outsourcing Typology. As mentioned before, the outsourcing-service provider is equipped with the expertise to handle the technical requirements of low asset specific IT outsourcing engagements.
engagements and thus, does not need to make additional investments for the project. This allows the outsourcing-service provider to enjoy economies of scale because resources used on other outsourcing engagements can be deployed on the low asset specific engagement. The savings are passed on to the outsourcer as well. Therefore, both parties are more receptive to forging relationships that are directed towards attaining mutual goals. This reflects the Integrative Outsourcing Typology. In general, the results of this investigation suggest that in the large IT outsourcing market, the outsourcing-service providers use a more integrative approach to their outsourcing contracts irrespective of the asset specificity of the project. The discussions conducted with the Mr. X revealed that OSP actually seeks projects that are highly asset specific. He states that: "We look for industries in state of change..." The reason for this was that when an industry is going through change, companies in that industry is under threat either because of greater competition, substitutes, changing regulations or supply or demand markets. Under these circumstances management has more incentive to create change that will foster better performance, better results, and better savings. When questioned about the high initial outlays that are involved with highly asset specific projects, Mr. X said: "We invest before we have a client...and this is justified because when you are pursuing clients, you are not going to get that business unless you show that you have the expertise to solve their problems and run their operations well....we have a preference for clients who have an annual IT spend of between 50 and 200/300 million dollars a year.....the key is the size of the revenue that we receive because being an outsourcing service provider, it is all about scale, and revenues are a proxy for scale. The larger the client, the bigger the revenue per year, the more you can do in terms of taking costs out of the system." These statements revealed that the outsourcing-service provider actually perceived additional investments as necessary outlays that add value to the service provider’s position in the IT outsourcing market. Nevertheless, there was a strong level of importance placed on the financial standing of the outsourcer. This suggested the importance of accounting numbers in the decision-making process as the outsourcing-service provider is seen as being concerned about the financial clout of the outsourcer. However, further inquiry revealed that OSP also relied on non-accounting factors. Mr. X claimed that: "We prefer large clients; enterprise clients who have market leadership or a significant base of operation; we target the top 200 corporations in Australia...size is an important factor. We look for a client with healthy business models, we do not really like start ups, we look for a healthy credit rating, a sustainable growing business model, and we look for clients that are in the Top 3 in the industry." These statements suggest that corporate reputation was also an important factor that influenced OSP’s decision in bidding for outsourcing projects. Moreover, Mr. X revealed that OSP shares the risks attributable to the outsourcing project with the outsourcer. "We prefer the all of IT so we like to take over the whole environment and manage the whole thing for the client (complete outsourcing), which will include, hardware, software, people, all future application development requirement.”

These statements suggest that after venturing into a highly asset specific outsourcing project, the outsourcing-service provider actually manages to derive large benefits by being able to deploy the assets of the outsourcer on other outsourcing projects within the same industry. Thus, the first project provides the service provider with the resources and expertise to start deriving economies of scale for projects within the same or a similar industry. The findings in regards to Propositions 1 and 2 reveal that OSP employs a uniformed strategy in bidding for outsourcing projects regardless of the asset specificity. Therefore, the level of asset specificity does not affect the nature of outsourcing relationships for large IT outsourcing-service providers.

Propositions 3 and 4 explore the duration of IT outsourcing engagements and its association to the relationship between the outsourcing-service provider and the outsourcer. Literature on strategic alliance and outsourcing have described long-term engagements as relationships that are influenced by elements such as corporate reputation, trust, and collaborative interactions to ensure sustainability. These factors reflect the Integrative Outsourcing Typology. Therefore, Proposition 3 described long-term outsourcing projects as relationships that reflected the Integrative Outsourcing Typology. This proposition was supported, as it was found that the outsourcing-service provider favoured long-term engagements, which allowed transacting parties interact in a collaborative fashion. The following statement further supported this result: “Typically, the contracts are between 3 and 10 years, and in a large infrastructure environment the investment that is put in and then to try and derive savings out of the environment, you would need a long-term to get the payback for yourself and give your clients savings. It is important to then form a collaborative approach to ensure that the engagement can survive into the long-term. “ With respect to the duration of outsourcing engagements, the results did not support Proposition 4. In line with extant literature, this proposition connects short-term contracts to the Distributive Outsourcing Typology. In short-term contracts, the parties involved are expected to try maximising their gains in the short period of time without focusing on the other party involved. Due to the time-constraint in such engagements, the transacting parties were expected to not behave in a collaborative fashion. Interestingly, this proposition was not supported. The results suggested that the outsourcing-service provider treated short-term contracts similarly to long-term contracts. Although the focus of decision-makers were expected to be solely on quantitative accounting factors, the results indicated that significant focus was also placed on factors like corporate reputation, trust, and collaborative interactions.
The reason for this was that the outsourcing-service provider engages in short-term contracts and treats those contracts as investments for the future, where the service provider is able to use the good relationship formed in the short-term contract to win long-term contracts from clients.

Propositions 5 and 6 were extensions of Propositions 1 to 4. The interesting finding with regards to Proposition 5 was that the high asset specificity of an outsourcing engagement is not a factor that is static in nature. The results suggested that upon contracting, the outsourcing-service provider employs its resources to efficiently develop the technological competence to reduce the specificity associated with the project. Also, the service provider uses resources from the highly asset specific engagement on other outsourcing engagements. This additional revenue earned balances-off with the initial high investments. Therefore, the high asset specificity of such engagements is reduced over time.

The results supported Proposition 6, which proposed all outsourcing relationships to reflect the Integrative Outsourcing Typology in the long-term. The interviews revealed that there are instances when the outsourcing-service provider engages with an outsourcer who may not have been thought to be trustworthy. The outsourcing-service provider was prepared to do so in view of the potential revenues that could be derived from the engagement. While this is reflective of the Distributive Outsourcing Typology, the respondent (Mr. X) made it clear that for a relationship to last into the long-term, efforts would have to be undertaken to ensure that the parties operate in a more collaborative fashion. This would require the parties to build trust and focus on attaining mutual goals. If unsuccessful to do so, Mr. X stated that the engagement should be terminated because it could affect the future operations of the parties involved. This suggests that in the long-term, the relationship between parties in IT outsourcing engagements will possess characteristics reflecting the Integrative Outsourcing Typology.

Additional analysis was conducted on the survey data to increase the rigour of the reported results. The mean values of quantitative accounting and qualitative non-accounting factors considered by OSP at the three stages of its engagements were calculated for the total sample. The results are reported in Tables 13, 14 and 15. The observation of the factors considered in the decision-making processes for the whole sample indicate that at the bidding stage, all variables, accounting and non-accounting were above the moderately important point (4) except the Outsourcer Financial Stability variable. The results are similar in the negotiation and management stages. It seems that there is very little difference between the perceived importance of accounting and non-accounting factors in the decision making processes of OSP, as indicated by the mean values. This suggests that the relationship of OSP and its outsourcers reflect the Integrative Outsourcing Typology.

However, the results above were based on simple mean values. A widely accepted limitation of such values is that it gives equal importance to all items in a sample (Gupta, 1997). It is important to note that there are cases where the relative importance of the different items is not the same (Gupta, 1997). Likewise, the survey sample of this study had a group of 16 outsourcing engagements with different characteristics and requirements. Hence, the revenue received from each of those engagements also varies significantly. It is therefore reasonable to assume that each engagement would have a different level of significance to OSP. Based on the amount of revenue contributed to OSP, each outsourcing engagement is given a weightage. The ‘Weightage’ of each engagement is the percentage of each engagement’s contribution to the total revenues OSP receives from the 16 engagements in the sample. The weightage of each outsourcer is then used to compute weighted mean values of each variable during the bidding, negotiation and management stages of each outsourcing engagement. This provides a more accurate depiction of the significance each factor in the decision-making process (Gupta, 1997).

Table 16 lists the engagements and their respective weightage based on contributed revenue. Tables 17, 18 and 19 list the 16 engagements with their computed weighted mean values for each variable in the bidding, negotiation and management stages. These results show that during the bidding stage, all factors are significant to the decision-making process. The non-accounting factors like Corporate Reputation of Outsourcer and Previous Dealings with Outsourcer have very significant weighted mean values: 5.58 and 4.57 respectively. At the same time, the accounting factors like Outsourcer Size, Outsourcer Profitability and Expected Profits also showed very significant values: 6.58, 5.03, and 5.87 respectively. In the negotiation stage, a similar trend is seen with factors like Project Size, Project Revenue. Expected Profit, Corporate Reputation of Outsourcer, Previous Dealings with Outsourcer, and Forging Long-term Alliance showing significant mean values: 6.17, 6.60, 5.45, 5.01, 4.58, and 6.76 respectively. The management stage also shows similar results with strongly significant weighted mean values for all factors. Here, the values were above 6.85 for four out of the six factors. Three of those four factors were non-accounting factors (Forging Long-term Alliance, Attaining Mutual Goals and Providing Savings to Clients). The two factors with values below 6.85 were Increasing Size of Project and Minimising Investment, and although their values were lesser than the other factors in the management stage, they were still significant (6.35 and 5.72 respectively). An
observation of the scores for individual engagements in Table 17, 18 and 19 also indicate that the differences between the significance of accounting and non-accounting factors are negligible. Together, the results suggest that both, accounting and non-accounting factors are significant in the decision-making processes of OSP. The next section discusses the nature of the outsourcing relationships between OSP and its outsourcers at the termination stage of the engagements. These additional findings are discussed below.

**Termination Stage**

At the outset, it was stated that this study explored the decision-making processes of IT outsourcing-service providers at various stages of outsourcing engagements to understand the nature of its relationships. The results presented in the sections above explored the factors that were considered at the bidding, negotiating, and managing stages of outsourcing engagements. No observation however, was made with regards to the termination stage of outsourcing engagements. This was due to the fact that, the sample of 16 engagement observations had only 2 terminated engagements. A contributing factor to this low number of termination of contracts is OSP’s ability to retain its outsourcing contracts. When asked about this, Mr. X stated that a large majority of OSP’s clients were highly satisfied with the service provider and usually extended the duration of engagement. Although relatively small, this small sample of terminated engagements does provide some insight into the nature of the OSP’s outsourcing relationships at the termination stage.

Of the two contracts, one terminated on stipulated contract termination date and the other after the stipulated contract termination date. This may be taken as an indicator that the outsourcers and OSP were satisfied with the engagement and the collaboration yielded positive results causing the parties to extend the duration of their engagement. To support this suggestion further, the answers to Questions 21 and 22 revealed that OSP provided support services to the outsourcers even after the termination of the engagement. When questioned in the interview regarding terminated engagements, Mr. X said the following: “Within the contractual framework, we have a number of clauses stating that we will offer all the assistance to transition back the people and assets without disruption to services of our clients. We would of course be paid for that and we would extend that continuity of service and assistance even if they were to outsource to another service provider. This is not something that we have to do, but it is done to emphasise our focus on forming partnership-type relationships.” This statement strongly suggests that OSP’s relationships reflect the Integrative Outsourcing Typology. An important point made by Mr. X was that, the support services provided to outsourcers by OSP were done even if the service provider was aware that the outsourcer was getting into a contract with a competitor. Such display of collaboration and trust strongly reflect the Integrative Outsourcing Typology. On the whole, the results from the interviews with Mr. X and the survey data suggest that OSP’s relationships strongly reflect the Integrative Outsourcing Typology.

**Conclusion**

The results in this study are significant because of its focus on asset specificity, in relation to the types of IT outsourcing typologies. Further, the role of accounting and non-accounting information in assisting OSP’s make decisions regarding outsourcing contracts was theorised, proposed and tested. A case study research methodology was employed to operationalise this study and data was collected from interviews and a survey. The respondents were high-level staff of a multinational IT outsourcing-service provider who obliged to participate in this study under a clause of confidentiality.

Of the six propositions proposed, the first two explored the effect of the asset specificity on the nature of IT outsourcing relationships. High asset specific IT outsourcing engagements were proposed to reflect the Distributive Outsourcing Typology in Proposition 1, while low asset specific IT outsourcing engagements were proposed to reflect the Integrative Outsourcing Typology in Proposition 2. The results did not support Proposition 1, but supported Proposition 2. This suggested that asset specificity was an important factor but it did not influence the orientation of the large IT outsourcing-service provider towards working in a collaborative fashion.

The next two propositions analysed the utility of accounting and non-accounting information on the distributive and integrative outsourcing typologies respectively. Proposition 3 aligned the use of non-accounting information to the Integrative Outsourcing Typology decision making process, while Proposition 4 linked short-term engagements to the Distributive Outsourcing Typology. The results supported Proposition 3, but did not support Proposition 4. This suggests that in both circumstances, large IT outsourcing-service providers maintained a collaborative approach with its outsourcing engagements. This conclusion, to a large extent, proposes an alternative solution to the usual relationship between the respective typologies and the relative utilities of accounting and non-accounting information in relation to them.
In Proposition 5, high asset specific engagements were proposed to reduce in specificity over time. To the knowledge of the authors, nothing has been documented about the variability of asset specificity in the IT outsourcing literatures, over a period of time. Though asset specificity has been frequently cited as a vital factor influencing the outsourcing decision, it is interesting that much research ignores its dynamic nature, assuming it to be a static condition. The results supported this proposition suggesting that high asset specificity IT outsourcing engagements involving large outsourcing-service providers are not static in nature, largely due to the increased pervasiveness of technology with the advent of time, thus lowering the specificity of assets.

The findings with respect to asset specificity interestingly highlighted the fact that asset specificity does not affect the manner in which a large IT outsourcing-service provider approaches its outsourcing engagements. Although researchers have found that outsourcing parties are reluctant to enter highly asset specific engagements, the findings in this study indicate that the large IT outsourcing-service provider perceive highly asset specific projects as opportunities for it to gain new clients in a relatively new industry environment. The service provider thus stands the chance of gaining competitive advantage over its competitors in that industry. As a result, the IT outsourcing-service provider uses measures to reduce the specificity of an outsourcing engagement to be able to attract more clients of that nature. This revealed that asset specificity of an IT outsourcing engagement is not static in nature when it involves large IT outsourcing-service providers because it is reduced it over time. However, this finding may apply to large IT outsourcing-service providers only. Due to their financial capacity, the large service provider is equipped with the competence to efficiently seek measures of reducing the specificity of an engagement. This may not necessarily be the case with smaller IT outsourcing-service providers.

Overall, the results suggest that large IT outsourcing-service providers (OSP) value non-accounting factors in their decision-making processes reflecting the Integrative Outsourcing Typology. Contrary to the findings of many researchers, the outsourcing-service provider adopted an integrative approach to its relationships as opposed to a distributive approach even in engagements that were highly asset specific, and short-term in duration. This finding further validated the fact that factors advocated by the Social Capital Theory such as corporate reputation, trust and collaborative interactions are crucial in IT outsourcing relationships. More broadly, via the use of a case approach, and within this setting, it is shown that the use of qualitative factors and their related management and psychological theoretical underpinnings as advocated in many management accounting literatures, do play a role in the decision making processes of what, on the surface, appears a purely financial decision. Notwithstanding this, the importance of accounting information was never compromised under any of the circumstances. All results suggested that accounting information is vital to the decision-making processes of IT outsourcing-service providers and that non-accounting information serves as an additional and important contributor to accounting information in the decision making process.

Limitations and Implications for Future Research

Although this study provides unique and interesting insights that are absent from some previous research, it has its limitations in regards to its results and contributions. First and most important is the fact that the scope of this study was limited to one IT outsourcing-service provider. Yin (1989) states that case studies, like experiments are generalisable to theoretical propositions and not to populations or universes. The objective here is to expand and generalise theories (analytic generalisation) and not enumerate frequencies (statistical generalisation) (Yin, 1989). Therefore, the main limitation of this study is its inability to generalise its findings. This has been widely acknowledged as a major barrier in doing case studies (Yin, 1989; Brownell, 1995).

To understand the relationship between an outsourcing-service provider and outsourcer, the case study is one of the best research methods (Yin, 1989). While this research method presents the best setting to analyse a phenomenon in its natural setting, it is not easily generalised. With regards to this study, the IT outsourcing-service provider was a large multinational organisation. At best, the results of this study could have similar implications to organisations of similar size and scale of operations. The results may not be generalised to smaller IT outsourcing-service providers because the technological and financial advantage present with the larger service provider may not be present for smaller service providers. To be generalised, repeated studies would have to be conducted on two or more outsourcing-service providers to assess if the results are expected to occur (Yin, 1989). Based on the replication logic, the results from conducting such replications can be accepted for a much larger number of IT outsourcing-service providers. Firstly, future research should study the relationships of another large IT outsourcing-service provider to ensure that the results of this study is not organisation specific and that it can be extended to organisations of similar scale.
As mentioned before, this study suggests that the asset specificity of IT outsourcing engagements is a factor that is not static. The results indicate that the high asset specificity of outsourcing engagements is variable in nature. However, this study has relied on the interview results to support this proposition. Future research should explore this finding further by conducting a more detailed experimentation of the nature of asset specificity with regards to IT outsourcing projects and also other types of outsourcing projects.

Implications for Industry

This study has strong implications for managers in the IT outsourcing industry. The results suggest that the IT outsourcing-service provider in this study is focused on forming collaborative relationships. Other IT outsourcing-service providers should also resort to forming more collaborative relationships with their clients. When an outsourcing relationship reflects the Integrative Outsourcing Typology, the parties involved are able to engage in a more relaxed fashion and assist each other in attaining mutual goals. Moreover, the findings in this study support the claims by research on outsourcing relationships that such alliances produce significant long-term benefits to all parties involved.

Outsourcers on the other hand should have more realistic expectations from the outsourcing-service providers. Outsourcers should realise that the outsourcing engagement can produce more benefits if all parties engage with a collaborative attitude. It is also important for the outsourcer to realise that the service provider is also an entity that needs to make profits to survive. Collaborative interactions with a focus on attaining mutual goals will benefit all parties in IT outsourcing engagements.

References


