The True Cost of Outsourcing IT Departments

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Outsourcing IT departments has major implications for the companies and the economy of the home country. Parry and Graves (2008) noted that the financial cost factor was the main driver for outsourcing in the last decade of the twentieth century, but companies were increasingly basing their decisions on several factors. This change in outsourcing decisions is influenced by the notion that outsourcing has hidden costs. The true cost of outsourcing IT departments includes the cost of transition, loss of managerial control, loss of key internal skills and negative effects on the economy of the home country.

The cost of transition involves choosing a vendor and transferring the work to the selected service provider. Vendor selection includes steps such as defining requirements, sending out requests for proposals and examining offers, and contract negotiation. This element of the cost of outsourcing amounts to about 0.2% to 2% of the total financial costs (OSF Global Services, 2012, p. 2). The cost of transition includes the cost of communications, legal fees, and technical costs. This cost varies with the size of the IT department. Companies require sufficient resources to select the appropriate vendor and transfer the department successfully.

The loss of managerial control over the outsourced function is a major limitation of outsourcing and has wide implications for the company. Outsourcing expands traditional organizational boundaries, giving rise to new challenges and the need to adapt the management of IT departments to match the change (Aubert & Rivard, 2008, p. 163). Important issues like the quality and reliability of IT systems is partly or wholly transferred to the service provider. Management loses control of these critical aspects of the department, increasing the risk of disruptions to operations.

The loss of key internal skills due to outsourcing translates to high costs of IT systems in the long run. The practice hampers the development of internal technical skills in the organization, which can undermine the company's competitiveness (Aubert & Rivard, 2008). The company incurs additional costs to transfer the work to another provider if the current provider becomes incapable of delivering the service. Similarly, if the company decides to return the outsourced function to in-house provision, initiatives to develop the required technical expertise increase spending significantly.

Outsourcing IT departments to providers located in foreign countries affects the economy of the home country in a number of ways, including through the loss of jobs, loss of revenue and reduced demand for the outsourced skills (Kohleick, 2008, p. 16). Part of the revenue in the outsourcing arrangement benefits the host country at the expense of the home country. Similarly, the host country experiences an increase in jobs while the home country loses jobs. The reduced demand for the outsourced skills in the home country influences the country's expertise negatively. Accordingly, the overall impact of outsourcing IT departments on the country is likely to be negative.

Outsourcing IT departments has financial and other hidden costs that affect both the companies and the home country. The true cost of the practice includes the cost of transition, loss of managerial control, loss of key internal skills and negative effects on the economy of the home country. Outsourcing decisions should involve a careful review of all the costs to establish whether the project is viable.

References

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