OFFSHORE ACCOUNTING OUTSOURCING: THE CASE OF INDIA

A report by

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Acknowledgments

Executive summary

This report explores the role of trust and control in mitigating risk in global outsourcing of accounting activities. During the 1990s, reductions in cost and increased capacity of telecommunications and computing facilitated the global outsourcing of various business activities offshore to places where the labour supply is both cheap and plentiful. India, Philippines, Sri Lanka and increasingly China, are key locations for this work.[1] The global IT industry has led the development of offshore outsourcing of various processes of software development. Structured activities such as programming, which can be clearly and relatively unambiguously specified, were the first to be outsourced to foreign firms. Activities in other business areas have followed including transaction processing, data input, transcription, and call centres in and outbound. Over time, outsourcing vendors and clients have improved their understanding of how outsourced activities may be undertaken remotely. Inevitably, clients aim to take advantage of labour cost arbitrage, which has led to offshore outsourcing of categories of work previously considered inappropriate. Since the late 1990s this has included more sophisticated accounting functions, beyond simple data input and transactions. However, the offshore outsourcing of accounting presents significant risks through the potential for poor performance and vendor opportunism.

Research on financial services offshore outsourcing has concluded that moving various activities to foreign locations can contribute to risk of undermining market confidence, of increasing financial crime and of harming consumer protection. The main problem identified is the complexity of achieving suitable management and control from a distance. However, appropriate governance frameworks, risk management systems and controls can identify and mitigate operational risks from offshoring (FSA 2005). What are these controls, risk management systems and governance frameworks and how effective are they in mitigating risks associated with offshore accounting outsourcing?

There have been many codes, standards and regulations such as the Sarbanes-Oxley Act for internal controls (section 302), ISO9000 (quality) and BS7799 (security) standards adopted by some firms with the aim of providing quality assurance and risk mitigation. Some firms have opted to attempt to control risks by opening offshore processing subsidiaries rather than outsource to a vendor. However, there is a danger that focus on compliance shrouds underlying risks, and increased control through ownership in subsidiary operations seems to offer no guarantor against fraud.

Some firms are returning operations to UK. For example in 2006 Powergen decided to bring back 980 call centre jobs from India. Abbey closed its call centres in India after customers reported dissatisfaction with the bank's 1,000 seat call centre in Bangalore. Furthermore, there have been numerous cases of financial 'scams' where Indian workers have supplied customer data to fraudsters. In 2006, £233,000 was taken from HSBC in a fraud case stemming from a breach of security in India. These are examples of two key risks of offshore outsourcing: opportunism and drop in performance, which may occur as a result of moving work offshore in subsidiary operations or offshore outsourcing.

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[1] *From outsourcing to offshoring*, special report SR5, London: Faculty of Finance and Management, ICAEW, October 2004 contains a review of locations for outsoucing. AT Kearney produce a location attractiveness index, *Offshoring for Long-Term Advantage: The 2007 A.T. Kearney Global Services Location Index*, Chicago: A.T. Kearney, Inc, 2007 available at www.atkearney.com/res/shared/pdf/GSLI¬2007.pdf

This report aims to investigate risks and risk mitigation through controls and/or trust, to facilitate offshore outsourcing.[2] After introducing the topic and the objectives of this study in Chapter 1, we outline the background of global outsourcing in Chapter 2. This chapter combines insights from prior studies on risk and risk mitigation, explains a framework to be used in this study, and highlights the main findings of the study. Chapters 3 to 5 provide detailed empirical findings in the form of three case studies. Data was collected during a period of intensive fieldwork in 2005–6. This included interviews with UK-based clients and vendors in India involved in outsourcing accounting activities offshore. Data was also gathered from discussions with accounting outsourcing experts (consultants, lawyers) in the UK and India. The case studies are used to illustrate how risks are mitigated in offshore outsourcing cases of varying size, complexity and types of accounting activity outsourced. The three case studies are representative of these factors.

The sample, firm names anonymised on request, includes the case study of Alphacorp and BetaCom, which is one of the world's largest examples of offshore accounting outsourcing in terms of firm sizes and volumes. Alphacorp is one of the world's largest petrochemical companies and BetaCom is one of the largest outsourcing vendors which has global centres for accounts processing. The second case study is that of Gowing and IndiBackOffice. Firms such as IndiBackOffice have regional coverage within USA, Europe and/or Asia. The third case study is of a relatively small firm of chartered accountants in North West England, Ardon, and their relationship with Technoaccounts, a small offshore outsourcing vendor operating from Chennai. We describe the case studies and then use the framework to identify how the risks evident in those case studies are mitigated by control and/or trust. The report concludes with the main lessons summarised below:

- A component of effective risk management is a balance of types and different levels of control and/or trust prescriptively related to the nature of the tasks outsourced (eg, see Aron and Singh 2005). But:

  – control can be seen as evolving, influenced by local contextual issues and attitudes; and

  – control and/or trust are shaped by particular historical circumstances.

- Small firms can engage in offshore outsourcing and there is a role for consultants, lawyers and other intermediaries to assist in providing standardised contracts and guidance at a reasonable price. Small firms considering offshore outsourcing should decide a predefined strategic planning goal beyond cost savings prior to offshore outsourcing.

- Guidance and recommendations on appropriate disclosure of offshore outsourcing should be provided. Our interviews revealed that some firms of chartered accountants do not inform their clients that their accounts preparation is outsourced to India.

- Vendors should be cognisant of the imperative for risk mitigation and present clients with a range of controls according to type of work and risk – control preference.

- Clients expecting more than the processing of generic 'rules-based' easily codifiable processes must expect to put a lot of effort into helping vendors 'get it right' supported by open gainsharing contracts. Vendors in turn must feel motivated to welcome, encourage and facilitate client access to form close working partnerships.

[2] Audit cost implications of offshore outsourcing are beyond the scope of this study.

1. Introduction

Offshore outsourcing of various accounting activities is becoming an increasingly attractive option for many companies as a means of gaining access to scarce skills, cutting costs and obtaining competitiveness. Due to the improvements in international telecommunications from the early 1990s, it has become possible for various business activities to be outsourced by clients, particularly in Western Europe and the USA, to vendor firms in foreign locations. Although other countries are involved, India is recognised as a leading location for software, remote customer interaction, data analysis, and importantly for this report, various aspects of accounting. Table 1.1 provides a list of activities which are commonly outsourced to vendors in India.

Table 1.1: Accounting activity outsourced offshore

Order to cash: order management, billing, accounts receivables, cash receipts and application, credit and collections, bank reconciliations.

Purchase to payment: purchase order management, vendor management, cash disbursement, bank reconciliations, contract administration, cost accounting, fixed assets.

Hire to retire: payroll, benefits administration, employee data administration, pension accounting, travel and expense compliance.

Financial reporting: general accounting, consolidation and management reporting, intercompany allocations, activity based costing, reconciliations, project accounting, tax compliance, tax returns.

Compliance and control: cash management, treasury, budgeting, forecasting, regulatory reporting, risk management.[3]

A recent ICAEW report[4] has established the importance of outsourcing, and in particular offshore outsourcing, of parts or all of the accounting function to India and other locations. While documents such as the ICAEW report into offshore outsourcing are a valuable contribution, there is currently sparse in-depth research on the practices and mechanisms involved in managing offshore outsourcing relationships. This report aims to fill the gap and complement prior literature (Wood, Barrar and Jones, 2001; Nicholson, Jones and Espenlaub, 2006).

1.1 Objectives

Prior research has concluded that the main risk of offshore outsourcing is the complexity of achieving suitable management oversight and control from a distance. However, appropriate governance frameworks, risk management systems and controls can identify and mitigate risks (Stanton 2006; FSA, 2005). This statement begs the question of what are the risks for accounting offshore outsourcing? What constitutes suitable management oversight and control from a distance? What are appropriate governance frameworks, risk management systems and controls for offshore outsourcing of accounting activities? This report attempts to answer these questions and provides an inquiry into risk and risk mitigation to facilitate offshore accounting outsourcing.[5] Mitigation includes the visible control mechanisms and less visible social interactions and relationships that underpin

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[3] The list of activities of a vendor – Outsource Partners International (OPI) www.opiglobal.com. OPI were interviewed as part of this research, reported in Nicholson et al. (2006).

[4] *From outsourcing to offshoring,* special report SR5, London: Faculty of Finance and Management, ICAEW, October 2004.

[5] Audit cost implications of offshore outsourcing are beyond the scope of this study.

trust in outsourcing offshore. The study has involved interviews with directors, managers and other staff in three case study organisations involving both the 'client' (in the UK) and the 'vendor' (in India). This research has two specific objectives:

- to identify the risks of offshore outsourcing; and

- to identify the types, role and impact of control and trust in managing risk.

1.2 Case studies

Access to suitable case studies presented a particular problem. As the offshore outsourcing of accounting is a nascent industry, processes and methodologies for some vendor firms were viewed as a source of imitable advantage. The sample consists of three client and vendor couplets, anonymised on request, all of which have all or part of the accounting function undertaken in India. There are other venues in addition to India for offshore outsourcing of accounting work, for example the Philippines and Sri Lanka. We have chosen to focus on vendors with Indian centres as India is currently widely regarded as the most attractive location for offshore outsourcing[6] and, according to the Indian trade association Nasscom,[7] is the leading country in terms of volume of offshore accounting work undertaken for foreign clients. Fieldwork in the UK and India took place in 2005–6 and involved interviews in client and vendor organisations with accountants and senior managers in the UK, Portugal and India. We also attended relevant trade conferences and interviewed specialist consultants and lawyers in the UK and India. In the initial interviews, the focus was on developing a historical reconstruction of events prior to the start of the study. Subsequent meetings concentrated on understanding ongoing challenges related to the control of risks. Secondary material included a wealth of information from corporate websites and internal publications including press releases, and related trade data.

1.2.1 Alphacorp–BetaCom

The first case involves one of the largest examples of offshore accounting outsourcing in terms of firm size and volume. Alphacorp is a global chemicals company, BetaCom is one of the world's largest global accounting outsourcing vendors.

Alphacorp has well-established operations in Europe, North and South America, Australia, Asia and Africa. Revenue turnover in 2005 was over US$200 billion employing over 90,000 staff globally. The accounting department in Alphacorp employs over 4,000 people. The first outsourcing of accounting for Alphacorp was in 1990 when it appointed Sigma, a competitor of BetaCom. In 1996, Alphacorp retained Sigma but handed responsibility for accounting operations across Europe to another major accounting outsourcing firm, Delta, who managed a processing centre in Holland, which handled outsourced work from Germany, Austria, Switzerland, and Belgium. In 2000, Delta established a processing centre in Portugal to cater for the offshored work from other European countries: Spain, France and Portugal. The hub in Holland served Germanic speaking countries and Portugal served the Latin and English speaking countries (UK, Spain, Portugal and France). In 2002, Delta was acquired by BetaCom. In 2004, Sigma and BetaCom began to transfer part of Alphacorp's outsourced accounting to Bangalore where both vendors maintain processing centres. BetaCom investment in India (and Portugal) is wholly owned by BetaCom. BetaCom through acquisition gained the 10-year Alphacorp contract worth approximately US$1 billion. In the first two years after outsourcing, Alphacorp saved approximately US$50 million and over the next eight years expects to save US$200 million. The acquisition of Delta extended BetaCom's industry

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[6] For example *Offshoring for Long-Term Advantage: The 2007 A.T. Kearney Global Services Location Index*, Chicago: A.T. Kearney, Inc, 2006 available at www.atkearney.com/re/shared/pdf/GSLI2007.pdf

[7] Details available at www.nasscom.in/Nasscom/templates/NormalPage.aspx?id=28489

expertise and added to BetaCom's core capabilities in application and IT infrastructure. As a result of the acquisition, BetaCom now supports Alphacorp's European accounting from Holland and Portugal. The centres are currently servicing 11 countries and employ nearly 600 staff, of whom 200 are in Holland, supporting accounting operations throughout Europe. In 2005, BetaCom extended a prior 10-year strategic business transformation services contract with Alphacorp by a further two years. Table 1.2 shows the timeline of events:

Table 1.2: Alphacorp–BetaCom timeline of events

Year	Event
1990	Alphacorp signed the first outsourcing deal with Sigma
1996	Alphacorp signed a 10-year outsourcing deal with Delta
2000	Alphacorp renewed the contract with Delta
2002	BetaCom acquired Delta
2004	BetaCom transfer part of Alphacorp's transactional processing work to BetaCom (India)

The accounting services outsourced from Alphacorp to BetaCom are mainly related to accounting transactional processing work. This includes cash receipts, cash and banking, inter-company accounts payable, fixed assets, yearly expenses, balance sheet accounting reconciliation; bank account reconciliation, the month-end close process, and providing information through general ledger in monthly reporting. Alphacorp still retains customer services, decision-making such as deciding the accounting code, and critical business activities such as collecting accounts receivable from Alphacorp clients, monthly forecasts, planning analysis, business analysis, cash management, policy and reporting. These services are performed by the Alphacorp internal accounting function. BetaCom transferred part of the transaction processing work to India, which included cash and banking, reconciliation of accounts payable to general ledger, fixed assets, and accounts payable such as the processing of invoices and vendor set up. Table 1.3 summarises the tasks being outsourced from Alphacorp to BetaCom and from BetaCom (Portugal) to BetaCom (India).

Table 1.3: Distribution of tasks between client and vendor

Location	Tasks
Alphacorp	Customer services Decision-making such as deciding the accounting code Critical business activities such as collecting accounts receivable from Alphacorp clients, monthly forecasts, planning analysis, business analysis, cash management, policy, closing of books and the reporting.
BetaCom (Portugal)	Cash receipts Cash and banking Inter-company accounts payable Fixed assets Yearly expenses Reconciliation General ledger
BetaCom (India)	Cash and banking Reconciliation of accounts payable to general ledger Accounts payable such as the processing of invoices Vendor set up

1.2.2 Gowing–IndiBackOffice

The second case study is that of Gowing and IndiBackOffice. Although smaller in size and scale than the case study of Alphacorp and BetaCom, a very high proportion of the accounting function (approximately 90%) of Gowing is outsourced to IndiBackOffice. Gowing is a firm in the travel industry. The company has 7,000,000 customers annually and by the end of 2004, employed over 17,000 staff. Gowing UK owns several popular brands for charter package holidays. Gowing faced a crisis of mounting debt and a UK-wide downturn in travel. The resulting financial restructuring plan included cost cutting, a debt-for-equity swap and outsourcing of accounting activities. Gowing engaged in a process of competitive tendering to choose an accounting outsourcing vendor which included a request for information and a proposal. There were at least three companies bidding for the contract. Gowing used an independent consultant to check the strengths and weaknesses of the bidders and a specialist law firm designed the contract. IndiBackOffice was short listed and won the Gowing contract in late 2004.

IndiBackOffice was launched in 2001 and has regional coverage (USA, Europe, and Asia) and several offshore centres in India. IndiBackOffice's group overall revenue in 2005 was in excess of £350 million; its total number of employees exceeds 7000 with approximately 3000 based in India. The company has experienced rapid growth; the number of employees in IndiBackOffice (India) has increased by 50% between 2004 and 2005. Revenue serviced by IndiBackOffice's Indian operations has increased by 45% in the same period. In addition to accounting, IndiBackOffice's services include a range of business and technology consulting across all major business sectors.

Gowing outsource approximately 90% of the accounting function to IndiBackOffice including accounts receivable, accounts payable overheads, accounts payable overseas, general ledger, principal ledger, financial reporting, cash management, applications management and support. (Accounts payable overheads relates to paying UK suppliers' rent and rates; and accounts payable overseas relates to paying overseas suppliers and hoteliers.) Principal ledger is a process which manages the relationship between Gowing and tour operators. IndiBackOffice sends part of the Gowing accounting to its offshore centre in Chennai, India – hereafter referred to as IndiBackOffice (India). This includes the transactional processing, accounts payable, accounts receivable, payroll, and business expenses, as well as financial reporting.

1.2.3 Ardon–Technoaccounts

The third case study is of Ardon, a relatively small firm of chartered accountants in North West England, and their relationship with Technoaccounts, a localised provider also based in Chennai, India. In 2006 Ardon had an approximate revenue turnover of £600,000, and 10 employees, three of whom were part time. Offshore outsourcing began in 1999 with a Mumbai-based firm, Globalcom, followed with a shift to UK-based homeworkers in 2002. The current relationship with Technoaccounts began in 2002. Outsourcing at Ardon has been followed since 2001 including two phases of offshore outsourcing: (1) outsourcing offshore to Globalcom (Mumbai, India) and (2) outsourcing offshore to Technoaccounts. Most emphasis is given to the latter period. Table 1.4 shows the evolution of the firm's outsourcing strategy over time.

Table 1.4: Evolution of outsourcing at Ardon

Period	Outsource provision	Reason	Services outsourced
Prior to 1999	In-house		
1999-2002	Globalcom	Cost, staff retention. Recommendation from industry group.	Low priority clients
2002	In-house – home workers	Stopped using GlobalCom after errors. Greater control and proximity of home workers.	All client work
2005	Techno-accounts	Home workers were unreliable. Cost. Technoaccounts promised greater control.	All client work

The decision by Ardon to outsource to Technoaccounts was taken in April 2005 and was ongoing at the end of our study in 2006. Technoaccounts was established in Chennai, India in February 2002 and is a joint venture between Indian businessmen but there is some equity ownership by a UK accounting firm. Currently, Technoaccounts has its operations in Chennai, India. When we visited Technoaccounts offices we found them to be in a busy Chennai street, offices were plain and basic and staff work in small booths in an open plan office.

Technoaccounts were selected after the director of Ardon attended a conference where he met a number of Technoaccounts clients who had used the service and stated that they were satisfied. This introduction through a trusted network and personal recommendation was enough to provide Ardon with sufficient trust in the competence of Technoaccounts to request a demonstration and subsequently a contract for 250 hours per month of service. This translated into 20 accounting jobs at an average of 12.5 hours in one month. Ardon told us they chose Technoaccounts for four main reasons:

- Consistent output to the same standard every time.

- Technoaccounts offer a fully-computerised system which would remove the need for any analogue processing (sending documents physically by courier).

- Data stayed in the UK. It was scanned and transferred to India electronically.

- Technoaccounts would be able to 'access India's massive labour pool' and thus Ardon could grow alongside Technoaccounts.

1.3 Report structure

In the following chapter, we outline the risks of offshore outsourcing of accounting. Subsequently, we identify how the risks evident in the cases are mitigated by certain controls and/or trust. The case studies illustrate how risks are mitigated in offshore outsourcing cases of different size, complexity and types of accounting activity outsourced. Chapter 3 presents the detailed case study of Alphacorp and BetaCom and illustrates how Alphacorp adopt a portfolio of controls to mitigate risks. Chapter 4 presents the case study of Gowing and IndiBackOffice. Chapter 5 presents the case study of Ardon and Technoaccounts. The experiences of Ardon show how small firms with limited resources face difficulties in managing attrition levels and expansion when offshore outsourcing. Finally, in Chapter 6 we provide some conclusions and lessons.

Readers may choose to examine this report from cover to cover. However, the case studies purposely represent a spectrum from small to very large in terms of size of firm, contract value and scope of accounting function outsourced. We would anticipate that all readers would read Chapter 2, and would choose to focus on a particular detailed case of closest relevance to their individual circumstances. Thus, a partner in a firm of small chartered accountants would find the case of Ardon (Chapter 5) of most interest. A medium-sized firm considering outsourcing a high proportion of their accounting function may extract most value from Gowing–IndiBackOffice (Chapter 4). Planners in large firms considering outsourcing may learn most of relevance from Alphacorp–BetaCom (Chapter 3). Naturally, in all instances value may be extracted from all the cases as even a small firm can learn something from Alphacorp–BetaCom and vice versa. We leave this to the discretion of our readers and hope that the experiences reported here will help them achieve success in their own offshore outsourcing endeavours.[8]

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[8] Suppliers of offshore accounting services may be found at www.nasscom.org, www.BPOindia.org or
  www.elance.com.

2. Risk and offshore outsourcing of accounting

Offshore outsourcing involves a relationship in which outside suppliers in another country are used, and in which the hiring company has no direct ownership (Stack and Downing, 2005). There is a growing trend towards offshore outsourcing of accounting activities. General Electric (GE), Dresdner Bank, British Telecom, Ford, American Express, HSBC, Citibank, BP, Standard Chartered, EXL (part of Conseco) and Hewlett Packard among many others, have transferred parts of their accounting function to third-party providers and fully-owned offshore subsidiaries based in India and elsewhere.

The growth of the offshore accounting outsourcing industry in India is rapid. According to India's software and IT-enabled services trade association, Nasscom, in 2001–2, 15,000 people were employed in the Indian accounting sector serving foreign clients generating revenues of US$300 million. Just over 12 months later, 24,000 personnel were employed, generating revenues of US$510 million (Nasscom 2003). In 2005, accounting revenues were US$1.84 billion and 126,000 people were employed, and by 2008, revenue is predicted to reach between US$2.5 and US$3 billion. The substantial wage differentials available in locations such as India are often stated as the major reason for the outsourcing of accounting activities, since for some activities, Indian vendor rates are up to 70% below the salaries of comparable staff in the US or Western Europe. In 2005, based on our own interviews, a monthly salary paid by an Indian vendor for a bookkeeper in Chennai, India, was around Rs10,000 (approximately £140).

Research in financial services offshore outsourcing, such as the PricewaterhouseCoopers (2005) survey of 156 senior executives in financial services, revealed that cost savings are the most significant benefit anticipated from transferring functions overseas, followed by focus on core competences, improved quality of service and strategic flexibility. This same survey provides an indication of the activities being undertaken in foreign locations. Unsurprisingly, in this study transaction processing activities are the most likely to be undertaken in cheaper locations but there is a trend toward outsourcing more sophisticated activities. India's Mphasis is already working on tax returns for US clients and another India-based outsourcing vendor, Evalueserve, refers to its services as 'knowledge process outsourcing' and has involvement in more strategic business research activity for its clients. However, the PricewaterhouseCoopers study reveals that only half of the 156 senior executives surveyed were satisfied with the overall impact of moving the activity or process to an overseas location, with problems including cost over-runs, difficulties in recruiting and retaining staff, and cultural differences between offshore employees and customers. Nearly a third of the PricewaterhouseCoopers survey population experienced an increase in costs after the first year of offshore activity and 15% reported no change in cost base even after five years. Table 2.1 indicates some of the risks identified by the respondents in the PricewaterhouseCoopers study.

Table 2.1: Risks identified by financial services organisations after outsourcing offshore

Finding/attracting people of right quality
Deteriorating quality of service
Cultural differences between home and host markets
Retention of top employees in offshore markets
Rising wages
Political and regulatory risks in offshore location
Changes to taxation, VAT and transfer pricing regimes
Cost over-runs
Inadequate level of compliance and internal control
Impact on management time
Security of intellectual property
Security of client data
Political and regulatory risks in home market
Inadequate communications infrastructure

Source: PricewaterhouseCoopers (2005)

Das and Teng (2001) provide an integrated three-part theoretical framework for the study of risk, control and trust shown in Figure 2.1. Trust and control are inextricably interlinked with risk, defined as the probability and impact of undesirable outcomes. The framework presents the risk of poor performance of an outsourcing vendor (performance risk) or a breakdown in the relationship (relational risk). These two categories of risk may be reduced (mitigated) by controls of a formal or informal nature; or by goodwill or competence trust. In the sections to follow, we consider risk and progress to discussing the relationship between risk, trust and control.

Figure 2.1: Framework of risk, control and trust
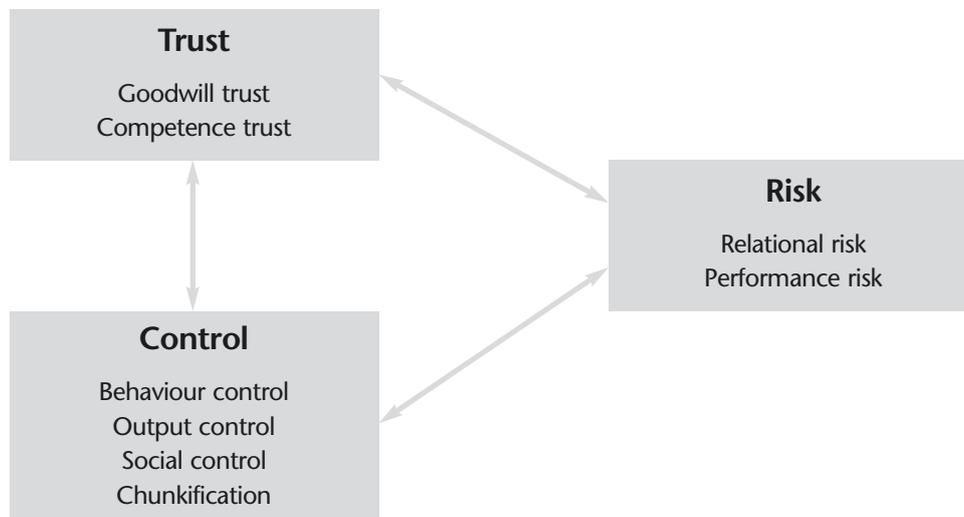
2.1 Risk

2.1.1 Relational risk

Relational risk is, in essence, the risk of a vendor or client not co-operating in good faith; it embraces the probability and consequences of not having satisfactory co-operation in an outsourcing relationship. Opportunistic behaviour such as cheating, shirking, distorting information etc. may be manifested by either vendor or client, or indeed both firms. Prior research provides instances of potential vendor opportunism in offshore outsourcing (Aron and Singh 2005, Aron et al. 2005) as follows:

- Vendors deliberately shirk while claiming full payment.

- Vendors poach proprietary business processes; resell them or use them in direct competition with the client.

- Vendors renege on promises made at commencement and for example stop investing in training of agents; or employ agents who are not as qualified as the agents they presented during negotiations.

- Vendors opportunistically renegotiate contracts after clients have migrated processes taking advantage of the difficulty the client would have in shifting its processes to another vendor or bringing it back in-house (vendor hold up).

Does outsourcing to India present additional relational risks to UK clients?

European firms are restricted by the Data Protection Directive of 1995 with regard to what data can be transferred or stored in countries without equivalent rules and enforcement procedures. India has no such regulations and outsourcing relationships are thus reliant on individual contracts negotiated between the client and the Indian vendor to address the data protection issues. Differences in legal institutions complicate the monitoring of outsourcing contracts where no comparable data protection law exists. Even if a legal case may be prepared, the Indian legal system, although based on the British colonial judiciary, is relatively overburdened and subject to backlog and delay. Other authors have drawn attention to widespread corruption in India suggesting a heightened risk of opportunistic behaviour from vendors (Transparency International, 2006; Varma, 2004). There have been numerous recent instances of highly-publicised security breaches and fraud in Indian call centres (Ahmed 2005). In 2005, former employees of a call centre in Pune, India, were indicted on charges of defrauding four Citibank account holders in New York of US$300,000. They were accused of charming PIN numbers out of customers. Also in 2005, three former employees of Mphasis were charged with collecting and misusing account information from customers they dealt with as part of their work at the call centre. In the same year, a tabloid newspaper journalist bought hundreds of British bank account details from a worker at an Indian call centre. In 2006, a security breach at HSBC's Bangalore facility led to a reported £233,000 being stolen from UK customers as a result of an employee who had passed customer information to fraudsters.

Findings

Client-side interviews across the three case studies indicated the general perception that outsourcing to India-based vendors presents no greater risk of fraud than may be experienced in any other country, including the UK. Some examples of potential relational risks are presented in Table 2.2. Attrition levels in India and endemic poaching of staff between firms present some heightened levels of risk specific to the India context:

Table 2.2: Examples of relational risks

Type of risk	Example
Poaching – Vendors may use information about the client for their own benefit, or develop expertise from the client's operation and transfer it to the client's competitor(s)	BetaCom serves a number of clients in the India centre, presenting potential for opportunistic poaching. BetaCom could use Alphacorp's proprietary processes or staff for another client. Moving staff between clients is an IndiBackOffice practice to provide variety for staff in order to overcome high attrition levels in India. 90% of Gowing's accounting function is undertaken by IndiBackOffice presenting a high risk of poaching. However, many clients see sharing as a benefit as it promotes efficiency and best practice. Clients are content to share when outsourcing back office processes (generic transactions) using common enterprise systems where there is little risk of loss of intellectual property. Experienced staff in India are often poached by other companies in the local cluster presenting the risk of lost knowledge of client processes.
Fraud – A study by Transparency International (2006) reports a high level of corruption in India. No equivalent EU law on data protection or intellectual property currently exists.	In 2005 a newspaper reporter from a tabloid newspaper was able to buy bank account, credit card, passport and driving licence details of UK bank customers from a Delhi-based call centre operative. Although a criminal breach of the Data Protection Act had occurred, UK police had no jurisdiction to prosecute.
Renegotiation – The vendor might act opportunistically during negotiation since, if the client has no alternative, then the client must accept the terms that the vendor offers.	Alphacorp no longer has in-house resources to perform accounting and would face difficulties repatriating processes. Gowing is outsourcing 90% of its accounting function to IndiBackOffice. As the sole supplier of accounting services to Gowing, IndiBackOffice could opportunistically raise prices (vendor hold up). However, exit assurance clauses are an integral part of client contracts and there are many examples of clients changing suppliers limiting the need for Alphacorp to reverse transition.[9] Reverse transition clauses are applied in some contracts.

2.1.2 Performance risk

Performance risk is defined as the probability and consequences that outsourcing objectives are not achieved despite co-operation between partner firms. Performance risk is concerned with the range of factors that may affect the vendor's ability to perform to the outsourcing agreement. Satisfactory performance is dependant on the resources and capabilities of the vendor firm including available capital, technology and the skills of vendor staff. Performance risks are caused by breakdown in operations at the vendor location, resulting not from deliberate opportunistic action, but due to the complexity of operations, geographical separation, cultural differences or limitations of communications equipment.

[9] A reverse transition plan is intended to repatriate client processes back to the client or to another vendor. It should include reverse knowledge transfer, project personnel debriefing and infrastructure decommissioning. The inclusion of such clauses is typically done at contract negotiation phase along with conditions indicating which party should bear the cost.

Does outsourcing to India present additional performance risks to UK offshore outsourcing clients?

Offshore vendors are separated from their clients by substantial geographical distances in areas often prone to natural disasters and geopolitical risks. For instance, floods are common in Mumbai which in 2005 put several Indian outsourcing firms out of operation, including UK Directory Enquiries. The earthquake in Pakistan in 2005 devastated vast swathes of Kashmir and caused the offices of offshore outsourcing vendors to shake violently in Lahore. Transferring accounting to India exposes the client to the potential consequences of such natural disasters and also the potential of a conflict such as between India and Pakistan where there was a resurgence of hostilities in 2001.

Prior research into various aspects of the management of offshore outsourcing indicates that communication between the clients and the offshore vendor may be problematic due to relatively poor telecommunications, cultural differences, accents and language ability. Time-zone differences accentuate these communication difficulties (Sarkar and Sahay, 2004; Walsham, 2002). The offshore personnel may lack domain knowledge in the client's business application, and the transfer of such knowledge is hampered by distance (Cramton, 2001; Nicholson and Sahay, 2004). Differences in infrastructural standards raise issues of reliability of telecommunications connections. Furthermore, there is considerable evidence to suggest that international variation in accounting standards and practices persists (Choi and Levich, 1991; Weetman and Gray, 1991). Gray (1988) notes the consequences on financial reporting practices. Although the level and quality of educational pools in India is high, US or UK GAAP is not widely taught in Indian universities. The potential labour supply risk is overcome by training programmes which equip Indian staff with this knowledge and by repatriation of Indians who qualified in Western Europe and the USA. However, high staff attrition is a characteristic of the Indian offshore outsourcing industry with normal staff turnover rates for transaction processes reported at around 30% per annum and much higher in call centres. Moving activities to India also exposes clients to accentuated risk of potential vendor bankruptcy, merger and acquisition, as the Indian IT-enabled services industry is in an early phase of development characterised by the significant potential for shakeout and consolidation (Mishra, 2005; *The Economist*, 2004).

Findings

Interviewees in Alphacorp perceived there to be no additional relational risk incurred by transferring work to India compared with UK or Portugal but considered there to be additional performance risk. Certain components of the outsourced accounting were served from the Portugal 'hub' to minimise risks arising from such impediments as language, culture and communication and maintain physical proximity. Flight time from UK to Portugal is around two hours as opposed to approximately nine hours to India. The experiences of Ardon show how small firms with limited resources face difficulties in managing attrition levels and expansion. The Ardon vendor in India, Technoaccounts, presents high potential for performance risks because of its small size. Performance risk in Gowing is accentuated compared to Alphacorp as a much greater proportion of accounting work is outsourced that either involves judgement or relatively unstructured tasks that are difficult to objectively codify and measure. Table 2.3 summarises some examples of potential performance risks across the cases.

Table 2.3: Examples of performance risks

Risk	Issue
Communication issues	Lack of ability to communicate clearly in English through emails and telephone caused frequent misunderstanding between the BetaCom Portuguese and Indian staff. Communication between IndiBackOffice (India), Gowing and IndiBackOffice (UK) occurs mainly through email. These were often delayed due to telecommunications infrastructure problems.
Cultural issues	At Alphacorp–BetaCom, public holidays occur at different times across the centres in UK, Portugal and India, presenting a relatively greater number of occasions when maintaining a critical mass of staff may be problematic. The team in BetaCom (India) were described by Portugal-based staff as not engaging in effective 'questioning behaviour' and instead often taking instructions on 'face value' leading to errors. The BetaCom (India) team were perceived by Portugal staff as lacking a 'sense of urgency' because they were not dealing directly with Alphacorp staff.
Knowledge	At the inception of BetaCom outsourcing from Portugal to India, staff who were leaving were unwilling to share information about the process during the transition period. Although processes were documented, training and handover was problematic especially when informal practices were involved which were undocumented. Variation in accounting standards and practices such as tax laws and statutory accounts are different in each country served by BetaCom. While vendor staff built up knowledge of these variations, performance was reduced. Performance of vendors is unlikely to be perfect from day one and should be reflected in key performance indicators.

2.1.3 Mitigating risks

The framework for analysis presents two major forms of risk affecting accounting outsourcing: performance risk and relational risk. Instances of these two categories of risk may be mitigated by implementing controls of a formal or informal nature or by the existence of goodwill or competence trust.

2.2 Control

Control may be understood as a process of regulation and monitoring for the achievement of organisational goals (Das and Teng, 2001). Control can be achieved through governance structures, contractual specifications and other managerial arrangements concerned with controlling the partner and the outsourcing alliance. A summary is given in Table 2.4.

Table 2.4: Examples of control types and mechanisms

Control type	Mechanism
Output control	Setting objectives and performance measures Planning and budgeting Reporting and procedures
Behaviour control	Policies, procedures, Reporting structure Staffing and training Standards
Social control	Participatory decision-making Rituals, ceremonies, networking
Chunkification	Decision on activities allocated to client and vendor Decision on portion or fraction of each activity allocated to client and vendor

Output control consists of control over the outcomes of a process during or at the end. Measures consist of metrics, benchmarks and indicators used to judge desired against actual performance. **Behaviour control** consists of rules, procedures and policies to monitor and reward. **Social controls** are concerned with propagating organisational norms, values, and culture to encourage desirable behaviour. Social control, in contrast with formal output and behaviour control, involves no attempt to specify behaviour or outcome at the start. Goal setting is decentralised and evolves through socialisation and consensus building, allowing members to develop shared views to influence behaviour. **Chunkification** is concerned with dividing any process into separate component activities or chunks that can be outsourced in a manner that reduces the risk relative to that of outsourcing the entire process (Aron et al. 2005 p38). Vertical chunkification describes which activities will be allocated to the client and vendor or multiple vendors. Horizontal chunkification describes what portion or fraction of an activity will be allocated to client and vendor(s).

Prior research indicates that the choice of controls depends on the extent to which tasks can be codified or specified in an exact and precise manner and whether the measurement of the outputs can be precise and objective (Das and Teng, 2001; Aron and Singh, 2005; Aron et al. 2005). Codifiability is essentially the ability of an organisation to codify its work according to pre-set rules. If it is possible to systematically describe each situation and stipulate precisely what employee responses should be in each scenario then according to Aron and Singh (2005) 'people anywhere in the world can do the job for them' (p138). Potential for measurement refers to the ability to measure outputs in a precise and objective manner. Das and Teng differentiate between metrics to measure outputs and those that measure the behaviour of the vendor's agents during the process. They posit that output control is appropriate in situations where outputs are measurable and may be used for control where codifying work is difficult. Such metrics may include tolerance limits for errors and completion times. Process (behaviour) control, such as policies and procedures, reporting structures and training, works best in situations where work is codifiable but outputs are not easily measurable. Where work is not codifiable and outputs are difficult to measure, social control is appropriate because it provides the ability for measurement to be avoided at the beginning but still allows control of the group members.

Findings

Table 2.5 below shows the governance structures in the two large firm cases.

Table 2.5: Governance structures at Alphacorp–BetaCom and Gowing–IndiBackOffice

Contract	Alphacorp's contract with BetaCom is based on open book gain-sharing. The contract has a baseline cost, the cost that Alphacorp would have to pay to BetaCom and the gain above the cost will be shared in the proportion agreed in the contract. Similarly, Gowing's contract with IndiBackOffice is based on an open book arrangement. Gowing and IndiBackOffice set the target price in advance and share variances and incentives.
Meetings	Governance meetings at Alphacorp–BetaCom and Gowing–IndiBackOffice consist of three levels: operational, middle and highest management level. The meetings are held jointly between client and vendor staff at appropriate levels of decision-making.
Participatory decision-making	Participatory decision-making at Gowing–IndiBackOffice is used to deter both client and vendors from acting opportunistically and reduce performance risk as it encourages both sides to concur on reasonable and achievable targets.

2.2.1 Behavioural and output control

Formal agreement on service levels, staffing, and training are behavioural control mechanisms used at Alphacorp–BetaCom and Gowing–IndiBackOffice. There is no direct reporting from BetaCom (India) to Alphacorp as Portugal acts as the communication conduit between vendor and client. The reporting structure in Gowing–IndiBackOffice is relatively informal. IndiBackOffice (India) staff communicate directly with Gowing. Both Alphacorp and Gowing impose output controls through a suite of key performance indicators (KPIs). Ardon, as a small company is reliant on vendor side controls and its own internal checks to establish control over vendor output. Table 2.6 lists examples of behavioural and output controls at Alphacorp and BetaCom.

Table 2.6: Behavioural and output control at Alphacorp–BetaCom

Behavioural control
Staffing and training – Alphacorp has involvement in the recruitment of vendor's staff and can access personnel files. Alphacorp can ask BetaCom to remove any staff member. Non-disclosure agreements are signed by all vendor staff.
Physical and systems security – physical security includes the use of security cameras, mobile phone detection, and clean desk policy. System security includes creation, validation, maintenance of identity cards, firewall and anti-virus system in accordance with BS7799.
Audit – an external audit and Sarbanes-Oxley audit (for USA) is performed by Alphacorp's external auditors at both Portugal and India sites.
Internal control manual – a formalised code of practice manual providing guidance on how tasks should be completed. There are semi-annual assessments against the internal control performed in both BetaCom (Portugal) and BetaCom (India) to report evidence of the control.

Table 2.6: Behavioural and output control at Alphacorp–BetaCom continued

Output control
Service level agreement (SLA)[10] – indicates the measures of BetaCom's performance and Alphacorp's expectations.
Key performance indicators (KPI) – Alphacorp examines a suite of KPI metrics such as number of invoices to identify related problems or issues.

2.2.2 Social control

An example of social control is 'silent running' used in the Alphacorp–BetaCom case study. Silent running was described as 'an idealised state where there are no complaints or problems, or the desirable state of operating silently'. Thus, silent running is the desirable outcome and effectiveness test of output and behaviour controls. However, by constantly responding to client needs, complaints and feedback ('noise') and making necessary adjustments, the vendor becomes attuned to the client and the process over time enables convergence of goals, procedures and work culture (social control). The process of escalation of issues from the operational up to higher levels enables the rectification of problems to be addressed at strategic levels as necessary also contributing to convergence. The Gowing case study demonstrates a further technique for social control involving the mediation provided by a middle person. The Gowing contract manager made a concerted effort to monitor the work of BetaCom and inculcate shared goals across the two firms. This was facilitated by frequent telephone communication and regular visits to India to monitor the outsourced process and to work informally with vendor staff. The third major mechanism of social control involved strategic decisions for seconded senior client staff to be actively involved in management roles within the vendor firm while remaining formally employed by the client. One Alphacorp staff member was in overall charge of the Portugal centre and the effect of this was to mitigate relational risk. The manager and other seconded staff maintained client employment status and obligation to best serve the interests of Alphacorp. These staff would also bridge the gap in managing the tensions of conflicting goals and aims across the client and vendor firms. They thus acted in a similar capacity to the middle person contract manager at Gowing but were employed in a formal seconded capacity. An unexpected consequence of this was that one senior seconded staff member was regarded by client-side colleagues as defensive and protective of the vendor when faced with criticism from her colleagues in the client firm. Table 2.7 summarises social control practices across the cases.

Table 2.7: Social control practices

In Alphacorp–BetaCom, silent running is used to formally record problems or issues within the process requiring resolution. If there is no noise (complaint), silent running has been achieved. Several key secondments of senior staff from the client firm included the most senior manager of the BetaCom (Portugal) centre.
In Gowing–IndiBackOffice, the contract manager of Gowing plays a major role in mitigating relational and performance risks. This person interpreted the open book contract as enabling full access to the outsourced processes and she would actively seek out problems and engage wherever appropriate in the process in IndiBackOffice (India) or the UK. Control measures include regular phone calls to the UK and India and regular quarterly visits to IndiBackOffice (India). She communicates directly with the team in India, working together with them on improving the process and solving problems faced by the teams across locations. Her actions were initially perceived

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[10] SLA is a formal part of the contract which typically will specify the measures for availability and performance and other attributes of the service. It also typically includes penalties in case of SLA violation.

by IndiBackOffice staff as 'performing out of the scope of her role as a contract manager' and attempts were made to restrict Gowing access to IndiBackOffice. This position was revised when it was realised that this person's knowledge of IndiBackOffice's process and political position in Gowing facilitated problem resolution.

2.2.3 Chunkification

Alphacorp determines the scope and the type of accounting outsourced to Portugal and India. Tasks that cannot be codified are not outsourced. Chunkification across the cases is shown to operate between hubs, these being BetaCom (Portugal) – BetaCom (India), and IndiBackOffice (UK) – IndiBackOffice (India). Hubs mitigate the communication, language and cultural risks through skills, institutions and infrastructure in the hub location. Vertical chunkification describes which activities will be allocated to the client and vendor or multiple vendors. Alphacorp outsource to BetaCom and one other major vendor. Ardon has relatively smaller needs in terms of volume, scope and the type of work outsourced to India. Only 'straightforward' accounting work is outsourced ie, that which would generate a minimal number of queries from the vendor staff in India. 'Client facing' activity (consultancy) is the other major category of work not outsourced. Table 2.8 presents examples of chunkification at Alphacorp–BetaCom.

Table 2.8: Chunkification at Alphacorp–BetaCom

Horizontal chunkification
BetaCom (Portugal) is an example of near shore outsourcing as Portugal is physically closer to the UK than India so travel is easier for alleviating any problems such as language capability of staff. Furthermore, Portugal is a data 'safe harbour', within EU and is subject to EU data protection legislation.
Vertical chunkification
Alphacorp maintain a second vendor ('dual sourcing'), which enables performance comparison and acts as a deterrent to opportunism.

2.3 Trust

The third dimension of the framework is trust, which may be understood as positive expectations in a risky situation (Das and Teng 2001). Two major types of trust are identified: competence and goodwill trust (Table 2.9).

Table 2.9: Mechanisms of trust

Trust type	Mechanism
Competence trust	Direct communication Networking with other firms
Goodwill trust	Institutions (ICAEW membership, Sarbanes-Oxley) Previous relationships

Positive expectations regarding goodwill and the competence of a vendor can act to reduce the perceived risks in an outsourcing relationship. Goodwill trust is concerned with a partner's positive intentions and integrity, and if present, may act to reduce the likelihood of opportunism. However, Das and Teng point out that goodwill trust has little or no impact on performance risk as sources of such risk lie in appropriate resources or industry competition, neither of which is affected by goodwill trust. Competence trust is based upon the various resources and capabilities of the firm. Resources may include capital, human resources, physical properties, market power and technology, and it is

these resources and capabilities that provide the basis for the competence or expertise that is needed in alliances (Das and Teng, 2001 p258). A reputation for competence is tantamount to low performance risk. Competence trust founded on experience or reputation, may provide a firm with sufficient confidence to outsource even the highest performance risk activities offshore such as cash forecasting or other activities involving analysis and judgement. However, Das and Teng point out that competence trust does not act to reduce relational risk, being concerned only with the **ability to do appropriate things** and not the **intention to do so**. Indeed, a competent firm may choose to act opportunistically. The institutional bases of trust that are indicative of competence include those Sarbanes-Oxley, codes of professional ethics, ISO9000, EU data protection directives and compliance with FSA regulations. This may impact on relational risk as opportunism is less likely if partners are in the same professional body, due to reputation effects and potential for disciplinary action.

Das and Teng (2001) discuss how formal control of outputs and behaviour, if considered excessive, may be to the detriment of goodwill trust. Close monitoring of behaviour and/or outputs may generate tension, making partners sceptical of each other's intention and compromising competence trust. Social control, in contrast, may boost goodwill and competence trust as the partners influence each other's behaviour through frequent meetings and communications, culture blending, and socialisation (p264) and develop shared norms, a step that indicates the partner's competence is trusted. Thus, a client's trust in a vendor's goodwill and competence impact on the effectiveness of control.

Findings

We observed the building of goodwill trust to reduce the likelihood of opportunism and the building of competence trust to reduce performance risk. This trust was manifested in the Ardon director's friendship with the Technoaccounts director and the pair exchanged regular conversations on the telephone. He told us that he believed that the Technoaccounts director was 'basically honest' and had integrity. The Ardon director even considered investing in Technoaccounts as he believed that the company was robust and likely to generate returns. Small firms often have limited resources to engage in extensive control. The Ardon director had a high level of goodwill trust in the Technoaccounts director which mitigated relational and performance risk and, while there was also a high level of competence trust, this was reducing as Technoaccounts had reneged on certain promises. Table 2.10 explains more about Ardon's reliance on trust.

Table 2.10: Small firm outsourcing practices at Ardon–Technoaccounts

- In 2006, Ardon was a relative veteran of offshore outsourcing having outsourced to India since late 90s and was cognisant of some of the risks (eg, data loss, natural disaster).

- Contact costs and performance risks were mitigated by recommendations of existing users enabling competence trust. Potential for vendor opportunism was mitigated by goodwill trust expressed in the growing friendship between the directors and regular informal communication between staff in both firms. Ardon did not have the resources to engage in a full due diligence process or engage in extensive India travel, risk analysis and tendering as in the large firm examples.

- Technoaccounts provided labour, standardised service and used IT effectively to reduce client-side control costs to a minimum. They have enabled Ardon to overcome skills shortages; focus on core competences with their clients and freeze price increases.

Table 2.10: Small firm outsourcing practices at Ardon–Technoaccounts continued

- Technoaccounts are subject to difficulties common to all small firms. The problem of high staff attrition in India impacted Ardon in the high number of queries and problems derived from lack of consistent Technoaccounts personnel. Technoaccounts reneged on promises as they struggled to cope with rapid growth and the tensions of staff attrition.

- The cost savings of Indian offshore outsourcing were not greater than could be achieved with outsourcing to a UK firm, which can be explained by the relatively low volume of outsourced transactions.

2.4 Summary of the chapter

This chapter has set up the conceptual tools to be used in relation to the case studies to be described and analysed in subsequent chapters. Illustrative examples from the cases to follow have been included to provide an introduction to the concepts and set the scene for the detailed cases.

3. Alphacorp and BetaCom

This chapter presents the case study of Alphacorp and BetaCom. It illustrates how Alphacorp, one of the world's largest firms, has pioneered large-scale offshore accounting outsourcing. The arrangement is operating between the vendor's 'hub' locations, these being in Oporto, Portugal and Bangalore, India. We discuss risks and their mitigation through output, behavioural and social controls. The chapter starts with consideration of the issues of governance, followed by risks analysis and ends with the control and trust used by Alphacorp–BetaCom to mitigate these risks.

3.1 Governance

3.1.1 Contract

The contract between Alphacorp and BetaCom involves open book gain sharing, which is based on operating cost reimbursement and sharing of savings against an agreed baseline. The baseline cost is the pre-contract cost incurred by Alphacorp for the contracted services. Any differences between actual BetaCom costs and baseline costs (savings) are shared between Alphacorp and BetaCom in the proportion agreed in the contract. BetaCom achieves a margin by supplying services below baseline cost, generally by improving processes, and by optimising the use of lower cost locations. The contract with Alphacorp states that BetaCom must pursue process improvements and cost reductions. In other words, the gain-sharing contract commits both client and vendor to continuous improvement, with both partners sharing in the cost savings. One example is BetaCom's implementation of imaging and workflow technologies, which result in faster entry of invoice details and a significant resource reduction.

The Alphacorp contract manager told us that the spirit of the contract between Alphacorp and BetaCom rests on a mutually beneficial commercial relationship, which is continually driving cost down and improving quality. He believes the contract motivates BetaCom to perform, manage, and deliver accordingly. Two quotes below summarise his views:

> 'I think the main protection is the contract, and the behaviour in the relationship that's inherent in that contract. If you have a contract that you're comfortable is going to work, incentivises the right sort of behaviour and contributes to a win-win partnership behaviour it's hard to go wrong if you're devoted partners.'

> 'The essence of the deal is to share savings between the partners based on the extent to which the actual vendor costs come in below the baseline. The baseline represents the cost of the outsourced activities immediately prior to the contract commencement. This mechanism was designed to ensure that both parties profited from lower operating costs (lower revenues to the vendor but higher profit) and that the right behaviours would be incentivised. Previous contracts with a mark up margin based on revenue had incentivised the vendor to increase revenue in order to increase margin and in the absence of an effective gain share mechanism Alphacorp costs would not come down. The relationship is based on performance and performance is based on-year-on year lower costs, improving quality and a sound control environment.' Contract manager, Alphacorp.

3.1.2 Organisation structure

The organisation structure of Alphacorp and BetaCom is based on the three-tier architecture shown in Figure 3.1.

Figure 3.1: Three-tier architecture of BetaCom

The first tier (T1) consists of regional groups such as the European group, Americas group, Australasian group, South African group, and other groups around the world. T1 refers to BetaCom staff co-located with Alphacorp which is rarely practiced. The second tier (T2) is a series of European centres in relatively low cost locations where the required qualified resources (especially language skills) are available. In this case, T2 refers to BetaCom (Portugal), which performs transactional accounting processing for Alphacorp in the UK, Spain, Portugal, and France. Since the transition of work to the India centre, the role of Portugal has gradually changed to co-ordination of the India centre and managing the relationship with Alphacorp. Portugal staff review and control the quality of work from India before delivering it to Alphacorp. The third tier (T3) consists of the 'global location', and the focus is India. T3 is a cost centre, and their staff do not interact directly with the client although this is changing as a greater amount of English language work from Alphacorp is being sent directly to India, thus bypassing tier 2. The communication between the staff in each tier is mainly through emails and telephone as well as via the in-house designed document management system (DMS). BetaCom has adopted the client accounting systems including SUN, SAP Financials and ORACLE release 11.

3.1.3 Meetings

> 'Our governance model is the most important part of the relationship. It ensures that at each level there are conversations, supported by relevant data, with knowledgeable people from both parties present. The escalation rules are a way of ensuring that issues are dealt with promptly and the data is to ensure that facts can be agreed between the parties.'
> Contract manager, Alphacorp.

The top-level governance committee is the joint review group (JRG), which deals with strategic issues escalated from the lower level committees. Overall, this level of governance is designed to assess whether the overall relationship delivers against expectations. The European operation network (EON) is the second level governance group and is focussed on the level of contract across all countries of operation considering service quality, control environment, and budgets as well as escalations from the in country day-to-day activities. The EON takes guidance and occasionally instruction from the JRG. The operational level of governance is concerned with the day-to-day issues. The day-to-day interaction between client and vendor is through telephone, email, or visits to Alphacorp centres.

Governance meetings at the three levels (JRG, EON and operational level) are maintained as physically co-present and face-to-face, rather than mediated by technology such as video conferencing. Thus representatives travel from each location for the EON and JRG and there is regular travel of Portugal-based staff for operational level meetings with Alphacorp. As well as language ability, proximity to the client is a major reason for the continued existence of the Portugal hub.

3.2 Risks

3.2.1 Relational risks

The potential for opportunism in this case is significant involving potential for poaching of systems, poaching of staff, fraud and renegotiation. Some of the material discussed

below concerns the transition stage of outsourcing. We indicate this where appropriate, as events at that stage do not reflect normal ongoing business in India. Rather, they reflect a transition phase where issues were expected and were managed with extra monitoring and staff.

Poaching of systems or processes

When outsourcing, there is potential for opportunism where the vendor may use information about the clients for their own benefit. An interviewee in Portugal highlighted the possibilities of using Alphacorp's systems or processes for vendor promotion to new clients:

> 'If the next big oil company comes to us then we will be able to say "well actually we do this for GlobalOil, we do this for Alphacorp, it may well be you want something similar."' Service manager, BetaCom (Portugal).

Aron et al. (2005) indicate the possibility that vendors could act opportunistically by developing expertise from the client's operation and transferring it to the client's competitor(s). It was observed that BetaCom (India) serves a number of clients in the same building, thus presenting potential for opportunistic poaching. Alphacorp's contract manager told us:

> 'Our expectation is that we would be acting in a way that's to our mutual advantage and BetaCom would find itself in some very difficult conversations if it were dealing with other clients to our cost.' Contract manager, Alphacorp.

Interviewees on both sides of the relationship stressed that Alphacorp has outsourced only 'back office' transactional activity which tends to be of a generic nature offering little in the way of competitive advantage if copied. Clients are often happy with the arrangement in offshore centres if it allows the vendor to increase scale and reduce fixed cost allocations to the client so long as only generic process is shared where no discernable competitive advantage will be gained or lost. Many multinationals are using common ERP platforms such as SAP with little difference between the back office processes across users.

Poaching of staff

High attrition level of staff in India, monotonous work and limited career development could contribute to the potential for opportunistic poaching of staff. Several BetaCom interviewees confirmed the attrition level in India as 14% per annum, with the industry average being 35% to 40%. Several interviewees told us that the work is monotonous as it focuses only on specific processing activities that over time, becomes 'unexciting' to the staff, and presents no challenge to those with MBA or bachelors degrees, a typical level of attainment of BetaCom staff on Alphacorp accounts. Several interviewees reported their views of this:

> 'You cannot expect people doing the same job for 15 years even if they do the highest of jobs in the value chain. They are not going to stay.' Finance manager, BetaCom (India).

> 'It's a high turnover industry. We have a lot of other competing processing firms around this place and so, it is a challenge to keep people motivated here. You have people who are doing MBA finance, doing the same kind of role as people who have a bachelor in communication. The level of interest in that particular role is different. There is some monotony in the whole process so you need to keep the employees motivated.' Human resource executive, BetaCom (India).

A common strategy is moving staff around to different accounts to keep the work varied. However, key BetaCom employees on Alphacorp accounts cannot be transferred to other contracts without the prior agreement of the Alphacorp contract manager (which is not unreasonably withheld). High staff turnover introduces quality issues because staff have to be hired and trained which presents a time lag before performance is achieved. We were told:

> 'If we lost any of our nominated key people because they (BetaCom) put them on somebody else's account without first getting my agreement then that would be a breach of the contract.' Contract manager, Alphacorp.

Limited career development in accounting outsourcing contributes to job dissatisfaction and frustration among India-based employees, thus encouraging them to look for better job offers from other companies. The staff might act opportunistically by moving from one firm to another or may be headhunted by other companies offering better opportunities. The Alphacorp contract manager raised his concern at this saying:

> 'We don't want to be the training resource for our future competitors but it happens and we have to be confident that BetaCom is managing its staff so that we don't have an excessive staff turnover.' Contract manager, Alphacorp.

Fraud

BetaCom transferring part of Alphacorp transactional processing work to India may have added to the risk of fraud. India has been reported as having a relatively high level of corruption and no equivalent law to the UK on data protection. Additionally, some security experts suggest that low paid labour may be more likely to engage in corrupt activities (BBC News, 2005). However, the Alphacorp contract manager felt that India presented no greater risk than anywhere else:

> 'In developing countries the need for a job is far stronger than the need for a job in the UK and therefore the temptation to break the law and risk losing your job is probably less. I don't think that living and working in a developing country really makes a difference to people's honesty and integrity.' Contract manager, Alphacorp.

The operation manager in BetaCom (India) also took the same view as the Alphacorp contract manager, believing that India presents no heightened risk:

> 'I don't think the risk will be any greater since you are dealing with people, you are susceptible to fraud in India, and you are susceptible to fraud in Portugal, or the UK or Bangkok or anywhere.' Operation manager, BetaCom (India).

Low levels of perceived risk can be attributed to chunkification. The contract manager is careful to ensure that only transactions offering limited potential for relational or performance risk are outsourced.

Renegotiation

If there are few qualified suppliers in the industry, the vendor might act opportunistically during negotiations since if the client has no alternative, then the client must accept the terms that the vendor offers (Aron et al. 2005 p43). It was mentioned by one of the interviewees in BetaCom (Portugal) that Alphacorp no longer has in-house resources to perform accounting work.

> 'Transactional accounting has been outsourced for such a long time now. Alphacorp would have difficulty manning the project with in-house resources because the in-house resources no longer have knowledge of what accounting is required.' Project manager, BetaCom (Portugal).

Back office processes such as those outsourced to BetaCom can be relatively easily transferred between suppliers due to generic processes and a large number of qualified suppliers. Thus, although the work would be unlikely to be 'insourced' back into Alphacorp, the potential for opportunistic vendor renegotiation is limited in such scenarios.

3.2.2 Performance risk

Several performance risks are identified in this relationship between Alphacorp and BetaCom (Portugal).

Communication

Although English is the de facto internal language of BetaCom, it is not the first language for staff in India or Portugal. Interviewees reported that they experience difficulty in communicating in English when using email and the telephone. This problem often causes misunderstanding, and delays the process, as one Portugal-based executive stated:

> 'We have some language problems. Sometimes it's difficult for them [Indian team] to understand me, and sometimes I have difficulty in understanding their accents. We speak English but it's not our first language.' Customer service executive, BetaCom (Portugal).

The level of our Portugal-based interviewees' English was clearly apparent during the interviews and it became clear that not all of the BetaCom (Portugal) employees were fully competent in English. We were also informed that they could not express their knowledge or explain instructions clearly to the team in India. At the same time, these interviewees complained that the team in India was not competent in English, French, Dutch, Spanish, or Portuguese, and thus had difficulty understanding instructions or explanations from the Portugal team. One of the interviewees in BetaCom (India) explained:

> 'People in Portugal do not know English very well. There might have been some miscommunication on the way they [team in Portugal] express things and what we [team in India] think.' Team leader, BetaCom (India).

A further complexity concerned public holidays which are at different times in the UK, Portugal, and India. Although the office in Portugal works to the UK schedule, festival periods in India present bottlenecks at holiday periods. During these times, the number of people working on a given process in India would be reduced.

> 'There was an agreement that there has to be one person in India during holidays there. We always ensure that there was a minimum of service that needs to be provided.' Customer service executive, BetaCom (Portugal).

The importance of infrastructure to support the communication process between BetaCom (Portugal) and BetaCom (India) was also highlighted. An interviewee in Portugal told us of problems where emails from India were occasionally 'trapped' in a server in another country and a delay of an urgent payment to an Alphacorp supplier occurred as a result:

> 'The communication problems took a long time to iron out and if a payment instruction to Bangalore is urgent, you can't wait for six hours…' Project manager, BetaCom (Portugal).

Such difficulties are overshadowed by the reported problems during initial set up where there were significant difficulties in arranging for telecommunications links to be established. Even for a global firm such as BetaCom, we were told:

> 'It took significantly longer and incurred more executive effort than expected to establish effective telecommunications and far beyond the norm in USA'. Senior manager, BetaCom.

Differences in business practice and non-standardised input

Previous studies (Gray, 1988; Choi and Levich, 1991; Weetman and Gray, 1991) have emphasised the consequences of variation in accounting standards and practices. In this case, business practices such as tax laws and statutory accounts are not the same in every country served by BetaCom (Portugal), and thus misunderstandings frequently occurred in performing the task at transition contributing to performance risks.

> '…even if the local differences are just the tax laws and the statutory chart of accounts, they have to be applied, because it's statutory and is a legal compliance.' Project manager, BetaCom (Portugal).

BetaCom organises country-based teams for activities such as tax, statutory accounting and general ledger. Other processing teams are cross country where processes are regarded as standard. However, according to the BetaCom operational manager, the input for transactional processing that is sent to BetaCom is often not standardised. For example, the invoices are in different shapes, sizes and forms. Some of the invoices are either not properly coded or approved by the client.

One interviewee commented that the team in India do not display the same 'sense of urgency' as the team members in Portugal. A reason given for this was that the Indian staff do not communicate directly with Alphacorp staff and in the event of a difficulty they are somewhat removed from the intensity of the front line of customer support:

> 'I don't believe they have the same sense of urgency as we have, because they don't have the clients pressurising them.' Project manager, BetaCom (Portugal).

Some knowledge was impossible to formalise into training and could only be gained through experience. An example was detecting errors in reconciliation: work which requires experience. One of the Portugal-based operatives told us:

> 'During reconciliation … when they take the report of some accounts, some figures are there but they should not be … which could only be identified if you have the experience of doing it … that is the kind of thing that they [Bangalore team] have to understand.' Team leader, BetaCom (Portugal).

3.3 Mitigating risks

Chunkification, behavioural, output, and social control mitigate the relational and performance risks. When asked, the Alphacorp contract manager told us that he felt location was not the main factor in risk assessment and that India presented no greater risk than Turkey, Greece, Portugal or the UK. A risk assessment review is undertaken and a risk mitigation plan prepared for all locations as part of the transition planning. Contractual controls ensure that all exported data is protected in line with European data protection laws and BetaCom manages operations to ensure that its legal obligations as data processor are clearly understood and discharged effectively. BetaCom (India) has signed agreements on data protection with Alphacorp entities in Europe.

3.3.1 Chunkification

We observed horizontal chunkification based on Alphacorp's decision to outsource predominantly rules-based transactions, and maintaining critical business tasks 'in house'. By maintaining some internal competence, Alphacorp reduces strategic dependence on any one vendor. Categories of transactional processing are approved by Alphacorp prior to being outsourced as codifiable.

> 'There's judgement that goes into whether we keep it [accounting services] in house, sometimes outsource or never outsource. So generally the scope we outsource is safe to outsource because it is mostly rules based.' Contract manager, Alphacorp.

We observed a further form of chunkification, which is the split of the outsourcing accounting tasks between BetaCom (Portugal) in tier 2, and BetaCom (India) in tier 3 (see Figure 3.1). We were told that Alphacorp and BetaCom agreed four exceptions for 'offshore-able scope' as part of the planning/risk management. Accounting would not be migrated to India and kept in Portugal in cases where:

- a high number of hand offs (interactions with Alphacorp) were required;

- direct face-to-face contact with Alphacorp staff was needed;

- there were frequent non-English language interactions; and

- there was a legal or fiscal impediment.

Alphacorp has a second vendor, Vendor B which performs transactional processing work for Alphacorp subsidiaries in other geographical areas. By maintaining a second vendor, Alphacorp prevents the possibility of contract loss due to poor performance and mitigates against opportunistic behaviour by building a competitive environment for the vendors.

'You could suffer because one or other party had to walk away from the deal or one party was cutting so many corners to meet costs that the quality suffered. It's never happened because we create mutually beneficial economic relationships with each supplier and have the ability to leverage across both suppliers.' Contract manager, Alphacorp.

The size of Alphacorp is significant for control as Alphacorp is one of the world's largest companies. Alphacorp is in a strong position to influence or negotiate with its supplier, thus deterring opportunism:

'We're in a good position because we're a big buyer and we get attention from suppliers. Both our suppliers rely on Alphacorp for a part of their future business and we know they're going to give us a good service.' Contract manager, Alphacorp.

The two suppliers are not directly compared nor does Alphacorp threaten a poorly performing vendor with moving revenue to the other vendor. Alphacorp does not 'demand' from service providers based on size and buying power.

3.3.2 Behavioural control

Behavioural controls include service level agreement, operational level agreement, staffing, training, and reporting structure.

Service level and operating level agreements

Key features of the contract are service level agreements (SLAs) and operation level agreements (OLAs). A series of SLAs indicate BetaCom responsibilities and duties. The SLAs are also linked to a series of OLAs which set out what client staff obligations are to enable BetaCom to meet its SLAs. BetaCom cannot be held accountable for meeting SLAs if Alphacorp has not met relevant OLAs. In the words of the Alphacorp contract manager the OLA represents:

'a kind of reverse SLA as it states specifically what the vendor should expect from Alphacorp to enable the vendor to meet its SLAs'. Contract manager, Alphacorp.

SLAs and OLAs are regularly reviewed:

'At least each month we will have the opportunity to review the key features of the contract: how many of these SLAs and OLAs have been achieved or missed. It's not really a tick or a cross it's much more of a discussion or a review. We also agree the operating level in the service level agreements. For example, BetaCom will pay x% of invoices within y days of receiving them.' Contract manager, Alphacorp.

We were also told by one of the interviewees in BetaCom (India) about how the SLA was broken into separate statements of work:

> 'We have a statement of work that ties into the overall contract, which details out everything I need to do and deliver. I have seen the SLA agreements that explain what I have to comply with to make sure the processes are healthy.' Operation manager, BetaCom (India).

Staffing

During the transition process from BetaCom (Portugal) to BetaCom (India) in 2004, full-time employees were hired in India according to levels of experience and qualifications. It was agreed between BetaCom and Alphacorp that tier 3 would be a multi-client centre. BetaCom cannot remove assigned staff, individuals holding key positions identified in the contract, from the Alphacorp account. This mitigates potential for opportunistic behaviour of the vendor moving inexperienced staff onto the account. Trusted staff working on areas where fraud could take place would not be rotated or replaced by unknown personnel. Alphacorp is not involved in BetaCom recruitment but has the contractual right to request removal of any person working on the Alphacorp account. This right is intended to maintain staff with competence to complete the work assigned thus mitigating performance risk. Crucial to the process are inter firm 'conversations', meaning dialogue:

> 'So we had a conversation with BetaCom. Okay, you bring in all the customers you want to Bangalore but you cannot take away anybody without a good conversation, anyone that we've agreed is a key person. We engage in conversation with BetaCom about their recruitment methods, about whether they access references or whether they've had people who have left who have fraud convictions. Occasionally we will ask them to remove somebody, who we deem to be unsuitable for the job.' Contract manager, Alphacorp.

Alphacorp has never requested the removal of any BetaCom staff in Bangalore. Each year an ethics certification is obtained from BetaCom detailing (among other items) any staff who have left because they have broken laws or committed fraud but prior years' certifications show that no staff committed fraud.

BetaCom (India) hiring policy includes reference checks, academic records, checking the previous employer's recommendation, and for senior staff consulting a published blacklist produced by Nasscom. The Nasscom blacklist, we were told, shows names of individuals who are regarded as having 'bad conduct in their work'. Although only more senior staff are recorded, a central aim of this list is to help to mitigate the risk of fraudulent activity.

> 'We have reports that are published as part of Nasscom, which is one of the governing bodies for the IT enabled services industry to which we belong to. Here we publish people who are blacklisted because they are of bad conduct in their work, they are not trustworthy.' Human resource executive, BetaCom (India).

BetaCom have in place staff reward and job rotation schemes to recognise achievement. There are schemes to move staff to new roles and assignments after a certain period to provide new knowledge and experience thus reducing boredom and enhancing the motivation of staff to stay longer in the vendor company.

> 'We have awards based on different criteria, and last month there were around 25 people who were awarded a total of US$135,000. After a certain period, they are moving to different roles, different assignments so they know the entire job.' Human resource executive, BetaCom (India).

With regard to knowledge retention and the impact of attrition, staff are instructed to document their work. A process simulation software package records the details of the task undertaken by the employee thus minimising the impact of attrition.

Training

At the time of transition, employees from India were given training in Portugal for six weeks. Additionally, a team from Portugal travelled to India before and during the transition to ensure that processing systems worked as required. Training was given in groups or individually:

> 'There's a combination of classroom training on what Alphacorp wanted to make sure that everybody knew, the packages and procedures. They [the trainers] sat with the people that were currently doing it (the task) and had everything explained to them such as how to recognise an invoice for rent as opposed to an invoice for oil or whatever using their keywords etc.' Project manager, BetaCom (Portugal).

There was also language training for Indian staff in Portuguese, Spanish, and French to mitigate communication risk. Several interviewees told us that they were provided with a language database containing 150 to 200 commonly used words translated from Portuguese, Spanish, and French into English. However, as we were told by one of the interviewees in BetaCom (Portugal) there were problems with the list of key words, which were found to be insufficient and incomplete. Staff in India had difficulties with words outside of the key terms provided and solving the problem had some impact on Alphacorp:

> 'They [Alphacorp] had to understand that T3 didn't speak Portuguese, French or Spanish and would only have a list of so many words which they would understand. So if you wanted to write instructions directly to them, then try to use the key words rather than some variation of it, because otherwise they won't understand it. So there was some education for the clients and some of them didn't like that and this is where client pushback came in. Alphacorp staff said "Why should I change what I do just because you sent it to India?"' Project manager, BetaCom (Portugal).

The troublesome requirement for Alphacorp staff to write clear instructions became, at a later date, a requirement within the implementation of control processes to meet Sarbanes-Oxley control objectives.

Reporting

The reporting structure defines how control is spread throughout the organisation. The formal reporting structure between Alphacorp and BetaCom involves governance meetings as discussed above. The reporting structure is augmented with a query log and key incident report. The key incident report is produced in the event of a problem and contains a definition, remedial action and agreement by both sides. The Alphacorp contract manager explains how the key incident report helps to mitigate performance risk:

> 'We have a reporting process whereby Alphacorp asks BetaCom to create a key incident report where the facts are included; the facts are agreed about who did what, what are the root causes and how we're going to prevent recurrence. These are logged, monitored and discussed at the quarterly meetings so we can see we're learning from our lessons and we're not repeating the same mistakes.' Contract manager, Alphacorp.

Physical and systems security

Physical and systems security in T2 and T3 centres includes the use of security cameras, mobile phone detection, and a clean desk policy. Many mobile phones have integral cameras and their use was prohibited. The clean desk policy requires desks to be clear

when not attended preventing unauthorised staff from viewing records. There are also system security mechanisms such as creation, validation, maintenance of staff identity, firewall and anti-virus protection all of which is periodically reviewed and reported to Alphacorp. Other measures designed to reduce fraud risk include segregation of duties (SOD) between several staff members so no single person has access to information that may lead to a fraud. Monthly system generated reports show all instances where a user has an access profile with SOD violations. These reports are provided to Alphacorp and the Alphacorp contract manager approves all unmitigated violations. The problem of collusion between several people to commit fraud is a generally recognised threat to security in India and elsewhere.

Audit

An external audit is performed by Alphacorp's external auditors on the transactional processing performed by BetaCom.

> 'Alphacorp had their auditors flown in to India to do a complete process check for the existing controls and the weakness, recommendations and so on.' Finance manager, BetaCom (India).

Internal control manual

There is an internal control manual that lists out the controls that BetaCom is expected to apply. The manual provides guidance on how each task should be completed with emphasis on control points, control activities, and what evidence is to be available for monitoring effectiveness of controls. Semi-annual assessments of the internal controls are performed in both T2 and T3 indicating gaps in the control and what is being done to remove the gap. The Alphacorp contract manager explains:

> 'We [Alphacorp] worked with the vendor [BetaCom] to design the self-assessment process for their controls, which we've agreed with them are the right controls. They test them with an independent BetaCom audit team to produce evidence. Alphacorp control process owners then form their opinions based on this evidence.' Contract manager, Alphacorp.

3.3.3 Output control

KPIs

Key performance indicators are measures of business performance, used to check performance against targets, or as benchmarks to signal areas of performance in need of improvement. Such measures are used in tier 2 and tier 3 as key output controls to mitigate performance risk. KPIs inform client and vendor whether target service and operating levels are being achieved. For example, KPIs indicate whether costs are within agreed budgets, and for demand management whether the number of invoices or cash receipts processed in a defined period has gone up or down as well as the proportions of efficient transactions versus inefficient (more costly) transactions in the period. Comparison with past periods is performed to identify trends and areas for improvement. The contract manager explains how KPIs lead to conversations:

> 'KPIs let us keep track of all important aspects of performance in the deal. KPIs also provide the basis for continuous improvement conversations. If the volumetric element of KPIs is seen to be moving significantly then KPIs can support scope change conversations.' Contract manager, Alphacorp.

3.3.4 Social control

Central to social control are the organisational practices of silent running and secondment of Alphacorp staff to BetaCom. These practices are important for mitigating both relational and performance risk.

Silent running

Silent running, or lack of, is a proxy measure of how successful BetaCom is performing in the eyes of the community of Alphacorp businesses. Essentially, if there is no 'noise' (complaints about cost, quality or controls) from Alphacorp, then it is assumed until there is evidence to the contrary, that BetaCom is meeting Alphacorp expectations and has achieved silent running. The evaluation of silent running is mainly by informal means and we interpret the central value of silent running as a social control to encourage the alignment of the goals, attitudes and values of the client and vendor. However, assuming silent running could be misleading if Alphacorp staff are too busy to complain. The Alphacorp contract manager expressed some dangers in overreliance on silent running without objective evidence or metrics in support:

> 'It's silent because no one's criticising BetaCom performance, and no one's sticking it up on the wall and saying this is broken. If silent running is not being achieved, my first priority is to restore it. If it stayed broken I would not be able to go after other objectives because I would be constantly involved in fixing silent running and getting people comfortable with BetaCom performance.' Contract manager, Alphacorp.

Alphacorp secondments and trust building

Secondment of Alphacorp personnel is a further mechanism for social control: three senior Alphacorp staff were seconded to BetaCom (Portugal). One Alphacorp secondee was a senior manager of the Portugal centre for a period of several years. These senior seconded staff contributed knowledge about Alphacorp controls and procedures to BetaCom and trust in the goodwill and competence of the vendor thus reducing relational and performance risk. Secondees helped to solve issues or problems within the process due to their knowledge of the client processes and drew on political connections within Alphacorp to resolve difficulties. The goodwill trust they embodied as Alphacorp colleagues with an obligation to their employers (the client) rather than the vendor minimised suspicion and contributed to shared values and goals between the two firms. The Alphacorp contract manager explains:

> '[The seconded Alphacorp manager] was important to BetaCom because she gave them the quality, the knowledge, and the experience of how things work at Alphacorp. The fact that she knows each person in Alphacorp from history allows her to deal with them effectively.' Contract manager, Alphacorp.

However, this had an unexpected consequence as we were told that one seconded Alphacorp employee became a staunch defender of BetaCom staff in the Portugal centre against Alphacorp complaints. However, secondees being a part of the BetaCom management team allowed the outsourcing relationship to develop beyond a service provider – client relationship as secondments were an important factor in trust building.

Processes such as staff recruitment and data security were also key mechanisms for trust building:

> 'We have a lot of faith in BetaCom's recruitment processes, their experience so far, and how well they treat their people. I think BetaCom keeps our data as safe in India as they do in the USA, Europe or elsewhere. It's the same systems, same technology, same access, same access controls, and same management processes and philosophy.' Contract manager, Alphacorp.

3.4 Summary of the case study

Table 3.1 shows a summary of the risks and control responses. It is interesting that in this case study the chunkification strategies of multiple vendors are outsourcing only routine transactions controlled by output and behaviour are in evidence. However, the social

control and trust building which theory would predict as normally only associated with outsourcing higher value activity is in place in an effort to instil a close partnership.

Table 3.1: Summary of the analysis

Control mechanism	Risk	Illustration from the case study
Chunkification	Poaching of staff, systems processes Fraud Vendor hold up Communication	Multiple vendors Three tier architecture Routine generic rule-based transactions only outsourced Rules on 'offshore-able scope'
Output control	Performance	Contracting KPI/SLA/OLA Key incident reporting Internal control manual Contract gainsharing Audit
Behaviour control	Attrition Fraud Communication Culture difference Knowledge	SLA/OLA Governance meetings Training Secondments Standards, audit Security Training, job rotation Contractual stipulations eg, on staff blacklists
Social control	Relational and performance	Silent running Secondments Open book contracting Governance meetings
Trust (goodwill and competence)	Relational and performance	Secondments Processes and standards Continuing track record

4. Gowing and IndiBackOffice

This chapter presents the case study of Gowing and IndiBackOffice. In contrast with the previous chapter, some outsourced work from Gowing to IndiBackOffice involves judgement on relatively unstructured tasks that are difficult to objectively codify and measure. The gamut of activities outsourced to IndiBackOffice went far beyond structured transaction processing to some higher value added accounting activities and the majority is processed in India. In particular, this case demonstrates the importance and dynamics of social control in offshore outsourcing which is appropriate for controlling higher value activities. The chapter begins with discussion of governance followed by a presentation of the risk mitigation practices.

4.1 Governance

4.1.1 Contract

The first outsourcing contract was signed in 2004 and comprised a seven-year agreement of approximately £30 million. Outsourcing is governed by an 'open contract' based on cost plus pricing. The contract contains an SLA with comprehensive KPIs providing measurements of IndiBackOffice's delivery performance. Service credit is applied in the contract as a penalty for vendor failure to reach KPIs.

Gowing mitigated risk of poor vendor performance risk by phasing the migration of accounting to IndiBackOffice. The first transition of staff from Gowing to IndiBackOffice involved transfer of approximately 200 Gowing employees to IndiBackOffice who remained based in the UK. In this stage, outsourced accounting services included accounts receivable, accounts payable overheads, accounts payable overseas, principal ledger, financial reporting, cash management, applications management and support. The first activities transferred to India involved accounts payable, payroll business expenses, cash management and principal ledger. In late 2004, IndiBackOffice (UK) transferred the entire remaining transaction processes to India. This involved receiving input, loading the input, processing the payment, and sending out payment advice. The transition arrangements from Gowing to IndiBackOffice (India) began mid 2004, starting with recruitment and staff training in India, replication and testing of the systems and processes from IndiBackOffice (UK). In mid 2005, the contract was extended by approximately £10 million over the next six years involving a further 210 people transferred to IndiBackOffice (UK).

4.1.2 Organisation structure

The Gowing contract manager is responsible for liaison with IndiBackOffice, for governance meetings and general process improvement. There is a 'one-to-one relationship' between the vendor's head of an outsourced function in the UK and the head of the same function in IndiBackOffice (India) in order to ensure clear lines of communication and deal with any issues which may occur either in India or UK. For example, within the accounts payable function, five staff in IndiBackOffice based in the UK liaise with two team leaders in India who are responsible for 65 to 70 India-based staff. Although most of the transactions are processed by India-based staff, a need for a UK presence remains. Managing the client–vendor relationship requires face-to-face meetings between Gowing and IndiBackOffice. However it is considered uneconomic to send a staff member from India to attend such meetings. Thus, senior client liaison staff are retained in IndiBackOffice (UK) as well as all senior management.

4.1.3 Governance meetings

There are three tiers of governance meetings which are attended by predefined Gowing and IndiBackOffice staff. The meetings have clear agendas and rules for escalation of issues to higher level governance for resolution. The lower management level comprises an operational monthly meeting attended by IndiBackOffice and line manager representatives from all the Gowing business units or functions. The middle management level meeting is also held monthly. These are primarily between UK-based staff – the India centre director travels to this meeting on occasion if there are particular issues requiring his input or participation. The highest management level, bi-monthly meeting is attended by Gowing and IndiBackOffice managing directors.

4.2 Mitigating risks

In contrast with the previous case, some part of the outsourced accounting activity from Gowing to IndiBackOffice requires a degree of judgement as it involves some relatively unstructured tasks that are difficult to objectively codify and measure. This occurs for two main reasons. Firstly, the client outsourced in reaction to a crisis and they had planned for 90% of their accounting function to be outsourced as part of restructuring the business. This gamut of activities outsourced to the vendor went far beyond structured transaction processing to more sophisticated accounting activities and in 2006 the majority of processing takes place in India. Secondly, at inception of outsourcing, the vendor was involved in extensive modification and redesign of client processes which is inherently unstructured work requiring judgement. As the extent of outsourcing is substantial, the risks faced by client and vendor were greater in terms of knowledge transfer and loss, attrition rates, security and fraud. This case particularly shows the importance, techniques and dynamics, of social control viewed by vendor and client as appropriate for the control of the higher value activities outsourced.

4.2.1 Social control

Socialisation and informal interaction between the client and vendor involves key personnel from both sides of the relationship. Vignettes of these key people showing how they nurtured and sustained social control are provided below.

Gowing contract manager

The Gowing contract manager interpreted the open book contract as providing complete access to all outsourced Gowing accounting processes:

> 'If I want to know anything, I can see or ask for it … we cannot be distanced from the vendor ... I see IndiBackOffice as an extension of Gowing's accounting department.'
> Contract manager, Gowing.

The contract manager made frequent telephone calls to check on progress (three to four per day) to IndiBackOffice in India and the UK and had frequent presence in the IndiBackOffice (India) centre. There was a recognition from IndiBackOffice staff that the Gowing contract manager's knowledge and experience of Gowing operations had been helpful at inception of outsourcing and subsequently. The Gowing contract manager was regarded by many in India as 'part of the team' and over time came to be regarded as an ally. Her position as a trusted senior Gowing manager with political influence on Gowing's most senior management enabled convincing explanation of IndiBackOffice's problems without suspicion. The contract manager also enabled change in Gowing's own internal processes where appropriate. Her deep involvement in Gowing and IndiBackOffice's day-to-day and strategic operations helped her to see beyond simple output controls and act bi-directionally to extend improvements into Gowing and the vendor. An IndiBackOffice India-based manager told us:

'[the Gowing contract manager] is trying to highlight the weaknesses in the Gowing business that are causing us problems so we can do things quicker and better. When it's Gowing who are holding us up, then she's prepared to take that back.' Operation manager, IndiBackOffice (UK).

On one of her frequent visits to India, the Gowing contract manager would hold meetings and training sessions, talk to managers and other staff, and identify issues to be taken to IndiBackOffice (UK) and to Gowing. Thus, she acted as a bridge to mutual understanding between the two firms and occasionally between the respective Indian and UK parts of the vendor organisation. Two IndiBackOffice staff gave their views emphasising the bi-directional approach to problem solving:

'She comes here and looks at the service delivery, the metrics, and any areas that need improvement.' Team leader, IndiBackOffice (India).

'Typically, she will come here and tell us the issues the UK people feel they are facing with India. We will give answers for that. We will also give her a list of issues which we are facing here.' Finance director, IndiBackOffice (India).

The contract manager was a key person in Gowing who could use her skills and personal networking across the three sites of Gowing, IndiBackOffice (UK) and IndiBackOffice (India) to drive changes in the process within client and vendor sides of the relationship. She would manage the outsourcing contract but also work personally and often informally with IndiBackOffice UK and India staff to bring a sense of mutually shared objectives, to improve transactional and higher value added processes, and to solve communication and cultural issues between both sides.

Key vendor personnel

An Indian executive at IndiBackOffice (UK) was employed due to a perceived need in IndiBackOffice (UK) to minimise cultural problems between the British and Indian teams.

'We brought Amit to the UK. He is from Sri Lanka, and knows a lot about Indian culture. He is going to be a key link for us in terms of helping us with some of the cultural issues.' Client director, IndiBackOffice (UK).

The India centre manager, Sundeep, plays an important role in overcoming staff attrition, building competence trust and ensuring service delivery to IndiBackOffice (UK) and Gowing. Gowing are outsourcing more than simple routine processes which requires a different skill set of senior leaders:

'Basic process control is a legacy but for today's outsourcing you need people like Sundeep to be always questioning the process. How can things be changed and flexibility added?' New client director, IndiBackOffice (UK).

This person's leadership style, manner, and communication skills were regarded as important in managing the relationship between Gowing, IndiBackOffice (UK) and staff in India. Individuals such as the Gowing contract manager and India centre manager provide a bridge to mutual understanding between India and the UK and these individuals were critical to the success of the relationship. However, it was recognised that reliance on a few individuals is problematic and an interviewee in Gowing (UK) told us that expatriates who could manage operations and mitigate cultural issues between the British and Indian teams would be transferred to the India centre in the future. What was proposed was similar to the secondments in the previous case:

'We want to see a more permanent presence of the UK managers in India … not necessarily running the operations but just being visible and helping with the cultural issues and the relationship.' IndiBackOffice manager (UK).

Contract

Open book contract and participatory governance meetings were regarded as encouraging mutually shared objectives. For example, the baseline cost contract provides guidance on how to determine what IndiBackOffice can offer in the future, the cost of services, and how to share the savings and improve the process. Dynamic attention to pricing and gain-sharing minimises the risk of opportunistic price increases. The controls were being renegotiated during the course of our inquiry:

> 'We are in the middle of scoping what the new baseline, service and controls need to be, measures that we need to have in place to measure success of that process. What it also does is highlight what the potential improvement opportunities are in terms of cost reduction, process improvements, that will ultimately drive down the cost price which is a good thing both for Gowing and us, because we share the savings.' Client director, IndiBackOffice (UK).

Use of such a method allows both client and vendor to develop a consensus on deterrents against either firm from acting opportunistically. Additionally, such an approach could also reduce performance risk as it encourages both sides to lay out reasonable and achievable targets.

4.2.2 Behaviour control

Behaviour controls include the use of reporting structure, staffing and training, physical and systems security, and audit.

Reporting structure

The formal reporting structure provides a role specification to facilitate the process of supervision and monitoring to mitigate performance risk. For example, Sundeep the manager in IndiBackOffice (India) is required to report on performance to the client director, IndiBackOffice (UK). Any written communication (typically email) between the contract manager of Gowing and Sundeep is copied to the client director, IndiBackOffice (UK). Direct communication is permitted but only under certain conditions:

> 'You don't need the approval from IndiBackOffice (UK) to deal with Gowing…but just inform them. This is basically ensuring that the protocols are fine; we call our UK counterparts and say that the client had directly called us and we are going to have a chat.' Finance director, IndiBackOffice (India).

In addition, IndiBackOffice produces a monthly service performance report for Gowing as required in the contract.

> 'We provide monthly reports and one of them is a service performance report, which sets out performance indicators … baseline volume, headline commentaries and that's produced monthly and that's something like a 70 page report.' Finance director IndiBackOffice (India).

An issue log was introduced to solve issues being presented based on 'hearsay'. As one of the interviewees in IndiBackOffice (UK) told us:

> 'We have got a noise level and it would all be hearsay, you go to a meeting and people would say, "oh this has gone wrong" and when I hear that, there would be no factual evidence. So we introduced an issue log. IndiBackOffice and Gowing raise issues on the issue log.' Operation manager, IndiBackOffice (UK).

Staffing and training

IndiBackOffice (India) provides a structured career path to motivate employees, and hence minimise risk of staff poaching by other companies particularly in India where

attrition is high. Career growth includes moving staff into new client tasks, processes, or service lines. The Finance director, IndiBackOffice (India) explains:

> 'They (vendor staff) are given a change in terms of moving to a new client, which means new exposure and an opportunity to travel to the UK adding to career experience. We are also trying to move people within the processes, within the same client or to a different service line.' Finance director, IndiaBackOffice (India).

IndiBackOffice also has in place an exit policy in order to overcome staff poaching by other companies. This policy requires an employee to give notice before leaving and to enforce this IndiBackOffice and other major India-based outsourcers are working with India's software and IT-enabled services industry body NASSCOM on a membership agreement to prohibit poaching of experienced staff. IndiBackOffice (India) also tries to control attrition through training:

> 'You cannot expect a person to work for you based on what he is presently qualified to do. His or her expectation is to be offered a capability road map. You have to have a very good training and development plan for people … There are about 40-50 training programmes we have within the company.' Finance director, IndiBackOffice (India).

Security and audit

Physical and systems security are the main mechanisms to mitigate risk of fraud. IndiBackOffice (India) has implemented physical security using identity cards, time passes, and security guards on doors and gates. The site itself is fenced and guarded by security personnel. These processes are in accordance with BS7799 compliance of information security. Auditing of control procedures in IndiBackOffice is undertaken by Gowing's auditors as if IndiBackOffice were a part of the Gowing business. Ernst and Young and Deloitte & Touche perform the audit in India.[11]

4.2.3 Output control

KPIs

The outsourcing arrangement between Gowing and IndiBackOffice is governed by a clear SLA with output controls in the form of KPIs in the contract. Service management is defined by KPIs which are measured and reported monthly. If IndiBackOffice does not meet service level, service credit is due. This credit is the amount payable to the client (given as a discount) if the vendors fail to meet certain service requirements. Payment of service credit is negotiable depending on IndiBackOffice's explanation of why the company could not meet the expectation.

> 'If I got a KPI to achieve 95% target, and if I don't achieve the 95% target, then I have to pay a service credit. They would expect that I would take the pay (service credit) or at least approach them and explain. If they say, that's perfectly reasonable, then we just agree that service credits don't apply.' Director, IndiBackOffice (UK).

4.2.4 Trust

Interviewees in IndiBackOffice generally expressed their intention to build and maintain good relations with the Gowing contract manager. Reporting the 'true' performance and delivering services beyond the contract were regarded as important in building trust:

> 'At the end of the third year or fourth year we don't have to worry that this contract will go. We will be very confident that this contract will be retained because the client is very happy with us. We have contributed more.' Finance director, IndiBackOffice (India)

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[11] A full consideration of the audit cost implications is beyond the scope of this study.

Gowing had competence trust in IndiBackOffice at the early stage of the contract when selecting the vendor and this trust has been augmented over time by positive experience of meeting SLA and vendor adherence to behaviour controls. Goodwill trust has been augmented by several instances of the vendor 'going beyond the contract'. For example, IndiBackOffice was able to accommodate an unexpected increase in the number of Gowing invoices:

> Recently, we were asked to process suddenly 30,000 invoices by Gowing. We had to take extra people from temporary resources. We had to make people work during weekends and everybody here was willing. The Gowing contract manager said, "You guys are just amazing".' Finance director, IndiBackOffice (India).

4.3 Summary of the case

Table 4.1 shows a summary of the analysis of this case study. This case contrasts with the previous case study in that the scope of outsourcing is much greater. Therefore, findings concur with theory in that the Gowing contract manager minimises risk by developing social control over the vendor by frequent travel and regular informal contact. A full and complete gamut of behaviour and output controls are also in place. The development of goodwill trust has been particularly enhanced by the number of occasions the vendor has shown great commitment to the client in 'going beyond the contract' and delivering services over and above the basic requirement.

Table 4.1: Summary of the analysis

Control of mechanism	Illustration from the case study
Chunkification	Phased implementation IndiBackOffice (UK) provides client management
Output control	KPI, gainsharing Service credit
Behaviour control	Reporting Training Systems audit Issue log Exit policy Security
Social control	Gowing contract manager as 'part of the team' Travel to India and informal contact Bi-directional process improvements Vendor staff also act as 'bridges to mutual understanding'
Trust (goodwill and competence)	'Going beyond the contract' Positive experiences over time

5. Ardon and Technoaccounts

This chapter presents the case of Ardon and Technoaccounts and shows how small firms with limited resources face difficulties in managing attrition levels in India. Ardon's vendor in India, Technoaccounts, presents high potential for performance risk because of its small size and thus limited resources. Ardon has relatively smaller needs in terms of volume, scope and the type of work outsourced to India relative to the previous cases and the tasks outsourced are limited in sophistication. Ardon rely on building trust to mitigate risk rather than in the other two cases discussed in this report. Small firms often have limited resources to engage in extensive control and instead the Ardon director relied initially on the reputation derived from recommendations and then personal goodwill relationships. We demonstrate how Technoaccounts struggled to maintain performance while simultaneously containing high staff attrition and expanding their operations. As in previous chapters, we start with a description of governance, followed by a discussion of the risks faced by Ardon and Technoaccounts, and finally mitigation of the risks.
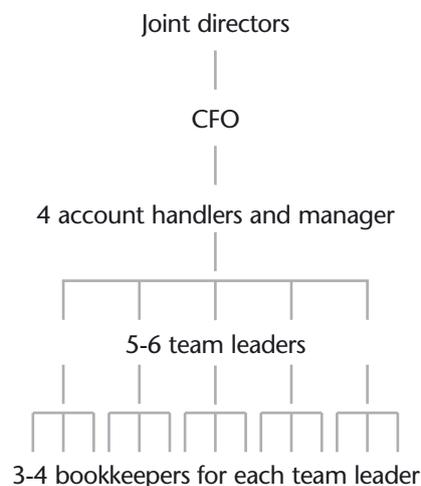
5.1 Governance

5.1.1 Contract

Technoaccounts have two contracts with their clients. Firstly, the executed sales agreement contains details of the service agreement, promises and guarantees to mitigate performance risk. The second contract is the data protection and confidentiality agreement which is based on UK law and intended to mitigate relational risk. A Technoaccounts manager told us of the behaviour controls written into the contract:

> 'We enter into an agreement in terms of confidentiality and non-disclosure. We don't allow part timers to work with us; anybody who is with us is the full-time employee of the company. We don't employ temporary employees and we don't subcontract work.'
> Chief financial officer, Technoaccounts.

Technoaccounts have personal insurance cover to mitigate the risk of being sued by a client so they would in most circumstances remain solvent in the event of a dispute.

5.1.2 Organisation structure

Figure 5.1: Technoaccounts organisation structure

Joint directors

CFO

4 account handlers and manager

5-6 team leaders

3-4 bookkeepers for each team leader

Each of the six team leaders has three to four team members. In addition six data entry staff help the bookkeepers to input the data. The four account handlers are not all qualified accountants but form the communications 'bridge' between the team leaders, bookkeepers and clients. The role of the account handler is to follow the status of outsourced accounting (known as 'jobs'), deal with client email and telephone communication and check the work of team leaders. Team leaders review the work of bookkeepers and perform some of the work themselves. The account handlers' focus is on understanding client needs and daily interaction with clients as all client communication is though the account handler. Most UK–India communication takes place between the Ardon administrators and Technoaccounts account handlers in India using MSN hotmail chat. Email is also used but less frequently than MSN chat and telephone communication is rarely used. We were told by the Ardon administrator:

> 'I think I've spoken to Marion [Technoaccounts account handler] about three times. I think it's more difficult to speak to them than by email. It's much easier to understand by email.' Administrator, Ardon.

The other major tool for communication and data transfer is the web portal, which is where all work is uploaded to Technoaccounts and control information is available on the progress of jobs. The MSN chat feature is permanently open on the Ardon administrator's Windows desktop and she would respond immediately to synchronous chat with India team members.

5.1.3 The process

A summary of how the process is transferred and managed is shown in Figure 5.2.
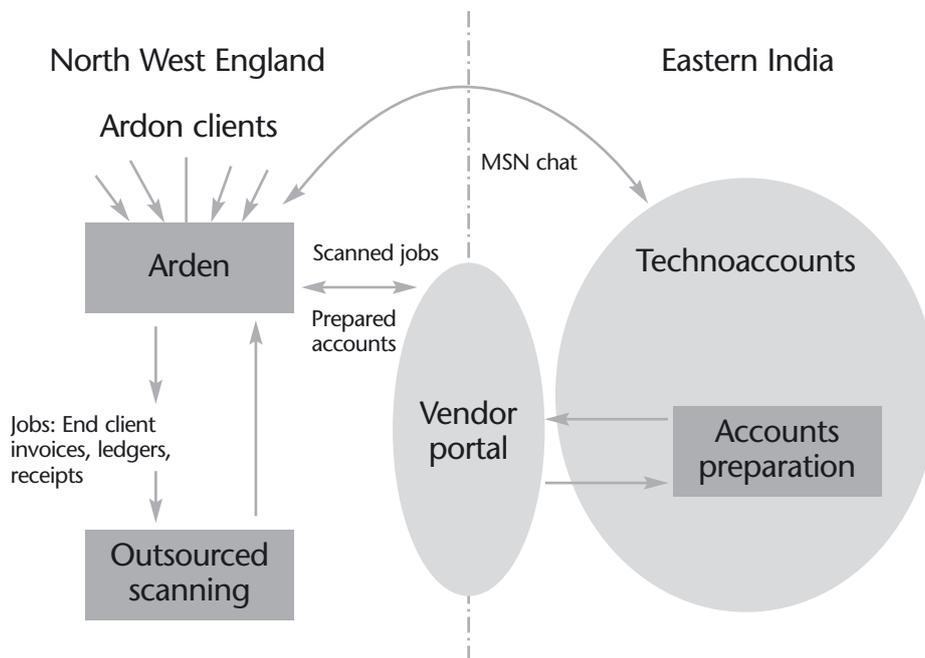
A typical Ardon client would bring computerised or manual records into the Ardon office. The Ardon administrator checks the records against the last year as Ardon pricing depends on the records being of a certain standard. The administrator compiles the information deemed necessary to go to Technoaccounts, which typically comprises appropriate parts of the cash book, bank statements and the previous year's file. A scanning firm collects the data once a week, scans and returns a CD containing the records. While the data is being scanned the administrator compiles Technoaccounts control sheets. The data, control sheets, an estimate of hours to complete the job and

any special instructions on how to prepare the accounts, are despatched to Technoaccounts via a secure FTP link using the portal. Special instructions attached may refer to requirement for bank reconciliation or VAT summary. Technoaccounts then prepares the job and submits queries as they proceed. Technoaccounts provides an analysis in Excel and posts the entries onto the client's accounting software. Technoaccounts is able to utilise Viztopia, IRIS, Sage and other software according to a client's specific needs. When a job is received by Technoaccounts from Ardon or any other client, it is allotted to a particular team or an individual member. Queries at this point tend to be focussed on missing papers or bank statements. Once the data is inputted and accounts produced, the job is internally reviewed by the quality assurance manager before pre-posting via the portal. Queries are then sent and resolved. The job ('final set') is then posted and completed.

A greater number of queries are generated if there is no previous year data or it is the first time Technoaccounts have worked on the account. The main volume of queries emanate from Technoaccounts' lack of access to the compete set of data. It is regarded by Ardon as impractical to send Technoaccounts everything relating to a client account; even a small firm client will produce thousands of pages of documents and invoices, and hence, a judgement is made by the administrator on what Technoaccounts needs:

> 'Nicky (Ardon administrator) will send them over what she thinks they'll need and if she's missed anything, which will always happen, there might be a thousand purchase invoices and they will think something has been miss-posted and they'll want to see a particular purchase invoice. Now we can either tackle that by sending another thousand invoices or you can wait until they ask a question and then go and dig out that invoice and scan that. So there's this back and forth, it's done by internet chat. They will raise queries and my team will answer those queries.' Director, Ardon.

Typically, two weeks after the initial package has been despatched, a pre-posting review is presented by Technoaccounts. Again, several queries will be presented with the job in a semi-complete state. The administrator answers the queries, the job is then sent back and Technoaccounts makes final amendments and returns the final set of accounts. This is then entered into the Ardon computer system and a meeting is arranged with the end client to do the tax planning and commercial work; the added value work that Ardon provides.

5.2 Risks

5.2.1 Relational risks

Switching costs and vendor hold up

The first instance of potential opportunism concerns vendor hold up (price rises) and high switching costs for Ardon. Over time, Technoaccounts builds up knowledge of the client, having worked on previous years' accounts, thus presenting Technoaccounts with an advantage over alternative vendors and imposing high switching costs for Ardon. Any new supplier would be faced with learning the Ardon client accounts, with concomitant queries and loss of staff time. Technoaccounts may engage in vendor hold up to the limit of the Ardon estimate of the benefit of remaining with Technoaccounts and the cost of switching. The problems of reverse transition were very apparent:

> 'If all those jobs now came in and we had to deal with them in house we'd have to recruit a lot more people and they'd be taking up all the office space here and then you'd have all the hassles that come with employing people, sickness and holidays.' Administrator, Ardon.

Increased cost of control

There is also evidence from the case that over time cost of control has increased for Ardon. Some of the cost of control was unexpected because Ardon had expected it to be provided by Technoaccounts. An Ardon manager told us:

'We were told specific things, a job will receive two reviews from a qualified chartered accountant and we're not seeing the evidence of that, we're picking up silly errors that if there had been any review at all, would have picked up on. We are having to do more than we were told we'd have to do, it's requiring a lot more of my internal review time here, which is expensive, very expensive for us to do.' Manager, Ardon.

Secondly, it emerged that promises made about consistent Technoaccounts personnel associated with the Ardon account were not being fulfilled:

'We were promised consistency of personnel, that we would get two, possibly three, dedicated individuals, and we've not seen that, we've had upwards of ten different people work on our jobs. We were told that we would have CVs put across to us, and that we would be able to choose the individual personnel. We were also told that once those people had been selected, we would have one of them come over here and spend three weeks with us, to get a full cultural understanding of what it is that we do.' Director, Ardon.

It was not made completely clear what the impact of this failure by Technoaccounts to abide by the agreement has been. It can be assumed that using the same staff on the Ardon account continually would build up a stock of knowledge of the various accounts outsourced, and hence, experienced Technoaccounts staff would have learned from mistakes and queries thus enabling them to work faster, and reducing the need for subsequent work at Ardon. Thus dedicated experienced staff would raise fewer queries and would be unlikely to make the same mistake or query more than once.

These problems may be explained by the context of the Chennai offshore accounting milieu, which is characterised by high attrition. Firstly, there has been a steep increase in the volume of work Ardon and other UK firms of chartered accountants have outsourced offshore to Technoaccounts. The problem of maintaining performance in an environment of increasing demand incurs capacity management problems common to many small businesses in an embryonic, dynamic evolving industry. The director at Ardon told us:

'They [Technoaccounts] are struggling to cope with the expansion, they're not delivering on all the promises that were made, and I don't think that's anything other than they've just under-anticipated how fast they were going to grow.' Director, Ardon.

The Ardon director's view of India's 'massive labour pool' and how Ardon and Technoaccounts 'can grow together' must be examined in relation to recruitment and retention difficulties in the local Indian context. Far from Technoaccounts being able to choose from a 'massive' labour pool, they are a small firm competing for staff with large multinationals, and this predicament often thwarts easy expansion and retention. A Technoaccounts director told us:

'Most multinational corporations have their own back office here. For example IBM and StanChart have a back office here.' Director, Technoaccounts.

Intermingled with this problem was an unexpected consequence for Ardon of acting as a reference site and advocate for Technoaccounts to other UK firms of chartered accountants. An Ardon director explains:

'I was initially so impressed by Technoaccounts, I have been very vocal in praising them and a number of people have signed up with them as a direct result of what I have said ... the risk for this firm is that the service standard that we get from Technoaccounts deteriorates as they take on more work. That has happened.' Director, Ardon.

Confidentiality and data protection

Contrary to what we expected, when discussing data protection and confidentiality issues Ardon perceived the physical distance involved in outsourcing records to India as a benefit. This must be put into context. Ardon's local environment is a relatively small town which Ardon described as a 'closed community' where 'everyone knows everyone else'. Thus, Ardon staff are required to be particularly careful not to discuss clients outside of the office. The Ardon director explains:

> 'I say to them [Ardon employees] when they join us, confidentiality is key to us, don't talk about clients in the pub etc. I think they're likely to breach that accidentally. The biggest risk I've got is somebody sitting in a pub, happening to mention who we act for. If somebody else hears they could say to our client "oh, your accountant was in the pub talking about you". The very fact that the people doing the transactional work are 5,000 miles away, I think is a benefit for confidentiality.' Director, Ardon.

5.2.2 Performance risks

Country risk

There were no voiced concerns over infrastructure or geo-political risk. However, during the time of our visit to India, we were told that 14 people did not arrive for work due to the floods that had affected Chennai in the preceding weeks. The power supply was discontinued on several occasions on the day we were in Technoaccounts' premises although the uninterruptible power supply (UPS) maintained power to computers. The Technoaccounts building is on an incline and was not affected by the flooding but senior staff were concerned that people might suffer from follow on sickness associated with high water levels.

Hidden complexity

We were told of difficulties with deciding which jobs are suitable for outsourcing and appreciating the complexity of a job before it is outsourced. Only 'straightforward' jobs would be outsourced. However, the Ardon administrator mentioned occasions when on first glance at a client's records in Sage, for example, the job can look 'very good' and 'straightforward', and hence would be outsourced to Technoaccounts. There may however be hidden problems which will cause great difficulty for Technoaccounts, resulting in many queries:

> 'It's only when you start to actually prepare the accounts and you think, well, the bank doesn't reconcile.' Accounts administrator, Ardon.

Thus, a job may be more complex than it may seem on a preliminary assessment. This causes a dilemma in the level of checking on the UK side before outsourcing. In order to detect such problems before outsourcing offshore, the job would have to be taken almost to a stage of completion.

Quality

A significant performance risk faced by offshore outsourcing clients is that of reaching and maintaining appropriate quality standards. A Technoaccounts manager believed that offshore outsourcing presented no greater risk than onshore and that the issues faced by in-house provision are similar:

> 'The overriding issue is quality. We face the same issues as the UK; people get bored, people get lazy, people make mistakes, and people leave.' Manager, Technoaccounts.

It was argued by this interviewee that the issues in India and the UK are similar. However, Indian firms are subject to higher levels of attrition than in the UK. The nature of work in the India centre, almost exclusively transactions, renders it harder to offer employees

more sophisticated types of work that might offer higher levels of job satisfaction. This leads to problems of motivating staff and contributes to attrition. This impact of attrition is greater on a small firm like Technoaccounts than a large firm employing hundreds or in some cases thousands. At Technoaccounts the loss of just a few people represents a significant percentage of the whole.

Typical quality-related problems which arise are caused by time pressure in the India centre and assumptions made by accountants who are often working on multiple client accounts with different standards. There were instances of problems associated with tacit knowledge, knowledge that is practically enacted but difficult to articulate. An example was given of this:

> 'If a job comes back from Technoaccounts sometimes they'll say "well what's this?" It's apparent to us because we'll say "oh building materials" or whatever, but they don't know the supplier.' Accounts administrator, Ardon.

Technoaccounts staff commented as follows:

> 'We have 21 clients so we have to maintain the quality of work and we have to use their templates to do their jobs. You have to remember each and every client's template … Sometimes we assume things, which they won't accept.' Quality assurance manager, Technoaccounts.

A further problem occurs due to the variation in standards of different staff:

> 'An example is treatment of expenses; it differs from accountant to accountant. One accountant will say this kind of expense should be treated one way and the other accountant says treat it another. This is especially the case with VAT … It differs from client to client.' Accountant, Technoaccounts.

A further quality-related problem concerns the expectations of clients who have cost reduction as an overriding imperative. Compromises on quality are necessary to accommodate this. A senior Technoaccounts manager explained:

> 'If I charge our client 10 hours, and I take about 20 hours, I produce a perfect job but clients would not be willing to pay for 20 hours of work. So what we have to do is try to do that perfect job in 10 hours. The quality issue is really the single greatest issue that we face as accounting outsourcing vendors. As we expand rapidly, our staff that are trained then are put under time pressure but this is exactly the same in the UK. It's like having a January deadline, and everyone working 22 hours a day to meet the January deadline.' Director, Technoaccounts.

5.3 Mitigating risk

5.3.1 Trust

Inception of outsourcing to Technoaccounts

Within five days of the Ardon director attending a trade conference, the director of Technoaccounts gave a demonstration and within two days of that, Ardon had a test run of three jobs outsourced to India. These were considered successful and within 30 days, Ardon signed a 12-month contract with Technoaccounts. The arrangement began with a trial period of one month during which time the Ardon administrator and a colleague checked the jobs completed by Technoaccounts but no parallel accounting was performed.

Contact stage trust

At the early stage of the relationship, Ardon had trust in Technoaccounts derived from the trade conference endorsement and this facilitated rapid movement to Technoaccounts giving a demonstration. The ensuing trial established a base of competence and goodwill trust. Many of Technoaccounts' other clients have signed contracts for the service but tend not to use it for the first few months. We were told by the Technoaccounts director:

> '…they install it [the Technoaccounts software portal and training] and then three months later they still have not sent us work. So you are sitting and facing this model of 100% installation, 20% use it immediately, 30% in the first month, 40% from months one to month six, and maybe 10% never use it.' Director, Technoaccounts.

Our interpretation of the behaviour of these 'sleeping clients' is that they are building up competence trust in Technoaccounts very gradually and mitigating relational and performance risk in this way. The behaviour of these firms is similar to the behaviour of early adopters of software offshore outsourcing: start small, outsource non-critical processes to test for opportunism and adequate performance.

Building trust with constant communications

The almost constant communications between Ardon and Technoaccounts using the chat forum contributes to goodwill and competence trust and thereby mitigates both forms of risk. Technoaccounts implementation of customer relationship management (CRM) software may be understood as impacting on competence trust. We were told by a Technoaccounts team leader:

> 'The CRM package means that every time I make a phone call to the client, I'll look for the client record and look at the last five phone calls, and see what we say to them and look at the feedback.' Team leader, Technoaccounts.

This log of performance is likely to contribute to reducing performance risk by improving the client's competence trust in Technoaccounts if the operator has clear knowledge of issues in last interactions.

We witnessed none of the social control techniques such as secondments or travel between sites of a contract manager. However, the account handlers were key to facilitating goodwill trust and thus minimising relational risk. We met three of the account handlers during our visit. We were struck by their excellent communication skills. Marian's mother tongue is English and is spoken without accent; she is a very relaxed and cheerful person and as a result builds a strong rapport and is much liked by clients. At lunch she told us stories of how clients had made special visits to see her. Vidya is educated to MBA standard and Sree is part qualified as an accountant. We met two other people with equally good communication skills and ability to develop rapport with clients. These 'interface accountants' were not engaging in the cosmetic subterfuge often encountered in Indian call centres such as accent training and false Western names. Technoaccounts did not pretend that the account handlers were English to Ardon. The Technoaccounts director boldly told us:

> 'We are an Indian company; we are not hiding behind the fact that we are an Indian company, so these are Indian handlers'. Director, Technoaccounts.

Some clients may find this honesty contributes to goodwill trust thereby mitigating relational risk.

5.3.2 Chunkification

A particular control problem is related to the number of queries Technoaccounts staff make to Ardon which caused an unexpected administrative overhead. The Ardon administrator commented:

'They are bombarding us with a huge number of little queries, which require my team to dig out files and go through invoices if they want clarification on how to do something. For example, we had a difficult job a couple of weeks ago where the client was an investment business and Technoaccounts weren't sure how to work out the list from the spreadsheet we'd given them. So I literally gave them guidelines, look at this column, look at that column, and pick these bits out.' Administrator, Ardon.

The proposed control solution to this involves chunkification. We were told:

'For the last four months all our work has been outsourced to Technoaccounts apart from the audit work we do for clients. Now we're in a situation where we've recognised that we probably need a middle ground. We need to identify work that is likely to generate a lot of queries from Technoaccounts and keep that in house or outsource it within the UK. Straightforward work, which we think will generate few queries, can be given to Technoaccounts. We estimate that 80% of jobs can go to Technoaccounts, 20% will have to stay in the UK'. Director, Ardon.

The decision on which activities will be sent to Technoaccounts is based on the nature of the job, its volume, size and how 'straightforward' it is deemed to be. 'Straightforward' jobs were regarded as the most structured, codifiable tasks, where queries would be unlikely and only these are sent to India:

'We will decide if a job is straightforward in which case it can go to Technoaccounts. If there are likely to be significant queries because of the nature of the job or the size, or the volume of transactions, we will undertake the work in house.' Director, Ardon.

There are some very definite areas that Ardon staff told us would not be outsourced to Technoaccounts. This strategy is adopted to mitigate relational risk, mainly potential opportunistic poaching:

'We haven't got them on forecasting yet. We've kept that in house at the moment. I think it's because of the limitations of the software that we use. I don't think [Ardon director] would be happy to let that go over to Technoaccounts because Technoaccounts are dealing with other accountancy firms. He wants to make sure our software package isn't used by anyone else.' Accounts administrator, Ardon.

Secondly, some work requires a personal touch:

'I don't think it [outsourcing to Technoaccounts] would work for personal tax because our personal tax clients pop in and they want to talk about their tax. They're here on the doorstep and you get to know them and they like that personal touch … a lot of our clients have been with us for a long time and they build up that relationship with a person. They stay loyal to the person more than the firm really. So I think there will always be that personal chat and understanding.' Accounts administrator, Ardon.

There were plans expressed by senior Ardon staff to move other activities to Technoaccounts such as corporate tax, payroll, VAT and quarterly management accounts in the future.

5.3.3 Output control

Technoaccounts output control

Output control at Technoaccounts is done at several stages by the team leader and manager. The pre-posting to the portal itself is a control point. This activity involves the Technoaccounts staff and an Ardon administrator; an Ardon director checks samples, but not routinely. The administrator is able to view every job with Technoaccounts via the portal. This shows the job, 'Technoaccounts handler' (ie, the person working on it), name of the client, the job code, the year end and state of completion. Status of a job may be indicated as for instance 'job pre-posted' or 'first review' and this is updated daily. In addition, at the end of a job, every file has an option for client feedback to be given on a Likert scale where it is scored as 'poor', 'average' or 'good' and comments added. A Technoaccounts team leader told us:

> 'If we ever have a poor mark, we then have an inquest with the client, with the team leader, with the account handlers: [as to] why did this happen?' Team leader, Technoaccounts.

To control for client side opportunistic poaching of proprietary processes, Technoaccounts protect spreadsheets and processes from being copied. Technoaccounts are ISO9001 accredited, but Ardon never mentioned this as an important criterion in the decision to outsource to Technoaccounts. However, it is likely that this accreditation has improved efficiency of processes between Technoaccounts and clients and internally in Chennai.

Ardon output control

In addition to Technoaccounts reviews, we were told of internal Ardon controls of Technoaccounts outputs. The Ardon director told us:

> 'The reviewer would fill in a checklist. For example if the gross profit had changed by 5%, they need to investigate. If the turnover's gone up by more than 20%, they need to investigate why. If overheads have gone up for some strange reason or gone down, they need to look why.' Director, Ardon.

However, we noted that there was no specific checking of Technoaccounts outputs to ensure that an entry had been correctly categorised.

5.3.4 Behavioural control

Control of attrition: overcapacity and training

Most attrition in Technoaccounts is at the lower staff levels, the team leaders have been in place for more than three years. To cope with high levels of lower staff level attrition, Technoaccounts hire more staff than are required based on anticipated work and to take account of loss through attrition. Behaviour control consists of training to mitigate performance risk of attrition and loss of skill in India. Appropriate skills and motivation of staff are key:

> 'What we do is we try to give them individual responsibilities. First six months it's an evaluation period. In [the] first three months, two to three months, he takes time to settle; after that he starts doing an independent job with the guidance of the team leader; then we try to move and give him a better profile saying that he can handle the independent accounts. So without much of a modification of compensation packages, we allow them to grow in terms of the responsibilities. That way we try to give him a sense of belonging and by end of year one he can aim to be a team leader.' CFO, Technoaccounts.

Use of IT for control

The Technoaccounts portal includes a facility for job tracking enabling Ardon staff to view online a list of outstanding jobs and status of completion. This acts as a control over the progress of the many jobs assigned. MSN chat acts as both output and behaviour control. Feedback is received at stages and informal coaching from the clients is provided when answering queries. IRIS, the chosen accounting package, presents an example of behaviour control in the shape of the embedded rules of the software ie, standard data entry screens.

Control of Technoaccounts staff opportunism

The bookkeepers who have worked on each job are recorded so in the event of any misdemeanour he or she could be traced:

> 'When we send the information over to Technoaccounts, they ask for the bookkeeper and the reviewer and we've set up five members of our team and we can basically highlight the members of the team who have been involved in that job.' Accounts administrator, Ardon.

Secondly, the risk of opportunistic behaviour by Technoaccounts staff contacting an Ardon end client is mitigated by behaviour control. We were told by a senior manager:

> 'We have written in the contract of employment in India, that if any member of staff ever contacts a client, or a client of one of our clients, they will lose their job by the time they put the phone down. We will sue.' Director, Technoaccounts.

However, as previously mentioned, suing an individual in the Indian courts is often a slow and cumbersome process.

Data security in India

Risk of data loss as a result of frequent power failure is mitigated by a UPS installed in Technoaccounts Chennai offices and a generator starts after a few minutes of UPS backup in the event of a longer power cut. To mitigate risk of fraud and identity theft, data is transferred via a secure FTP server and a backup line is installed. Behaviour control in the form of policies prohibiting non-business email and online chat are in place in employment contracts. Physical security controls are installed including the removal of CD writer drives from computers and complete removal of floppy drives and USB ports. The internet firewall prevents access beyond named sites. The potential for loss of data in the result of disaster is minimised by multiple backups. Another key concern is posting of jobs to incorrect clients but the software for job posting incorporates a structure to prevent clients receiving the wrong job:

> 'Whatever jobs are there will be listed, so once you do some work that job name will come on the top. You cannot post missing info of Y job on X. So that way it's pretty safe.' IT manager, Technoaccounts.

A security guard is employed on the door of the building who we were told by several interviewees randomly checks employees for writing materials, CDs, cameras and mobile phones on entry and exit.

5.4 Summary of the case study

Table 5.1 shows a summary of the analysis. This case displays no examples of social control which is not surprising as margins are very tight at this part of the offshore outsourcing market and thus frequent travel between UK and India is not economical. The emphasis is on outsourcing codifiable transactions only and minimising risks by standardisation, output and behaviour control or outsourcing infrequently (the 'sleeping clients'). Trust has been fundamental to Ardon taking the leap of faith in outsourcing to

their vendor. They trusted the recommendation of other Technoaccounts users (trust in the competence of Technoaccounts) and then relied on personal relations and regular communication between the staff in both firms to develop goodwill trust. However, service has been variable as the vendor has struggled to cope with expansion and attrition. Some contractual promises have been broken and Ardon have had to improvise solutions (adding extra controls, outsourcing only 'straightforward' jobs). The case shows how trust which mitigates risk can go into reverse in the event of a regression in trust caused by reneging on promises for example. This will lead to implementation of compensatory controls or the search for alternatives.

Table 5.1: Summary of the analysis

Control mechanism	Risk	Illustration from the case study
Chunkification	Cost of control Queries, errors High attrition in India	'Sleeping' client base Outsource only 'straightforward' jobs The portal, standard procedures Hidden complexity of jobs pre-outsourcing
Output control	Quality errors Reneging	Ardon impose internal checks Portal displays jobs for review at stages
Behaviour control	Non-standard practices of clients and staff Problem of hidden complexity Attrition Fraud	Training Job tracking Fraud and data security procedures Rules of IRIS Non-disclosure agreements ISO9001 Staff overcapacity
Trust (goodwill and competence)	Switching costs Vendor hold up	'Sleeping' clients Recommendations from industry conference Regression of trust leads to control implementation. Generation of goodwill through good personal relations between staff in both firms particularly using MSN chat.

6. Discussion and conclusions

In this section we reflect on the key risks, control and trust findings and provide some general lessons for clients and vendors.

6.1 Risk

Despite the institutional differences, interviewees across the case studies on client and vendor sides of the relationship perceived that Indian vendors do not present a greater risk of opportunistic shirking, reneging, cheating or poaching than vendors in any other country. There were, however, additional performance risks associated with offshore outsourcing associated particularly with knowledge transfer, knowledge retention (managing high levels of attrition) and communication across distance and language. The experiences of Ardon and Technoaccounts particularly show how small firms with limited resources face difficulties in managing attrition levels and achieving growth.

6.2 Control

The cases dealt with the risks in many different ways. At Alphacorp–BetaCom, only codifiable transactions are outsourced. Parts of the outsourced accounting are undertaken in the Portugal hub to minimise risks arising from such impediments as language skills in India. Accounting would be kept in Portugal and not be migrated to India in cases where:

- a high number of hand offs (interactions with Alphacorp) are required;

- direct face-to-face contact with Alphacorp staff is needed;

- there are frequent non-English language interactions; and

- there is a legal or fiscal impediment.

Ardon has smaller needs in terms of volume, scope and the type of work outsourced to India. Some work is kept 'in house' if it presents the need for a 'personal touch' due to established face-to-face relationships with clients or if the work presents unacceptable risk of vendor opportunism. The results here concur with Das and Teng (2001) as behaviour and output control was shown to be used to good effect when the transactions are codifiable and measurable in the case of lower level accounting functions (eg, payroll). The results also match the theory in the Gowing case where social control was used extensively when outsourced transactions involved judgement, were relatively non-codifiable and contained un-measurable output (eg, process improvement). However, the results do not concur with theory in the unexpected use of social control at Alphacorp–BetaCom where outsourced transactions were codified, controlled by output and behaviour control but secondments and silent running were adopted and considered highly important to outsourcing success. Thus, control decisions made purely on the characteristics of the transaction alone may be misleading and managers may consider the introduction of controls such as secondments even for codifiable transactions where the volumes involved are sufficiently high and where it is expected the relationship will move to higher value activity over time.

Gowing outsources high value activities to IndiBackOffice and the Gowing contract manager's frequent travel to India and direct involvement in problem solving, sometimes at a practical operational level, had the effect of inculcating mutual understanding among staff in the vendor's Indian centre and in Gowing (UK). The Alphacorp case study shows how the middle person role can be taken further involving direct secondment of client staff to manage the vendor centre.

The Gowing–IndiBackOffice case has many similarities with Alphacorp–BetaCom in that both are in outsourcing arrangements with a proportion of processing done in India. However, there are contrasts between all three case studies which are summarised in table 6.1 below:

Table 6.1: Comparison of cases

	Alphacorp – BetaCom	Gowing – IndiBackOffice	Ardon– Technoaccounts
Size of firms	Global multinationals	Regional presence – UK/India	Local, small firms
Volume – number of transactions	Large	Relatively small compared to Alphacorp	Smallest
Scope (type of transaction being outsourced	Narrow. Only transactional processing, codifiable, rules based, generic processes	Wide scope of accounting activity being outsourced – 90% of Gowing accounting function	Codifiable 'straightforward' tasks

Alphacorp–BetaCom and Gowing–IndiBackOffice contracts are open book designed to develop partnership arrangements over a long term. However, the size and scale of the Alphacorp–BetaCom contract coupled with outsourcing to a second vendor acted to minimise risk of vendor opportunism. Also, the global reputation of BetaCom and its presence as a very large employer in India has the implication of lower attrition levels relative to the norm in the local cluster.

The Gowing case study shows how the risk of outsourcing non-codifiable accounting tasks may be mitigated. These activities were outsourced initially due to a crisis which justified the boldness of approach and extent of offshore outsourcing. When moving up the accounting value chain to activities involving judgement, open book contracting and social control were seen to be effective to inculcate shared values and a sense of 'pulling together'. Such mechanisms require key leaders on both sides of the relationship and the Gowing–IndiBackOffice case gives some insight into the behaviour, personalities and skills possessed by such leaders. However, the use of social control to mitigate risk for higher value functions may create tensions in an outsourcing arrangement. Effective social control requires clients to have access to areas of the vendor's operation which might previously have been considered 'out of bounds'. For the control of these higher value added activities, leadership style and communication skills become as crucial as technical ability.

All three case studies demonstrate the impact of the attrition problem in different cities of India although BetaCom is able to absorb the problem more readily due to its size of operation and its reputation as a large employer. BetaCom can transfer part or all operations to another country if salary and/or attrition levels become intolerable but the other two vendors offer only a single country centre.

Although both of the larger outsourcing arrangements have established governance meeting structures, the reporting structure in Alphacorp–BetaCom tended to be more formal than Gowing–IndiBackOffice. There is no direct reporting from India to Alphacorp. The reporting structure in Gowing–IndiBackOffice by contrast relies extensively on informal interaction mainly emanating from the Gowing contract manager's travel and frequent telephone calls to vendor staff in India and the UK. Reports on security standards BS7799 and SAS70 were features of both of the larger cases accompanied by a set of measures to prevent hacking and staff opportunism (eg, security guards, card access).

The control mechanisms observed across the cases can be summarised in the following table:

Table 6.2: Control and trust mechanisms across the case studies to mitigate risk

Control and trust mechanism	Illustration from the case studies
Governance	Open book contract Meetings Participatory decision-making
Behaviour control	SLA/OLA Reporting Staffing and training Physical and systems security Audit Standards and policies Internal control manual
Output control	KPIs/Service credits
Social control	Silent running Secondments Regular visits of middle person as bridges to mutual understanding Personality and skills of middle person
Chunkification	Vertical and horizontal chunkification Near-sourcing arrangements Phased implementation
Trust	Small firms particularly rely on trust and controls provided by vendors Going beyond the contract Positive experiences over time

6.3 Trust

Ardon had a high level of trust in the goodwill and competence of Technoaccounts to mitigate relational and performance risk. However, trust is regressing as Technoaccounts renege on certain promises. Small client firms do not have the resources to engage in a full due diligence process or impose controls in the way the large firms in the sample do. Small firms may rely to a greater extent on the controls provided by the vendor to mitigate relational and performance risks. The vendor's goodwill could not overcome the problems they experienced with staff attrition in India. Subsequently, the case shows how trust can 'go into reverse' when the vendor reneged on promises causing Ardon to install costly controls in the form of checks and audits of the vendor output and even consider alternative vendors.

The other cases differed in the extent to which trust was seen to mitigate risk. The Alphacorp–BetaCom case study involves a long-term outsourced process. Alphacorp is one of the pioneers of offshore accounting outsourcing and relationships and processes are mature. Goodwill trust built on track record and personal relationships derived from secondments and regular face-to-face co-present meetings act to minimise risks which include the impact of surveillance of the vendor that such arrangements afford. The relatively more recently established Gowing–IndiBackOffice outsourcing arrangement commenced as a result of a crisis. This relationship moved up the 'trust curve' very quickly due to the urgency of the need for outsourcing. The actions of the contract

manager have been effective in inculcating a sense of common goals and thus social control. This has built goodwill trust on both sides shown in the vendor 'going beyond the contract' to help in crises. The contract manager has also been able to build competence trust when engaging in surveillance of the vendor. When in India and during the frequent informal contacts this manager is able to supplement formal output controls, and check behaviour controls are adhered to – both of which minimise performance risk.

6.4 Discussion

Following Aron and Singh (2005) and Aron et al. (2005), the need to assure effective risk management by achieving a balance of types and different levels of control and/or trust can be related to the nature of the tasks outsourced. However, there are limits on such prescriptive models that present risk related to causal relationships between factors focussing only on the attributes of transactions. Instead, these cases show how choice of control can be seen as evolving (eg, trust can go into reverse), to be influenced by local contextual issues (eg, attrition in India) and attitudes (eg, perceived need for secondment), and that control and/or trust is shaped by particular historical circumstances (eg, Alphacorps's long-term vendor relationship) and the actions of individuals and groups (eg, the Gowing contract manager, Technoaccounts reneging). Effective control of offshore outsourcing is as much a social process as a technical one. Outsourcing codifiable processes does not limit control to outputs and behaviour as we observed social control to be as a major feature of the Alphacorp–BetaCom relationship. Managers thus need to select from an appropriate range of controls based not just on transaction characteristics alone but the anticipated future of the outsourcing relationship.

Small firms can engage in offshore outsourcing and there is a role for consultants, lawyers and other intermediaries to assist in providing standardised contracts and guidance at a reasonable price for small clients. The Ardon–Technoaccounts case is much smaller in terms of scale and scope than either of the other cases. At Ardon, cost savings were not a major factor underpinning the decision to outsource to India. Instead, the major benefit and challenge was seen to lie in standardised output and constant labour supply. We were told that the savings achieved as a result of outsourcing offshore were roughly commensurable to outsourcing to UK-based freelance homeworkers and thus dramatic cost savings were not achieved. This can be explained by considering the relatively small volumes outsourced compared with Alphacorp or Gowing. Small firms have the potential to use offshore outsourcing successfully, at Ardon offshore outsourcing led to several benefits such as a focus on consultancy services for clients. Small firms considering offshore outsourcing should consider a predefined strategic planning goal beyond cost savings prior to offshore outsourcing.

Guidance and recommendations on appropriate disclosure of offshore outsourcing should be provided. Our interviews revealed that some firms of chartered accountants do not inform their clients that their accounts preparation is outsourced to India.

Vendors should be cognisant of the imperative for risk mitigation and present clients with a range of controls according to type of work to be outsourced. Clients such as Gowing which are outsourcing considerably more than simple codifiable generic transactions expect 'value added' from vendors beyond reduced cost and quality within SLA tolerance limits. Effective management of such relationships requires client access and active participation in areas of the vendor's operation which might previously have been considered 'out of bounds' to clients. Clients have responsibilities to vendors too which can be formally and informally acknowledged, for instance, Alphacorp was governed by the OLA to enable the vendor's SLA. For the control and innovation of higher value added activities, leadership style and communication skills become as crucial as technical

ability. It is not however the solution for clients to think of BetaCom as an extension of their accounts department as that may lead to tensions around boundaries and responsibilities. After all, vendors have responsibilities to many clients. However, the Gowing case shows that clients expecting more than the processing of generic rules-based codifiable processes must expect to put a lot of effort into helping vendors 'get it right' supported by open gainsharing contracts. Vendors in turn must feel motivated to welcome, encourage and facilitate client access to form close working partnerships.

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