IT Outsourcing Evolution – Past, Present, and Future

By Jae-Nam Lee, Minh Q.Huynh, Ron Chi-Wai Kwok, and Shih-Ming Pi
Communications of the ACM May 2003/Vol.46 No. 5 Pp. 84-89

Summary of the paper

IT outsourcing has evolved from the days of service bureaus providing services and facilities management to software support, integration and to the present days of total solutions management.

Early 70's saw organizations outsourcing IT and programming projects on a contract basis to corporations specializing in providing such services and who owned the expensive hardware and support systems required for such purpose. Later on, with the development of low-cost computing machinery, organizations began doing their IT related work in-house. In the 1990s, with the rapid growth in the computer networking arena, IT outsourcing resurfaced again, this time to address the need for specialized services for network management, distributed systems integration, system support and application development. Outsourcing contractors began providing total solutions to the organizations’ IT needs. Experts from the outsourcing companies were routinely deployed at client locations and onsite work contributed to a major chunk of outsourcing revenues. With the software systems becoming increasingly complex, there has been growing demand in expertise for software systems integration.

In the early days, outsourcing decisions were two fold – ‘make ’or ‘buy’. A big factor that influenced the outsourcing decisions was the motivation to outsource. When could outsourcing result in significant cost-reduction and better fulfillment of organizations' needs?

With time, outsourcing became an essential part in the IT framework. The dominant question became not the issue of whether to outsource or not, but instead, how much to outsource. Concerns were raised whether to make outsourcing total or selective, have long term outsourcing contracts or limit them to short periods. A main issue with total outsourcing is the organizations’ dependence on the contracting company, the complexities involved with the outsourcing contracts, with having multiple clauses included in them by both parties to secure themselves against unexpected contingencies, possible cost increases and opportunistic behavior on part of the service provider or unjustified demands of the client.

Since it is not possible to identify all elements and issues when writing a contract, a successful outsourcing decision is exemplified by a closer relationship between the clients and the service providers, which nowadays has become to be called partner-based outsourcing. It is more of a relationship based on mutual interests. Since the service provider gets to have a stake in the client business, it becomes even more closely involved with making the outsourcing work well in favor of the client too. Clients on the other hand, by giving the application service provider a financial interest in their business get them to involve more deeply thereby safeguarding their own business interests.

The partner-based alliance in outsourcing is becoming a key factor in contributing to the growth of this industry. Also, it has been shown that outsourcing contractors are now required to have an even deeper understanding of the client processes. IT outsourcing giants like EDS, CSC, Computer Associates have developed expertise in the domains their clients do their business. Many times, IT personnel from the client become a part of the service provider when such partner-based
outsourcing contracts are signed. Typically, these contracts are long-term contracts and are a constant source of revenue to the Application Service Provider (ASP). The client organization in return gets reliable support and can make long term business decisions about their IT outsourcing needs.

Strength

Using Application Service Providers to address the IT needs, organizations leverage benefits in cost, marketing time and effort, being able to access and utilize the technological edge and specialized problem-solving expertise of their partners. The field has come a long way from the early days of outsourcing when clients dictated all aspects (a win-lose strategy as the authors call it) to a more realistic view which is good for both the client and the ASP; it reduces the challenges faced and makes the process comprehensible, smooth, efficient and less problem prone.

Weakness

Having a complete dependence on ASPs to address their IT requirements, businesses expose themselves to failure in IT support if the ASP systems shut down. Such dependence is not advocated for services which are critical for an organization to run its business. Many-a-times, incompatibility between the client systems and the ASP complicates the integration of the two ends.

Interesting Points

The concept of web services highlights the new pattern that is emerging in the field of outsourcing. Application service providers (ASPs) make available a set of services through the web that can be purchased by the clients. This way the ASPs can sell their services to more than one business and recover their cost faster. The benefit to the clients is that even small businesses can take advantage of the IT products they can not afford to develop themselves or incur the cost in outsourcing the operations. This pay-for-use paradigm is gaining wider acceptance in the industry.

When judging the benefits of outsourcing, key areas such as efficiency, cost reduction, user and business satisfaction, and service quality are compared and assessed against a traditional business infrastructure.

Critical Questions

1. When should an organization go for in-house development or when to rely on third party vendors to meet their software requirements?
2. Outsourcing for total systems management runs a big risk of potential loss of control, flexibility, qualified personnel in the subject matter and the risk of being outdone by competition.
3. If outsourcing has been decided as a way of dealing with the IT needs of an organization, a number of issues need to be addressed at this stage and at many subsequent steps in the course of a running contract.
4. With the web services paradigm of offering services, security, privacy, scalability and preservation of intellectual property are known major issues which need to be addressed for each client.