

Unlocking path dependencies in Business Process  
Outsourcing decision making

- Research in progress -  
Submission for the 4<sup>th</sup> Global Sourcing Workshop 2010

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# **Unlocking path dependencies in Business Process Outsourcing decision making**

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## **ABSTRACT:**

The objective of this study is to examine the decision process and outcome at the end of an outsourcing contract and how this process evolves over time. Despite the vast amount of literature in IS Outsourcing, little is known about the determinants, the process, the context and the outcome of the last phase in an outsourcing relationship. In order to better understand the complexity and dynamics of the contract termination or extension, we will apply a process-theoretic logic. It draws on Path Dependence Theory which suggests that path decisions are rooted in circumstances or events that take place in precedent phases of the outsourcing process. Based on the results of 21 Business Process Outsourcing (BPO) cases, our findings confirm the existence of significant path-dependencies which lead to sub-optimal economic results. Once a business process has been outsourced, the client organizations get literally locked-in the chosen path and tend to continue the contract with the vendor, even if initial expectations did not accrue.

In order to better understand the pattern of such path trajectories, a process model will be presented which integrates distinct stages of the service delivery phase, the expectations of the client organizations, and internal as well as external stimulation events that lead to expectation gaps. These stimulation events are necessary but non-sufficient conditions for breaking the path. In addition, significant resource commitments from the clients' perspective are required for breaking the path. If these commitments are not be made, the lock-in situation prevails, i.e. back-sourcing or a vendor change is unlikely to take place.

**KEYWORDS:**

Business Process Outsourcing, path dependence theory, process theoretic logic, lock-in effect, contract extension, provider change, backsourcing, decision process

## **1. INTRODUCTION**

Within the overall outsourcing market, business process outsourcing (BPO) is by far the fastest-growing segment (Rouse and Corbitt, 2004; IDC, 2009). In a BPO deal, an external vendor “*is responsible for performing an entire business function for the client organization*” (Dibbern et al. 2004). Thus, the fulfillment of businesses processes is the principal service element. Since most business processes are supported by IT systems, BPO can also be defined as a logical extension of pure IT outsourcing (Rouse and Corbitt, 2004; Froeschl, 1999; Lacity and Willcocks, 2001). IT is considered as an important, often decisive “ingredient” to enable and automate new process patterns as well as to deliver the promised productivity gains and cost savings to the client. Therefore, the concepts of information technology outsourcing (ITO) and BPO are closely intervened; in virtually every BPO engagement, the service provider assumes responsibility for not only the business process to be performed but also the underlying hard- and software services (Kern, Lacity and Willcocks, 2002). One of the key differences between pure ITO and BPO, however, is that business process responsibility is handed over to an external vendor in case of BPO, while it mostly remains at the client side in case of ITO. This likely leads to a stronger level of dependence on the vendor and a stronger locking into the relationship with the vendor in case of BPO, because the client loses a significant part of both its IT and business knowledge. Hence, bringing both resources back in-house may be more difficult for BPO clients (Willcocks et al., 2004). Thus, the relationship between client and vendor takes on the role of a marriage rather than a contract (Ghose, 2003; Weisman, 2005). The potentially high resource dependence of the client may result in strong path dependencies during the course of a contract. Such path dependencies could potentially constrain the client’s degree of freedom within the post contractual sourcing decision. This decision may entail the following options (see Figure 1): (A.) extend the contract with the service provider, (B.) change the provider, (C.) reintegrate the externalized services, i.e.

backsourcing (Lacity and Willcocks, 2001), (D.) a combination of an outsourcing and backsourcing strategy, e.g. through a joint-venture where capital and hence assets and responsibility are shared between client and vendor (Lacity and Willcocks, 2003).

While some research on ITO has been performed on the backsourcing decision (Whitten and Leidner, 2006; Hirschheim and Lacity, 2000; Veltri, Saunders and Kavan, 2008) as well as on the decision to continue the outsourcing relationship in the future (Nam, Rajagopalan and Chaudhury, 1996), there is a research gap along three lines. First, almost no attempt was made to compare and explain the choice among various sourcing options at the end of an outsourcing contract (Jayatilaka, 2002). Second, the post contractual sourcing decision of BPO rather than ITO has rarely been examined. Third, there is scant research that has taken a process theoretic view on the post contractual sourcing decision (Dibbern et al., 2004)

In order to fill this threefold research gap, this study intends to unravel the process that eventually leads to the post contractual sourcing decision in case of BPO. To this end, a multiple case study design is chosen. The study is exploratory in nature. It draws on Path Dependence Theory which suggests that path decisions are rooted in circumstances or events that take place in precedent phases along the path process, i.e. the process between the initial BPO decision and before the subsequent renewal or change decision. Based on an analysis of 21 BPO cases, the relationship between path dependencies and the post contractual sourcing decision is described. In particular, the trajectory from (a) prior expectations as major sources of path dependencies, to (b) stimulating events that challenge the fit between prior expectations and actually realized expectations to (c) path breaking responses to close expectation gaps rather than implicitly accepting them are outlined. The un-locking of path dependencies occurs either through adjusting expectations and extending the contract or through more radical responses in form new organizational arrangements, i.e. backsourcing or provider changes.

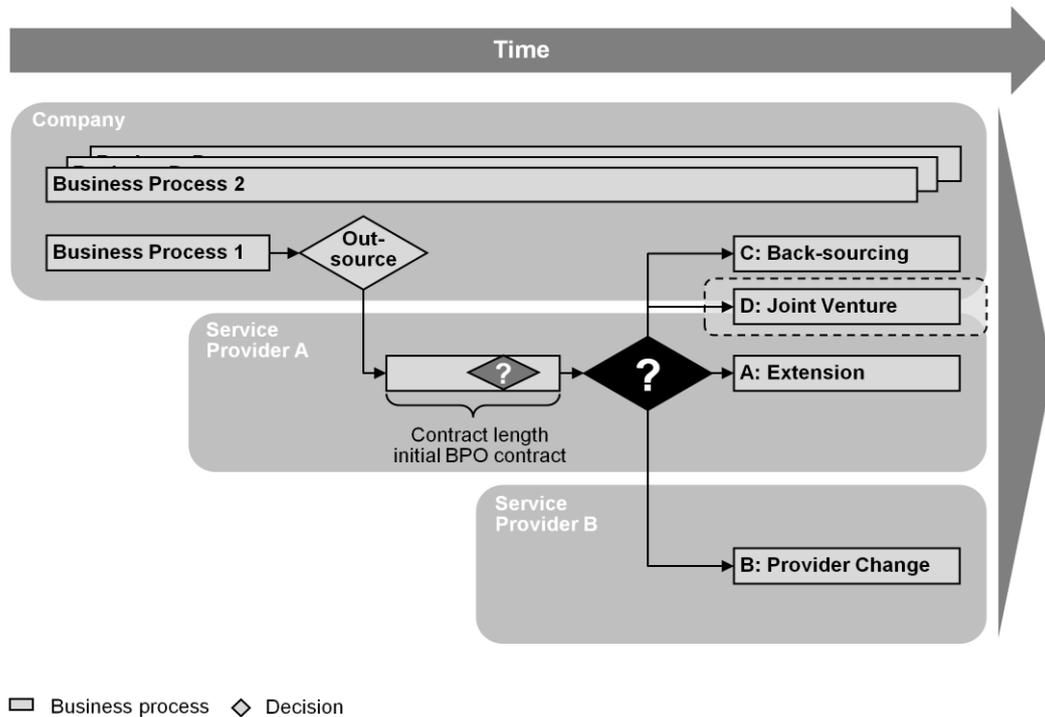


Figure 1: Options at the end of an outsourcing contract

## 2. THEORETICAL FOUNDATION

After Kodak outsourced its IS functions in 1989, a new trend was born for practice, which in turn stimulated the development and growth of academic research in this segment. A significant theoretical and conceptual body of knowledge has been shaped which has been built around “*various theoretical notions developed in the fields of strategic management and economics*” (Cheon, Grover and Teng, 1995). As a consequence, different theoretical lenses have been deployed and extended for explaining phenomena in IS outsourcing. According to Dibbern, Hirschheim and Jayatilaka (2004) the most relevant theories are the Transaction Cost Theory, the Resource-based and Resource-dependence Theory, the Agency Theory, the Power Theory, the Institutional Theory and the Innovation Diffusion Theory.

All of these studies have used a variance theoretic logic (Markus and Robey, 1988) in order to investigate the determinants of the outsourcing decision regardless of their formation in a

certain period of time. Since an outsourcing decision needs to take precedent expectations and experiences into account, we believe that a time-invariant variance theoretic logic can fruitfully be extended by an evolutionary perspective. Thus, our research aims to follow a process theoretic logic which analyzes the events and circumstances that happen prior to the next contract phase in BPO arrangements and that potentially influence the post contractual sourcing decision outcome. In fact, we believe, that our investigation is one of the first approaches to take a time-variant perspective within the stream of ITO and BPO research.

In this vein, we intend to analyze the path of events that leads to a specific decision outcome (Markus and Robey, 1988; Scott, 1994). Our subject of analysis is a “*series of occurrences of events rather than a set of relations among variables*” (Mohr, 1982).

As such, this study seeks to explain how a particular post contractual sourcing decision, e.g. a contract extension or a backsourcing decision, is influenced by a sequence of precedent events. Accordingly, the time ordering among the contributing events is likely to be crucial for the decision outcome. Furthermore, the states and events are not scalable. Poole et al. (2000) developed a typology of process theories for explaining organizational change. Based on the unit of change, respectively the mode of change, they differentiate between evolutionary, dialectic, life-cycle based, and teleological change archetypes. According to a teleologic typology, every decision process or path can be analyzed on the basis of its initial goals, the implemented results, the evaluation of the respective outcomes, and – in case of a goal-outcome-mismatch – as a process for modifying previous assumptions and decisions elements (Van de Ven and Poole, 1995).

These phases in the teleologic typology help organizations to create, shape and possibly to reverse focal decisions and managerial actions regarding the outsourcing of business processes. Since these decisions lead to trajectories or paths which are hard to break, a certain level of path dependence may be the outcome of such reasoning.

The term path dependence was coined by David (1986) and Arthur (1988) within the context of competing technologies. Based on David, *“a path dependent stochastic process is one whose asymptotic distribution evolves as a consequence of the process’ own history”* (Ackermann, 2001). Arthur described so called lock-in effects in the historical development of competing technologies in a way that a path could be taken that leads to suboptimal results. He defined the prerequisite for the development of such a path as *“increasing returns”* (Arthur, 1988) meaning that some kind of self-reinforcing advantage has to exist.

One example for path dependence in the technology context is the development of dominance of the QWERTY keyboard. Based on David (1985) the QWERTY design won a test trial against a more efficient keyboard and thus the development of path dependence was started. The key advantage in that competition was not the design of the QWERTY keyboard but the fact that the user of the QWERTY keyboard was trained to type with 10 fingers, his competitor was not (Arthur, 1994). Even after several attempts to introduce a better and more efficient design for keyboards, the QWERTY design remained predominant indicating the strong dependence on the initially taken path.

Thus, we will apply Path Dependence Theory to our research problem. As Sydow, Schreyoegg and Koch (2005) state, *“there are very few studies that have rigorously applied path dependency to the study of organizations”*. They argue that one reason might be that the original model of path dependence which was developed in the context of technology paths *“does not suit the needs of an (inter-) organizational analysis”*. Path Dependence Theory in an organizational context explains the conditions under which history influences institutional decision making and the effects that history can have on contemporary institutional decision making (Robinson and Meier, 2006; Schäcke, 2006). In particular, Sydow, Schreyoegg and Koch (2005 and 2009) expanded the original model of Path Dependence Theory in the

following three areas. First, they substitute the “*utility-maximizing premise by less restrictive positive feedback dynamics that are driven by individual or organizational self-interest and based on mechanisms of self-reinforcement*”. Second, they argue that path creation in the organizational context is not only dominated by a random selection of choices but can also be a result of intentional decision making and behavior which are based on expectations. Finally, they consider the “un-locking” of path dependence in the organizational context as an important impetus for leaving suboptimal trajectories. In contrast to initial technological context which was described in natural law fashion, path dependencies in the organizational context can be broken and reversed by organizational decision making. The resulting expanded model is shown in Figure 2.

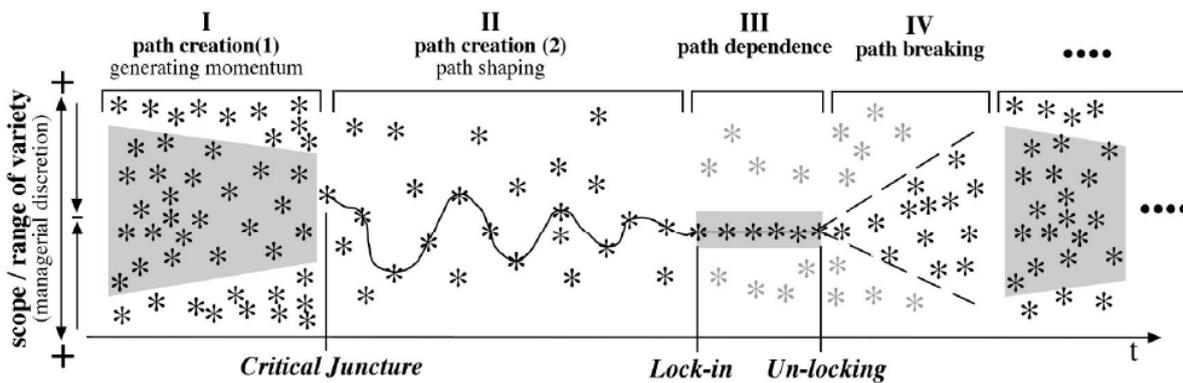


Figure 2: From path creation to path breaking (Sydow, Schreyoegg and Koch, 2005)

According to this model, path creation is formed by initial goals and expectations, managerial decisions like outsourcing lead to a path-dependence, and expectation-result-gaps or other stimulation events may lead to a renunciation of the existing path trajectory.

### 3. RESEARCH METHODOLOGY

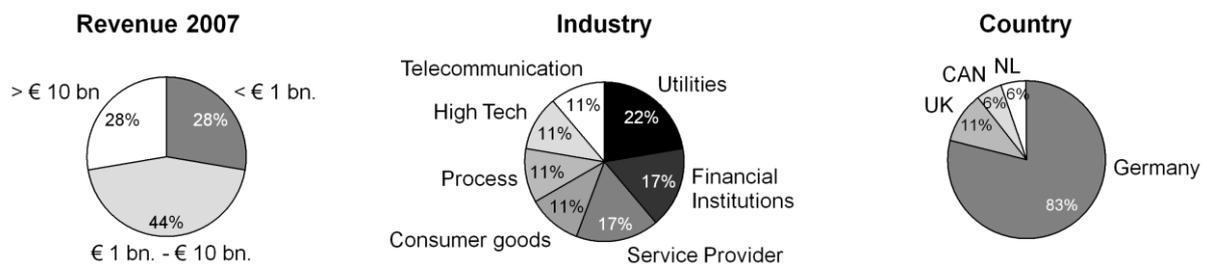
The objective of this study is to explore corporate BPO decisions at the end of an outsourcing contract phase. Furthermore, it seeks to analyze whether path dependencies exist within the

context of such decisions, how they evolve over time and how dependent paths can be unlocked. The challenge in this kind of research is “*to identify the circumstances that created the particular twists and turns in each case*” (Poole et al., 2000). Therefore, we chose an exploratory qualitative approach since it allows us to identify the formation of paths as well as events that finally lead to path breaking behaviors over a certain period of time. In order to capture the richness of the phenomena involved, we deemed a cross-sectional study with time-point based case studies that include the historical development from the initial BPO decision to the post contractual sourcing decision. Based on the empirical evidence solicited, we would like to deepen our understanding of the BPO extension/non-extension decision as well as the existence of path dependencies. Based on our findings, we will develop a model for BPO path dependencies, which will be refined stepwise from case to case.

The qualitative data collection has been conducted on the basis of key informant interviews with no limitation to a single industry or specific business process. The event sequence that leads to a specific decision about the future of a BPO deal has been gathered post hoc with companies that have already passed the post contracting decision. Thus, the design can be classified as archival research (based on Poole et al., 2000) as it leverages retrospective interviews, analysis of documents and records and other historical observations.

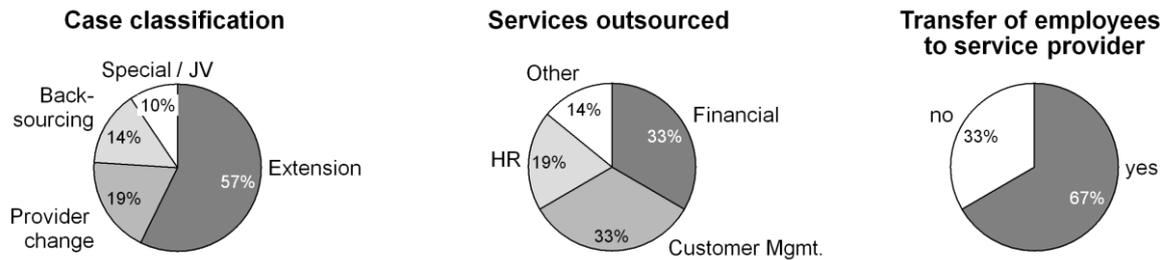
For each case, we tried to gather all relevant events that had an impact on the final decision at the end of the contract. In a first step, the events were classified based on time of occurrence, duration, impact and dimension of expectation. In a next step, event sequences were developed before they were analyzed regarding temporal dependencies. Finally, we tried to identify coherent patterns in these data (based on Poole et al., 2000, and Yin, 1994).

In total, 31 interviews regarding 21 BPO cases in 18 companies serve as a basis for our empirical evidence. Additional supporting documents like contracts or performance review reports of service providers were utilized if available. The classification of companies participating in the study is illustrated in Figure 3 with respect to their company size, industry and country of origin. 72% of all companies have earned more than € 1 bn. in revenues, and as indicated in the research design, this study was not limited to one specific industry but represents cases from seven different industries. The majority of participating companies is located in Germany (83%), followed by the United Kingdom (11%), Canada and Netherlands (each 6%).



**Figure 3: Classification of participating companies**

The classification of analyzed cases in 18 companies is shown in Figure 4. In 57% of all BPO arrangements, the contract was extended, 19% of all cases reported a provider change, 14% of the companies sourced the respective business process back in-house, and the remaining 10% entered into the construction of a special solution, e.g. a joint-venture. As indicated before, this study was not limited to a specific business process. In one third of all cases, the subject of BPO was on financial processes, in another third on customer management processes, in 19% on HR processes and in the remaining 14% a process from other areas. In 67% of all cases, employees were transferred to the service provider in the transition phase of the outsourcing contract.



**Figure 4: Classification of BPO cases**

In 23% of the 31 interviews, the interviewees were senior executives, in 48% department heads and in the remaining 29% project leaders in charge of the outsourcing relationship. Data collection took place between October 2006 and May 2009.

All interviews were conducted in person at the specific company site in order to get the maximum amount of information from the interviewee and for the purpose of easy access to further supporting documents. The interviews followed a structured questionnaire that was developed a priori following our theoretical lens as well as the literature. The interview guideline had been pre-tested with subject experts. The duration of each interview was between one and three hours.

#### 4. RESULTS

The following table (Table 1) lists the 21 cases based on 31 interviews conducted as a basis for the empirical analysis of this study. The two key results that will be described in more detail are (4.1.) confirmation of path dependencies for the context of business process outsourcing decision taking and (4.2.) development of a model how those paths could be unlocked.

Case ID	Company ID	Size		Industry	Country of case	Service outsourced	Transfer of employees	# Interviews	Decision taken
		Revenue (€ bn., 2007)	# Employees (2007)						
6	E	1 – 10	> 10.000	Service Provider	Germany	Customer Mgmt. Services	yes	1	Extension
9	Q	> 10	> 10.000	Process Industries	Germany	Financial Services	yes	1	Extension
1	L	> 10	> 10.000	Consumer goods	Netherlands	Financial Services	no	1	Extension
3	P	1 – 10	1.000 - 10.000	High Tech	Germany	Human Resources	yes	1	Extension
16	B	1 – 10	1.000 - 10.000	Financial institution	Germany	Financial Services	yes	1	Extension
17	B	1 – 10	1.000 - 10.000	Financial institution	Germany	Financial Services	yes	2	Extension
20	C	1 – 10	> 10.000	Financial institution	Germany	Customer Mgmt. Services	yes	2	Extension
4	A	> 10	1.000 - 10.000	Financial institution	Germany	Financial Services	no	2	Extension
8	O	< 1	1.000 - 10.000	High Tech	Germany	Logistic services	yes	1	Extension
10	G	1 – 10	1.000 - 10.000	Utilities	Canada	Customer Mgmt. Services	yes	2	Extension
12	H	1 – 10	1.000 - 10.000	Utilities	Germany	Financial Services	no	1	Extension
21	F	> 10	> 10.000	Service Provider	Germany	Financial Services	yes	2	Extension
5	D	< 1	1.000 - 10.000	Service Provider	Germany	Human Resources	no	2	Provider Change
14	M	1 – 10	1.000 - 10.000	Telecommunication	Germany	Human Resources	yes	2	Provider Change
15	N	1 – 10	> 10.000	Telecommunication	UK	Human Resources	yes	2	Provider Change
18	I	< 1	1.000 - 10.000	Utilities	Germany	Customer Mgmt. Services	yes	1	Provider Change
2	K	< 1	< 1.000	Consumer goods	Germany	Customer Mgmt. Services	no	2	Back-sourcing
7	E	1 – 10	> 10.000	Service Provider	Germany	Customer Mgmt. Services	no	1	Back-sourcing
19	J	> 10	> 10.000	Utilities	UK	Customer Mgmt. Services	no	2	Back-sourcing
11	R	< 1	1.000 - 10.000	Process Industries	Germany	Procurement Services	yes	1	Special / JV
13	H	1 – 10	1.000 - 10.000	Utilities	Germany	Marketing and Sales	yes	1	Special / JV

**Table 1: Overview of 21cases**

Once the process had been outsourced, the client organizations were literally locked-in the chosen path. Despite suboptimal outcomes, company representatives reported that they did not re-evaluate their decisions on a regular basis. In contrast, those cases that entered alternative arrangements, like a provider change, back-sourcing or a joint-venture, reported the existence of a significant stimulation event which facilitated the un-locking of the existing path.



#### **4.1. Path dependencies in BPO relationships**

As a first indication, the interviewees of the study reported in 20 of the 21 cases (95%) that they feel a medium or high dependence on the current service provider of their outsourced services and on the path of continuation of that particular contract. The admitted level of dependence was stronger when employees had been transferred to the service provider in the context of that contract.

Sydow, Schreyoegg and Koch (2009) report three conditions that have to be met in order to substantiate path dependence based on their model of organizational path dependence (Figure 2). These are (I.) identification of strategic persistence or operational rigidity within an organization, (II.) identification, exploration and reconstruction of the self-reinforcing feedback mechanisms, and (III) the search for a triggering event that was likely to have started the path-building process.

Based on the data from our empirical study, we can confirm these three prerequisites or features in the outsourcing context. Regarding the operational rigidity, (I.) Sydow, Schreyoegg and Koch (2009) further state that *“the lock-in phase is nevertheless constitutive for path dependence. If actors were not locked in, one would not call the process path dependent.”* Based on Sydow, Schreyoegg and Koch (2009) this feature was confirmed if inefficiencies could be demonstrated in the current path. As shown in the table below, the interviewees reported only in 3 of the 21 cases that the current setting was optimal. In the remaining 18 cases, they admitted that at least over a longer time horizon a different path (e.g. different provider, stronger provider management) would have been more beneficial than the current one.

In all cases, the interviewees experienced self-reinforcing feedback mechanisms over the lifetime of the outsourcing contract. These were mainly learning effects (19 of 21 cases) but also adaptive expectation effects (2 of 21 cases). Learning effects express that the subsequent iteration of the process leads to efficiency gains due to an ongoing optimization. The learning effects in outsourcing (e.g. by process standardization and economies of scale) are often even stated within contracts in form of a yearly efficiency increase target. The concept of adaptive expectations is related to a situation where individuals or organizational units take a specific decision because “*they expect others to do the same and wish to end up on the side of the winners*” (Sydow, Schreyoegg and Koch, 2009).

The required triggering event (III.) for the initiation of the path dependence in an outsourcing context is the signature of the outsourcing contract. Before the contract is signed, several choices (e.g. other service providers, insourcing, joint-venture) still exist for the company. However, the signature leads to a pre-defined path where positive, self-reinforcing feedback can lead to the described lock-in effect.

Case ID	Impression that current situation/setting is suboptimal	Self-reinforcing feedback mechanism		Reported level of dependence of company on the service provider	Resulting level of path dependence	Decision taken
		Existence (y/n)	Key mechanism			
6	no	y	learning effect	medium	no – low path dep.	Extension
9	no	y	learning effect	high	no – low path dep.	Extension
1	no	y	learning effect	high	no – low path dep.	Extension
3	yes, in some degree	y	learning effect	high	medium path dep.	Extension
16	yes, in some degree	y	learning effect	high	medium path dep.	Extension
17	yes, in some degree	y	learning effect	high	medium path dep.	Extension
20	yes, in some degree	y	learning effect	high	medium path dep.	Extension
4	yes	y	learning effect	low	path dependence	Extension
8	yes	y	learning effect	medium	path dependence	Extension
10	yes	y	adaptive expectation	high	path dependence	Extension
12	yes	y	learning effect	medium	path dependence	Extension
21	yes	y	learning effect	high	path dependence	Extension
5	yes	y	learning effect	medium	path dependence	Provider Change
14	yes	y	learning effect	medium	path dependence	Provider Change
15	yes	y	learning effect	medium	path dependence	Provider Change
18	yes	y	learning effect	medium	path dependence	Provider Change
2	yes	y	adaptive expectations	high	path dependence	Back-sourcing
7	yes	y	learning effect	medium	path dependence	Back-sourcing
19	yes	y	learning effect	medium	path dependence	Back-sourcing

11	yes	y	learning effect	high	path dependence	Special / JV
13	yes	y	learning effect	medium	path dependence	Special / JV

**Table 2: Characteristics of path dependence**

The identified sources for the path dependencies in the cases were e.g. high upfront investments into the relationship that would be lost in case of a contract termination, learning effects leading to efficiency increases, fulfilled expectations, lowered or adapted expectations during the outsourcing arrangement leading to a feeling of satisfaction with the arrangement, imprecise monitoring of the status quo as well as the missing of a regular re-evaluation process regarding the chosen path (even in cases where suboptimal outcomes were reported).

Table 2 indicates that only in 3 of the 21 cases analyzed, no or only a low level of path dependence has been reported due to the fact that the interviewees considered the current setting as optimal. In only four cases, the level of path dependence seems to be at least medium and in the other 14 cases it seems that the level of path dependence is quite high.

As a first identified pattern, we can further separate the cases of medium or high path dependence based on the interviewee’s general attitude towards outsourcing, satisfaction with the outsourcing partnership and satisfaction with the results of the outsourcing deal.

Category (a.) is defined by having a positive attitude towards outsourcing and at least a positive level of satisfaction either with the outsourcing partnership or the results of the outsourcing deal. Category (b.) are those cases where the company considered outsourcing as the superior organizational setup, however was unsatisfied with the outsourcing provider or results (neutral or negative rating). Category (c.) contains those instances where the overall attitude of the interviewees have changed so that full outsourcing was not the preferred option anymore but was rather considered as neutral or negative.

In the cases of category (a.), i.e. positive attitude and positive outcome, the final decision was (with one exception) a contract extension. Category (b.), i.e. positive attitude but negative outcome, has led to a provider change (with one exception, too). Category (c.), i.e. negative attitude and negative outcome, triggered either back-sourcing or a special governance form (e.g. a joint-venture).

Case 10 is one of the noteworthy exceptions. The client organization was highly unsatisfied with the BPO partnership and the outcome of the deal, however, it was not able to un-lock the strong path dependence and, thus, extended the contract (after a renegotiation). In addition, the client organization in Case 5 was fully satisfied with the partnership and outcome but decided in favor of a provider change. This change was caused by additional demands in the requirements of the new contract which could not be satisfied by the old service provider. Thus, the path was un-locked and the company decided to undergo a provider change. The related overview of cases and classifications is shown in Table 3.

Case ID	General attitude towards outsourcing (- negative, 0 neutral, + positive)	Satisfaction with outsourcing partnership (- negative, 0 neutral, + positive)	Satisfaction with results of outsourcing deal (- negative, 0 neutral, + positive)	Decision taken	Category
3	+	+	0	Extension	a
16	+	+	+	Extension	a
17	+	+	+	Extension	a
20	+	+	0	Extension	a
4	+	0	+	Extension	a
8	+	0	+	Extension	a
10	0	-	-	Extension	Exception a
12	+	+	+	Extension	a
21	+	0	+	Extension	a
5	+	+	+	Provider Change	Exception b
14	+	-	0	Provider Change	b
15	+	-	0	Provider Change	b
18	+	0	0	Provider Change	b
2	-	-	-	Back-sourcing	c
7	0	-	-	Back-sourcing	c
19	0	-	0	Back-sourcing	c
11	0	-	0	Special / JV	c
13	0	0	0	Special / JV	c

**Table 3: Classification of cases with medium or high path dependence (at the time of decision)**

#### **4.2. Understanding the formation of path breaking patterns**

According to Sydow, Schreyoegg and Koch (2005), conditions exist under which paths can be un-locked. Based on our initial findings, a model of path breaking incidences in the BPO context has been developed which integrates the distinct stages of the service delivery process, the expectations of the client organizations, and internal as well as external stimulation events that lead to expectation gaps.

Based on this model, stimulation events arise, if the initial expectations of the client organization prior to the start of the BPO arrangement are not met according to at least one of the following four dimensions (see Figure 5): (a.) company specific expectations, e.g. strategic direction, (b.) BPO deal specific expectations, e.g. satisfaction with the partnership, (c.) provider specific expectations, e.g. economies of scale in the area of the outsourced process, and (d.) environmental specific expectations, e.g. laws and regulations. Coad and Cullen (2006) use these domains to cluster specific evolutionary processes in the context of evolution of cost management practices in inter-organizational domains. They expect that “*evolutionary processes within one domain to influence and be influenced by those in other domains*” (Coad and Cullen, 2006).

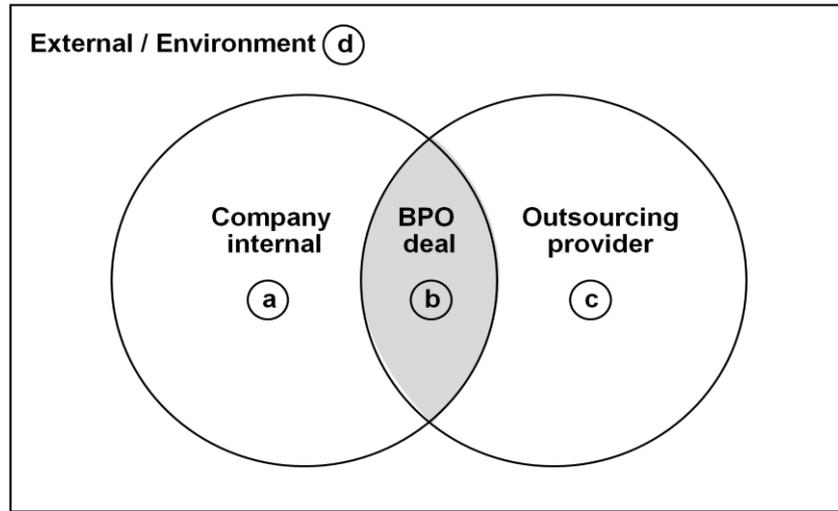


Figure 5: Dimensions of expectations (adapted model of Coad and Cullen 2006)

In all 21 cases, the companies stated to explicitly set specific expectations in at least one of these dimensions regarding the BPO deal. The key expectations were in most cases documented in the business case or contractual agreements, however, several expectations were not stated explicitly in the contract but do exist implicitly as indicated in the following overview (Table 4). The interviewees also stated that expectations in dimensions a, c and d, are often stability of the status quo whereas the expectations towards dimension b, are in particular related to changes of the status quo.

Dimension of expectations \ Nature of expectation setting	Company	BPO Deal	Provider	Environment
Explicitly noted expectations	11	21	14	6
Implicitly articulated expectations	8	-	5	12
No expectations stated	2	-	2	3

Table 4: Absolute frequency of expectation setting along the dimension model (21 cases)

Furthermore, it has to be noted the client's expectations are dependent on the phase of the BPO relationship (see Figure 6). Directly after going-live with the outsourcing arrangement, the goal of Phase I is to get the service up and running after the transition of the business process and its resources from the client to the service provider. The overall objective of Phase II is to return to the performance level as it has been prior to the transition phase. In Phase III, the predefined contractual objectives and expectations shall be met. Finally, the goal of Phase IV is to exceed the initial goals of the outsourcing contract. Thus, the relationship model denotes increasing levels of performance throughout the relationship. If the objectives in this service delivery phase can be fulfilled by the vendor, an ongoing increase in the level of trust in the capabilities of vendor will be the result.

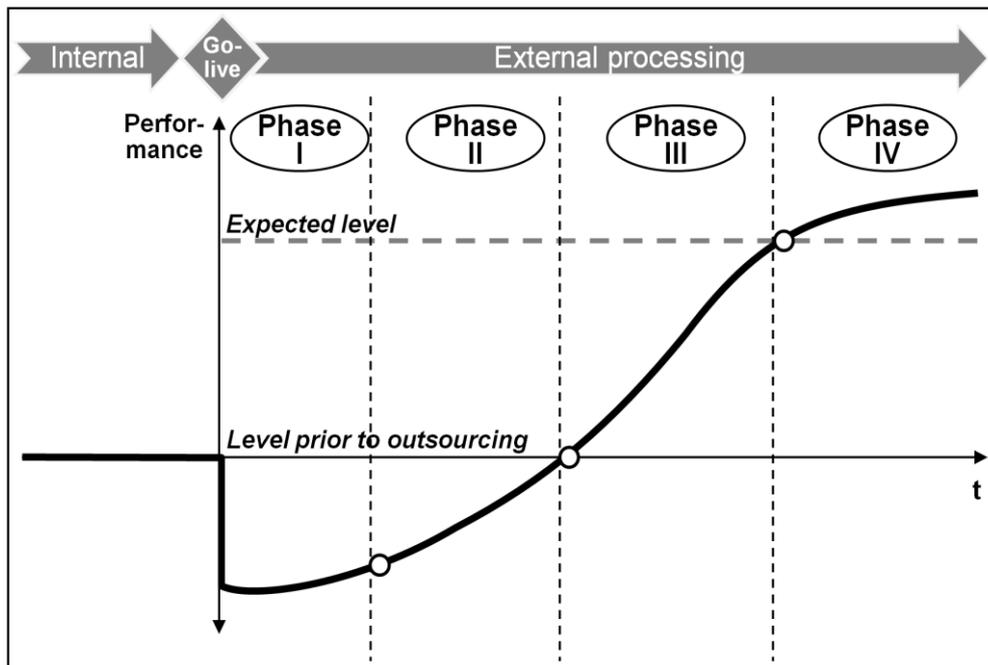


Figure 6: Phase model of BPO relationship

March and Simon (1985) define the process of decision making as a sequence of separable stages, ordered through time and with transition routines to make adjustments between the different stages according to the fulfillment of the decision maker's expectations. In this vein, Figure 7 elaborated a proposed model of monitored expectation fulfillment where the initially

set of expectations in the four dimensions will be compared with the status quo in each of these dimensions for all four phase in the service life cycle. If the status quo within every phase of the model matches the initial expectations (within a small range of tolerance), the path is likely to be continued. In contrast, if the status quo deviates from the expectations, a stimulation event occurs which has the potential to break the existing path and, thus, can open the arena for alternative arrangements.

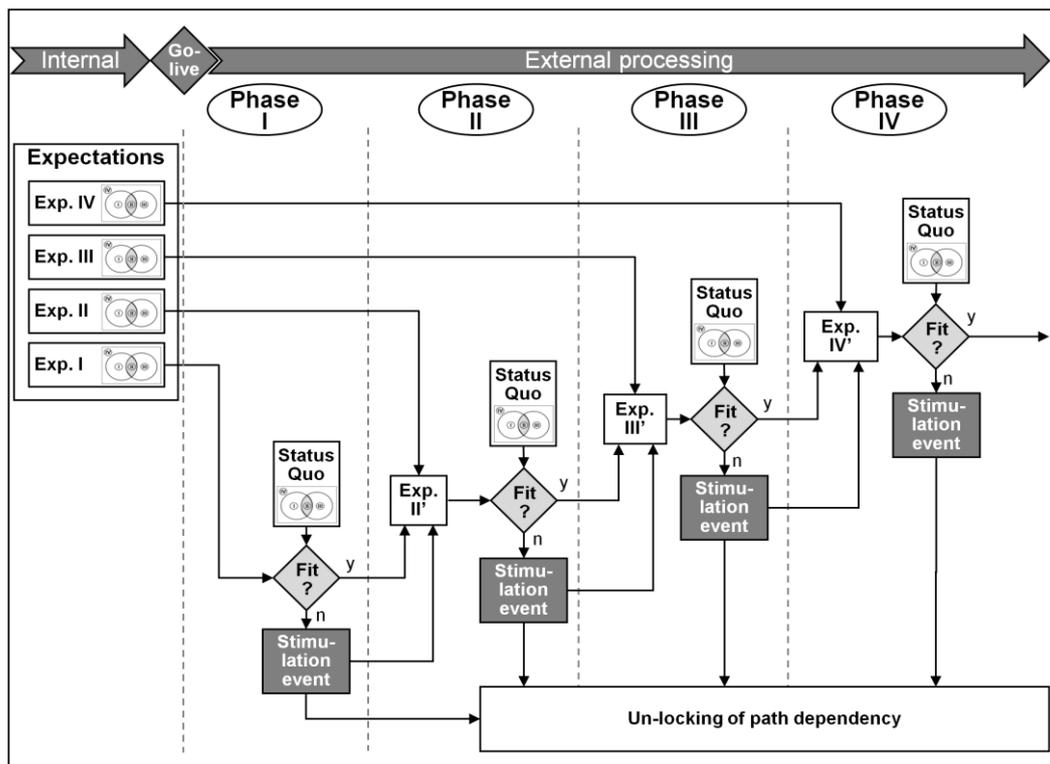


Figure 7: Model of monitored expectation fulfillment

Interestingly, as described by March and Simon (1985), stimulation events occurred in eight cases where an adjustment of the initial expectations (e.g. Exp. II → Exp. II') could be found instead of breaking the path through implementing an alternative arrangement. In case 4, for instance, a CEO of a financial service provider stated that the initial expectations towards the BPO arrangement have not been met. However, due to lacking time and management capacity they would not re-evaluate the entire BPO decision but only update the contract conditions.

This example underlines how existing path dependencies develop retention forces that may lead to sub-optimal outcomes.

In order to provide a deeper understanding of the retention forces, we will further outline two cases for understanding the proposed logic of our model of monitored expectation fulfillment in BPO. Table 5 indicates the properties of the cases where stimulation events were triggered due to a mismatch of expectations with the status quo.

Case ID	Specific expectations prior to deal (-): stability of status quo (x): change of status quo				Phase of mismatch	Stimulation event			Result
	Company	BPO Deal	Provider	Environment		Dimension of mismatch	Severity	Description	
10	x	x	-	x	I	Deal	High	First invoice revealed catastrophic contract design leading to higher costs than expected for a service level below expectations	Extension (after contract termination & renegotiation)
14	-	x	x	-	III	Provider	Medium	By the end of the initial contract the provider had not gathered further customers for that HR service → no potential for improvement from others / economies of scale	Provider change

**Table 5: Exemplary cases with stimulation events triggered by a mismatch of expectations with status quo**

In Case 10, the outsourcing company had set explicit expectations in the dimensions a, b, and d prior to signing the contract. This case demonstrates that in some cases even a severe stimulation event might not be able to break the path dependence of a BPO deal – in this case, the inertia was created due to a very high upfront investment of the outsourcing company. The mismatch of expectations regarding ongoing costs and service levels with the status quo triggered a severe stimulation event in Phase I. The company finally decided to terminate and renegotiate the contract with the current service provider. Thus, the client returned to a path where the initial expectations could be met. However, the stimulation event was not significant enough to break the path completely, i.e. to enter a new arrangement.

In Case 14, the company was the first client of the service provider in the area of HR outsourcing. In order to benefit from the experience of the service provider, the client assumed that the service provider would manage to attract further clients and, thus, be able to improve the efficiency of all processes. These expectations were not met at the end of the contract in Phase III which triggered the un-locking of the path and lead to a provider change.

## **5. DISCUSSION**

The proposed framework which has been developed as a first result of our study will be further analyzed and refined in the remainder of the study. These initial results of the study indicate a high level of path dependence according to the definition of Sydow, Schreyoegg and Koch (2009) within the context of BPO decision making. However, the collected data will be further analyzed with process-theoretic methods and a strong focus on event-analysis as described by Poole et al. (2000) in order to reveal and describe the underlying mechanisms of change in BPO paths.

The proposed model confirms the existence of path dependence in the context of BPO decision making and deepens the understanding on un-locking path dependencies by offering a framework based on the emergence and impact of stimulation events. In this framework, path dependence theory has been linked to theory of human decision making which highlights two notions. First, client organizations are not seeking for an optimal outcome regarding their BPO relationships. Thus, they can be attributed as satisfiers rather than optimizers (Simon 1957). Second, instead of making the necessary investments for reaching initial expectations, client organizations rather negotiate and update their conditions in their BPO deals in order to partially re-justify the initial decision. This behavior can be interpreted as a first evidence of a high level of transaction costs which is the actual reason for the lock-in effect. Monitoring and updating the delivery of the contract as well as potentially looking for a new vendor causes transaction costs that organizations seek to avoid. Accordingly, rather than enforcing the fulfillment of prior expectations through radical responses, like a provider change or back-sourcing initiative, organizations tend to adjust their expectations. This phenomenon needs to be further explored.

Practical implications accrue for both, the client and the vendor side. Client organizations which have signed or intend to sign a BPO deal are advised explicitly set and document their expectations regarding the contract. Furthermore, they are well advised to incorporate early contract termination clauses in case the pre-defined goals are not met. An active management of the expectations and the BPO relationship is recommended in order to avoid the negative consequences of the reported lock-in effects.

Vendor organizations are advised to actively manage the client's organizations expectations pro-actively as well. Especially, vendors need to develop a deeper understanding of stimulation events as well as procedures for their early detection. In case the crisis is inevitable, vendor organizations shall possess reconciliation practices that help to avoid or overcome relational trauma in such situations (see also Willcocks, Kern and Van Heck, 2002). Altogether, a vendor study could facilitate the detection of successful path management techniques.

## **6. TENTATIVE CONCLUSIONS AND OUTLOOK**

In summary, our study has made the attempt to provide a process-theoretic perspective on BPO which confirms significant path dependencies for BPO clients. These dependencies are caused by high upfront investments in BPO deals, direct increasing returns throughout the life-cycle of a BPO contract ("learning effects"), fulfilled expectations, lowered or adapted expectations or imprecise monitoring of the status quo in a BPO relationship.

The presented model indicates the provenience of expectations gaps, the different phases and goals throughout the BPO phases, as well as ongoing comparisons of the status quo against

the pre-set expectations. The model describes how BPO paths may be un-locked or how expectations may be lowered in order to follow the pre-defined path.

The final conclusion is simple but decisive. Only those client organizations that have maintained a positive attitude towards BPO throughout the relationship and whose initial or adjusted expectations have been met are likely to extend the contract with their service provider(s).

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