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Control of Relational Risk in Offshore Accounting and Finance Outsourcing: Case Evidence from UK and India

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Abstract

Many companies in USA and Western Europe are taking advantage of developments in information technology and outsourcing parts of the accounting process to vendors in other parts of the world. Offshore outsourcing of accounting presents some unique risks, control problems and challenges. In this paper we focus on the control of relational risk, a form of risk concerned with the potential for an outsourcing partner's opportunistic behaviour. Drawing on multiple case studies of global outsourcing relationships involving India based vendors and clients in UK, this paper identifies relational risks and the controls adopted by vendors and clients. It is argued that the findings have more general implications for the management of offshore outsourcing of administrative functions.

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Control of Relational Risk in Offshore Accounting and Finance Outsourcing: Case Evidence from UK and India

Introduction

Offshore outsourcing involves a relationship in which outside vendors in another country are used, and in which the client company has no direct ownership (Stack and Downing, 2005). Accounting and finance (AF) offshore outsourcing is part of a wider global outsourcing trend involving a range of activities including customer care and human resources (e.g. payroll) outsourcing. International Data Corporation (2004) predicts the worldwide AF outsourcing market to reach \$47.6 billion in 2008. Although other vendor countries are involved, India remains the favoured destination for offshore AF outsourcing (ATKearney, 2005). India's AF offshore outsourcing industry is experiencing rapid growth. According to India's trade association Nasscom, in 2005 outsourced AF revenues were \$1.84bn and the sector employed 126,000 people. By 2008, revenue is predicted to reach between \$2.5 and \$3bn (Nasscom, 2006).

The aim of this paper is to improve our understanding of relational risk in offshore outsourcing arrangements that call for the global extension of control beyond the boundaries of the firm and country. Relational risk is the risk of a partner engaging in opportunistic behaviour such as surreptitious cheating, shirking and renegeing (Das and Teng, 2001 a,b; Williamson, 1975). Opportunism, understood as 'self interest with guile', (Williamson, 1975) was chosen as our focus as it encompasses many of the concerns of potential offshore outsourcing clients (Price Waterhouse, 2005). When outsourcing to an offshore vendor, the activity is

undertaken across time and distance in a different embedded economic, institutional and cultural context (Dacin et al 1999), accentuating the potential for opportunism and presenting additional managerial challenges (Nicholson et al, 2006, Sahay et al 2003). To date no study has focussed on the globalisation of AF outsourcing, relational risk and control choices taking account of embeddedness.

The paper addresses three research questions: our first question is: *what are the relational risks of offshore AF outsourcing to India?* Secondly, following prior research (Das and Teng 2001a, 2001b; Eisenhardt,1985; Ouchi 1979; Nicholson et al, 2006), we would expect relational risk to be minimised with particular controls. Thus this paper extends previous research on control of offshore outsourcing (Nicholson et al, 2006) by examining *how vendors and clients use controls to minimise relational risks across time and space.* Thirdly, we are interested in *how embedded context impacts on control global outsourcing relationships.*

The next section examines the literature on relational risk, offshore outsourcing, embeddedness and control. This is followed by a description of the research methods. The forth section presents evidence drawn from an empirical study involving case studies of India based vendors and UK based clients outsourcing all or part of the accounting function. The sample of firms includes small and large vendor and client firms engaging in outsourcing of both transactions and higher value activities (e.g. management accounting). The final discussion and conclusion sections draw out implications for theory and practice.

Risk and offshore outsourcing

Risk in strategic alliances is defined as the probability and impact of undesirable outcomes. In outsourcing arrangements, risk is understood as potential for poor performance of an outsourcing vendor (performance risk) or of potential opportunism (relational risk) (Das and Teng, 2001a). Potential performance risks include disasters of natural causation or as a result of armed conflict. At a more operational level of analysis, sources of performance risk could be related to problematic communication between an India based vendor and client located across time zones and distance. Prior research points to relatively poor telecommunications in India, cultural differences, accents and language ability coupled with time-zone differences all of which accentuate communication difficulties. In addition, staff in India may lack knowledge of a client's business application, which may be difficult to transfer (Nicholson et al, 2006; Sahay et al, 2003; Sarkar and Sahay, 2004).

Relational risk, the focus of this paper, is 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 or in essence potential for opportunism. Either vendor or client, or indeed both firms may manifest opportunistic behaviour such as cheating, shirking, distorting information etc.. In this paper, we focus mainly on the potential for *vendor* opportunism, for example, deliberate shirking while claiming full payment and poaching of a client's proprietary business processes. A vendor may renege on promises made at commencement and stop investing in training of agents; or employ agents who are not as qualified as the agents they presented during negotiations. Another example of opportunistic behaviour is "vendor hold-up" where vendors renegotiate contracts after clients have migrated processes thus taking advantage of the difficulty the client would have in shifting its

processes to another vendor or bringing it back in-house (Aron and Singh, 2005; Aron et al, 2005).

Prior literature provides evidence of a heightened potential for vendor opportunism when a client out sources offshore to an Indian vendor. This can be understood at economic, institutional, and social levels of analysis derived from research into embeddedness (Dacin et al, 1999). The economic context of high staff attrition is a characteristic of the Indian offshore outsourcing industry. Industry average turnover rates for transaction processes are reported at around 30% per annum and much higher in call centres (Rai, 2005). Movement between firms is commonplace and poaching by competitors is normalised (Chiamsiri et al, 2005). Secondly, Indian legal institutions display many contrasts with that of Europe and USA. 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. Under the Safe Harbour Agreement between the US and Europe, US firms operating under the agreement pledge to protect data from European partners in accordance with European law. India has no such regulations and data protection and privacy is reliant on individual contractual controls negotiated between the client company and the Indian vendor (Nicholson et al, 2006). Myriad differences in formal and informal legal rules complicate attempts at contract enforcement and conflict resolution through the Indian courts. Thirdly, research and commentary on the Indian social context (Transparency International, 2006; Varma, 2004) presents evidence of widespread corruption. Nicholson and Sahay (2004) describe the experiences of a small UK software firm with operations in Bangalore who were surprised at having to pay bribes, often referred to as unofficial 'felicitation fees', to obtain equipment through customs and to expedite basic infrastructure

installation to their offices. Several high profile cases have been reported in the global public media of fraud and security breaches at Indian call centres (Ahmed, 2005).

Control

We adopt a behavioural definition of control as ‘a process of regulation and monitoring of individuals for the achievement of organisational goals’ (Das and Teng, 2001a). Prior literature in this area identifies two main types of control: formal and informal (Ouchi, 1979; Eisenhardt, 1985; Das and Teng, 2001a). Two further categories of formal control have been identified consisting of outcome and behaviour control. *Outcome control* consists of control of the final and interim outputs of a process. Outcomes, goals and rewards are pre defined and stated in the contracts and service level agreements negotiated between vendor and client. Typical examples of mechanisms of outcome control are key performance indicators to measure the required performance of a vendor against actual outcomes. *Behaviour control* consists of control of the process; the rules, procedures and policies to monitor and reward vendor staff. In offshore outsourcing, typical examples of behaviour controls may include codes of practice, rules and regulations, non-disclosure agreements; observation using seconded client staff or periodic meetings and/or phone calls. *Informal or social controls* are concerned with propagating organisational norms, values, and culture to encourage desirable behaviour. Eisenhardt (1985) defines this form of control as “clan control” and in contrast with formal control it 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 and objectives thus influencing behaviour. Socialisation and consensus

building of shared views serve to regulate behaviour and commitment to the organisation thus reducing potential for opportunism.

Choice of control depends on the attributes of the transaction and the potential for measurement of the outputs and monitoring of behaviour (Das and Teng, 2001a; Aron and Singh, 2005). Das and Teng (2001a) attempt to link risk and control and posit that relational risk will be reduced more effectively by behaviour control than output control. This is because relational risk is concerned with surreptitious or underhanded vendor actions that cannot be detected by examination of outputs but explicit clauses and other ex post deterrents may regulate conduct. Social control would be appropriate for reducing relational risk where behaviour control is difficult to impose. This is because of the difficulty some activities presents in predefining outcomes, imposing codes of practice or where surveillance may be regarded as deleterious to performance. Other authors such as Aron and Singh (2005) and Aron et al (2005) also focus on the characteristics of the transaction to minimise risk. *Chunkification* is concerned with dividing any business process under consideration for outsourcing 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, 2005:38). 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).

Research into embedddness does not attempt to match controls with risk types or to reduce risk by redesigning the tasks. Instead the importance of context in control design is emphasized. Elharidy (2005) argues that management control systems in globalised outsourcing relationships are embedded within a web of interactions that are influenced by the surrounding local environment. When control is stretched across

time and space, Elharidy argues for the effects of context on management control systems at economic, institutional and social levels of analysis. For instance, at the institutional level, an environment with relatively weak, slow or corrupt legal system explains the tendency towards social control of outsourcing relations, as contract enforcement is highly problematic.

The theoretical frame is thus comprised of relational risks and two separate perspectives on risk reduction drawing on transaction attributes linked to control (Das and Teng 2001a, Aron and Singh 2005, Aron et al 2005) and secondly acknowledging that offshore outsourcing involves multiple embedded contexts which impact control choice and effectiveness (Dacin et al 1999).

Methodology

The research approach for this study is intensive case study (Walsham, 1995; Yin, 2002) and data collection was carried out between 2001 and 2002 and between 2005 and 2006 in client and vendor organisations in three core case studies all of whom have some outsourced work undertaken in Indian processing centres. The resulting case studies are used to illustrate how risks are mitigated in offshore outsourcing cases of different size, and types of accounting outsourced. We have chosen to focus on vendors with India centres as India is currently widely regarded as the most attractive location for offshore outsourcing and is regarded as the leading country in terms of its volume of offshore accounting and finance work undertaken for foreign clients (Nasscom, 2006; ATKearney, 2005). Pseudonyms are used since access was granted on condition of anonymity.



Case Description

The cases are identified as A, B and C. Each case is comprised of vendor – client couplets thus the sample contains vendor A, B and C linked with the corresponding client. The cases were chosen because of the variances in size of the client and vendor firms, numbers of transactions and scope of accounting activities outsourced. Case A is one of the largest examples in the world of offshore accounting outsourcing in terms of firm sizes and volumes of outsourced transactions. Client A is a global chemical company with headquarters in Europe. It also has well-established operations in North and South America, Australia/Asia and Africa. Client A's turnover in 2005 amounted to over \$20 billion. Currently, the Accounting and Finance (AF) department in Client A employs over 4,000 people. AF operations across Europe are outsourced to several European hub centres and thereafter to India. Vendor A is one of the largest global accounting outsourcing vendors with global centres including its centre in India. Revenue turnover in 2005 was over \$200 billion with over 90,000 employees. The AF services being outsourced from Client A to Vendor A and undertaken in India now include cash and banking, reconciliation of account payable to general ledger, fixed assets, and accounts payable such as the processing of invoices and vendor set up.

Case B has many similarities with Case A in that both are in third party non-equity outsourcing arrangements and have a proportion of India based processing. Client B outsource a smaller number of transactions but a wider scope of accounting activity than Client A. Client B outsource almost 90% of its accounting function while Client A only outsource transactional processing work. Client B by the end of 2004 employed 17,000 staff. In 2003 and 2004, Client B was struggling to manage debt and the resulting financial restructure plan included cost cutting and outsourcing of AF

activities. In 2004, Client B engaged in a competitive tendering process to choose an AF outsourcing vendor. Vendor B was short listed and won the contract. Vendor B has regional coverage (USA, Europe, and Asia) and has several offshore centres particularly in India. Its group overall revenue in 2005 was over £300 million and over 6,000 employees of which 3000 are based in India. Client B outsources transactional processing, accounts payable, accounts receivable, payroll, and business expenses, as well as financial reporting.

Case C is of a relatively small chartered accounting firm in England (Client C) and their relationship with a localised provider operating from Bangalore (Vendor C). The case is much smaller in terms of scale and scope than that in either Case A or Case B. In 2006, Client C had an approximate revenue turnover of £600,000, and ten employees, three of whom are part-time. The decision to outsource to Vendor C was taken in April 2005. Vendor C was established in February 2002 and has a small operation centre in Chennai employing 30 staff with revenues commensurate with Client C.

Data Collection

Data has been gathered using multiple semi structured interviews involving 52 hours of interviews with 35 individuals including accountants and senior managers at the three companies located in the England, Vendor A's European hub and the three vendor's India centres. Data was also gathered from interviews and informal discussions with accounting and finance outsourcing experts (consultants, lawyers etc) in the UK and India. The interviews were taped, transcribed, and summarised. We took notes in interviews that were not taped. We did not have predetermined interview protocols but sets of issues to discuss with the respondents drawn from the

theoretical framework discussed in the previous section. These issues changed over time. In the initial set of interviews with all three cases, we focused on developing a historical reconstruction of events prior to the start of the study. Subsequent meetings focused on understanding ongoing challenges related to control of risks. Secondary information was gathered from corporate web sites and internal publications including press releases and related trade data. In between the interviews, we had the opportunity to observe the office layout, how people worked together, and the kind of activities that took place in the course of normal everyday work. These observations were interspersed with informal conversations while having a coffee break for instance. Research diaries are maintained to record our interpretations during the course of the inquiry.

Data Analysis

Data analysis was undertaken by identifying issues, interpretations and themes through a process of multiple individual readings of the transcripts followed by intensive periods of discussions between the researchers. These discussions were supported by our reading of relevant literature, which we attempted to relate to the case data using data displays (Miles and Huberman, 1994). We prepared a report in which we summarised our findings in relation to the theoretical framework and made some suggestions for action. This report enriched the subsequent analysis, verified our interpretations with case respondents and facilitated discussion and comments between the authors, colleagues in our respective universities and other industry stakeholders.



Findings

This section first considers the relational risks in the categories of poaching, fraud, renegotiation and renegeing in offshore outsourcing. We then describe the control modes used in each of the cases. Subsequently in the discussion section we reflect on the choice of control and importance of embeddedness.

Relational Risk :Poaching

Actors in all three cases (vendor and client) presented views on the potential for poaching of processes and of staff. A manager in Vendor A highlighted the possibilities of using Client A's systems or processes for promoting to new clients:

'If the next big chemical company comes to us then we will be able to say well actually we do this for Shell, we do this for Client A, it may well be you want something similar.' – Service Manager, Vendor A

In Case B, there were instances where documents or processes would be shared and subsequently used by vendor or client:

'There are times when they (Client B) have taken our documentation and would use the documentation. For instance, they have a project initiation document and they have tended to use that in their own projects now. All our procedures are documented and they're all in our project library.' – Operation Manager, Vendor B

However, the poaching of documents and processes was not, in the main, regarded as opportunistic behaviour by either party and the 'poaching' was tolerated and considered quite unimportant. Moreover, it was regarded by some interviewees as essential sharing and part of the elements, which constituted their 'partnership' approach to outsourcing, embodied in the contracts though not formally stated. Opportunistic poaching of staff by competitors or staff leaving without observing

employment contracts was common. Several vendor interviewees across the cases confirmed the industry average attrition level at 35% to 40%. The risk was perceived by clients in relation to providing resource to their competitors:

'We don't want to be the training resource for our future competitors but it happens and we have to make sure Vendor A are managing their staff so that we don't have an enormously high staff turnover'
– Contract Manager, Client A

From the vantage point of Indian vendors, there was a strong perception that their experienced staff move or are poached by competitors in part as a result of the nature of outsourced work. We were told by a Finance Director of Vendor B in India that 'routine transactional jobs if given to qualified accountants will lead to boredom and their expectations will increase, because of the monotonous work'. Taken together, limited career development and monotonous work contributes to vendor staff dissatisfaction and frustration, thus encouraging them to seek better job offers.

Opportunistic poaching was seen to take place within clients' own firms exploiting the previously established offshore outsourcing relationship. In an interview with a consultant in India we were told of how a UK based qualified accountant who was an employee of a small UK chartered firm outsourcing its client work to an Indian firm had acted opportunistically by resigning and setting up a new business. The relationship with the offshore outsourcing firm switched to this new firm enabling the now ex-employee to poach her ex-employer's customers without employing any new staff or setting up large office infrastructure etc. Clearly, outsourcing increases a client firm's vulnerability to such opportunistic action as the role of the chartered accounting firm is as intermediary and it was simple for the Indian vendor back office to switch. Potential for this act of opportunistic poaching was not covered within the original contract and we were told it would be problematic for legal action to be taken in the Indian courts over the vendor's complicit cooperation with the new firm.

Perceptions of fraud in India

There were common perceptions across the cases on the potential for fraud in India. European managers and Indian vendors alike could not see why India presents a greater threat of fraud than elsewhere contradicting much of the prior evidence of the propensity for corruption in India. A contract manager in Client A argued:

‘The need for a job in India is far stronger than the need for a job in UK and therefore the temptation to break the law and risk job is lesser. The developing country context makes no difference to people’s honesty and integrity.’

Similarly, the view of an operation manager in Vendor B, India concurred with the contract manager:

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 UK or anywhere. – Operation Manager, Vendor B, India

The director of Client C perceived that the processing of accounts in India actually diminished the potential for breaches of client confidentiality. This company’s local environment is a relatively small town described as a ‘closed community’ and UK based staff were given explicit instructions to prevent disclosure of client business affairs outside of the office environment. The Client C director perceived that:

‘The very fact that the people doing the transactional work are 5,000 miles away, I think is a bit of a benefit for confidentiality’.

A contrasting perception was given by an interviewee with a consultant who although felt that potential for fraud was no greater than in UK or USA told us of potential for extortion. We were told that some client’s accounting practices when outsourced offshore were considered “dubious” by Indian staff such as spurious attempts to claim tax relief on inappropriate expenditure. These tax avoidances if detected by staff in an

Indian outsourcing centre present the risk that UK clients could be blackmailed by India based vendor staff.

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Renegotiation and renegeing on promises

Certain tensions around renegotiation and vendor hold-up were mentioned in both of the larger client firms in the sample. A project manager in vendor A explains :

'The accounts had been outsourced for several years ... Client A no longer has knowledge of what accounting is required'.

Thus, Client A at one level appears to have been placed in a position of vulnerability to opportunistic renegotiation. However, the renegotiation risk is shared by the vendor as they face considerable risk of underestimating the complexity of work required on client processes when outsourced and the potential for client refusal to renegotiate. Vendor B exemplified this when they accepted processes, which were outsourced in a crisis, much of which was considered to be 'broken'.

The main thrust of comment on potential for opportunistic renegeing came from Client C who were disappointed that certain promises had not been met by their vendor. Vendor controls that had been promised were not realised and Client C's director told us:

'We were told specific things, a file will receive two reviews from a chartered 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.'

Secondly, it emerged that promises concerning Vendor C personnel associated with the Client C 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

files...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, Client C

These episodes had caused a regression in the relationship shown in the reluctance of the Client C’s director to act as advocate of Vendor C to prospective users, a role he had previously enthusiastically fulfilled.

Control Responses

A range of controls were adopted across the cases to minimise the relational risk. In the sections to follow, we consider each of the control types identified in the theoretical frame above drawing on the categories derived from Das and Teng (2001a), Ouchi (1979) and Eisenhardt (1985). We provide some analysis of the effectiveness of these controls in minimising relational risk.

Output Control

Output controls at Client A consisted of the timing of key outputs: payroll dates, year end etc. Secondly, the evaluation of the outputs consisted mainly of contractual key performance indicators (KPI), which in Case B were sanctioned by service credits. This credit is the amount payable to the client if the vendor fails to meet the service requirement. The service credit is negotiable depending on vendor’s explanation of why they could not meet the KPI. However, KPI figures themselves were perceived as limited in providing contextual data and also were not considered to present the ‘true’ picture of the vendor’s performance. The objectivity of KPI information as a mechanism for detection of opportunism is brought into question when considering the potential for misinformation from vendors:

'I could look at what I do and I could come to the conclusion that actually what I needed to do was to deliberately fail Y in order to achieve X, even though for you as a client that is not the smartest thing that you want me to do. I could create a situation that says, I'm fine, I did exactly what you asked me to do, but over here, we have disaster.' – Client Director, Vendor B

This evidence from the case causes us to concur with Das and Teng (2001a) that output controls are very limited in aiding the detection and prevention of opportunism in outsourcing relations.

Behaviour Control

All three of the major case studies had in place behaviour controls in the contract and service level agreement focussing on specifying desired vendor behaviour, enabling client surveillance; information and communication systems, controlling attrition and implementation of standards. The first element of specifying behaviour was set out in the contract. Data protection and confidentiality agreements based on UK law were incorporated in all three cases. The contract at Vendor C also promised not to employ external staff or subcontract to protect confidentiality:

'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–Director Vendor C

Secondly, the reporting structure provides role specifications to facilitate the process of client supervision and monitoring of vendor behaviour at a distance. This control is both by the client and on behalf of the client. For example, the Finance Manager of Vendor B in India is required to report performance and associated issues to the Client Director of Vendor B in UK. Any communication between the contract manager of Client B and Vendor B in India is made transparent to the Client Director of Vendor B in UK. In addition, Vendor B is contractually obliged to produce a monthly service

performance report for Client B. The almost constant communications between Client C and Vendor C using MSN chat messenger enable checking on progress together with an online web based “dashboard” enabling the presentation of key metrics updated several times during a day.

Control over high attrition levels in the India context was perceived by the clients in the sample as a vendor related task. Vendors try to address this in different ways. Career growth includes moving staff into new client tasks, processes, or service lines:

‘They’ve been given a change not only in terms of moving to a new client, which means new exposure, and also may be an opportunity to travel to the UK, because every travelling experience is an experience. We are also trying to move people within the processes, within the same client or to a different service line.’ - Finance Director, Vendor B, India

However, this rotation of staff and duties to control attrition had some unexpected consequences. Vendor A staff in India have over time built up knowledge of the unwritten rules or tacit nature of the outsourced task or process. Client A produced a list of key words used on invoices for India based staff but many additional words and phrases were required and a full lexicon was never developed and transferred. This was because the list would require constant updating and some aspects were tacitly understood by the Client A’s employees. Staff have to learn “on the job” on a ‘case by case’ basis from peers. A change of staff member through rotation or attrition would reduce the efficiency of the process, add to errors and thus increase the amount of processing and supervision time necessary.

Another attempt to control attrition presents employees with a structured career path. In the Vendor B India centre, there are three levels of employees known as bands. The India based Finance Director told us:

'I tell them that you should really challenge your team leaders, your managers so that you vie for that position'.

Once again, this presented a tension as staff are all highly qualified often to postgraduate level and a route to promotion cannot be granted to all so there is an inevitable attrition.

Vendor B emphasises the use of an exit policy requiring a notice period in order to overcome the issues of staff poaching by other companies. However, this informally agreed practice between established firms in the local cluster is increasingly being ignored by new firms moving into Bangalore and desperate to recruit staff to set up their operations. Vendor B is working with India's software and IT-enabled services industry body NASSCOM, on an agreement to prevent poaching of experienced staff. However, it is unclear if any serious sanctions can be imposed by Nasscom beyond a voluntary code. Vendor B also tries to control poaching of staff through various training incentive schemes as there is an expectation among potential new recruits for training and they will use this as criteria in assessing competing job offers. Other behaviour controls focussed on strict codes of conduct regarding Vendor C staff contacting the clients of Client C. We were told by a senior manager of Vendor C:

'We have written in contract of employment in India, that if any member staff ever calls another client, or client's client, they will lose their job by the time they put the phone down.... If you do it, you lost your job, we will sue you. There is no way you can prevent people, you can't prevent people from doing things, the thing you can do is to make them aware of the legal consequences.' – Director, Vendor C

Policies prohibiting non-business email and online chat are also in place in employment contracts. In addition, the traceability of bookkeepers on each job is recorded so in the event of any misdemeanour he or she could be traced. In Case A, there is an exclusive agreement allowing Vendor A to bring other clients to the India

centre but they cannot poach key nominated staff. This reduces the potential for the vendor moving inexperienced staff onto the account and also guards against potential for fraud. Trusted staff working on areas where fraud could take place would not be rotated or replaced by unknown personnel possibly with criminal convictions. In addition, Client A is involved in the recruitment of vendor staff and can ask Vendor A to remove any person working on their account. We were told by one of the interviewees in Vendor B, India that their hiring policy strictly depends on reference checks such as checking the records, checking the previous employer's recommendation, and checking on a published blacklist produced by the trade association Nasscom.

Physical and systems security are part of behavioural control elements to reduce fraud risk. In Case B, ID cards and security guards control entry to the buildings and internal office areas. The site itself is fenced and guarded by security personnel. Control over computer systems is governed by independent IDs and passwords. These are in accordance with BS 7799 compliance of information security. At Vendor C, physical security controls are installed including the removal of CD writer drives from computers and complete removal of floppy drives and USB ports. We also observed the physical and systems security in Vendor A centres. These include the use of security cameras, mobile phone detection, and a clean desk policy. The security camera monitors the activity of the team members, while mobile phone detection prevents use of mobile phone and cameras. Clean desk policy requires desks to be cleared when not attended. There are also system securities such as creation, validation and maintenance of ID, firewall and anti-virus system, which is reviewed and reported to Client A.

Auditing is also part of the behavioural control mechanisms used to mitigate the risk of fraud. For example, Client B requires Vendor B to be audited:

We are audited by our clients, internally and externally, as if we were apart of their business.

Ernst and Young and Deloitte Touche have been around here. We do get audited in India, but so far it has not increased costs. – Director, Vendor B

There is also Sarbanes Oxley audit of the process and controls in India in the case of Vendor A. An internal control manual lists out the control that Vendor A has on Client A's processes and provides guidance on how tasks should be completed.

Social control

'Bridge' actors – Client B's contract manager was an important actor in facilitating social control. She inculcated a sense of mutually shared objectives, solved communication and cultural issues between vendor and client. This was done by taking frequent trips to India, networking with Indian staff, informal socialising and making regular phone calls to the India and UK sites of the vendor. This actor was keen to work proactively and participate alongside the vendor staff in identifying and working towards process improvements, which might require vendor or client to make changes. Over time, Client B's contract manager became perceived as an ally by Vendor B's staff since her political influence with Client's B senior management enabled explanation of Vendor B's difficulties removing any suspicion they may have of Vendor B's opportunism. Several quotes from the vendor staff give impressions of this actor:

'She comes here and looks at the service delivery, the metrics, and any areas that need improvement.' – Team Leader, Vendor B, India

'Typically, she will come here saying that, yes these are the issues UK people feel they are facing with India. We will give sufficient answers for that. We will also give her list of issues, which we are facing there.' – Finance Director, Vendor B, India

She (the contract manager) is trying to highlight the weaknesses in their (Client B) business that are causing us problems so if we could do something quicker and better, whether it's Client B are holding us up, then she's prepared to take that back – Operation Manager, Vendor B, UK

In Case C, the bridge actors were known as account handlers. We met three of the account handlers during our visit. We were struck by their excellent communication skills. Although Alice is Indian in appearance she is of part British parentage. Her mother tongue is English and is spoken without accent and as a result builds a strong rapport and is much liked by UK based clients. We were told of how clients had made special visits to see her.

A further example of bridge actors facilitating social control was in Case A, where Client A seconded a key staff member to Vendor B hub in Europe. The seconded person was actually involved in a managerial position for a period of several years and during that time was responsible for any issues raised by Client A and Vendor B. The Client A's contract manager explains:

'She is important to Vendor B because she gave them the quality, the knowledge, and the experience of how things work within. The fact that she knows each person in Client A from history allows her to deal with him or her effectively. – Contract Manager, Client A

The effect of the permanent presence of this person in the vendor's centre in a senior management position was to provide impetus for partnership. This actor actively assisted Vendor B in sharing knowledge, overcoming conflict and at times defending the vendor against her employers. An important facilitator of social control was the contract. The Client B contract manager interpreted the open book contract as ensuring complete access to all accounting process outsourced to Vendor B:

If I want to know anything, I can see or ask for it ...we cannot be distanced from the outsourcers ... I see it as an extension of Client B's accounting dept.' – Contract Manager, Client B

This contract facilitated the access to enable social control as discussed earlier. The contract also provides guidance on the cost of services, and how to share the savings. This dynamic attention to pricing and gain-sharing possibilities mitigates the risk of vendor hold-up.

Discussion

Relational Risk of offshore AF outsourcing

Prior literature (Ahmed, 2005, Transparency International, 2006; Varma, 2004) suggests the importance of social embeddedness pointing to increased propensity for corruption in India. However, our findings from respondents across the cases generally considered that India presents no heightened risks than elsewhere and may even benefit confidentiality. Nevertheless, we found potential for poaching of processes and documents in Case B, however this case shows that opportunistic poaching as portrayed in the control literature is not universally detrimental to alliance performance and in some circumstances such sharing may demonstrate mutual openness and lead to beneficial consistency. In case B, both vendor and client tolerated poaching of processes and both sides were seen to engage in this practice quite freely. Interestingly, some interviewees regarded 'poaching' of this nature as essential sharing and one of the informal control mechanisms facilitating partnership in the outsourcing relationship. We thus contribute an additional facet of opportunistic poaching and mechanisms of social control to established control literature.

The practice of offshore outsourcing of accounting and other processes introduces new risks for clients of offshore vendors. For instance, we show how

existing employed staff in a client's firm chose to act opportunistically taking advantage of offshore outsourcing outside of the client's embedded institutional setting. After setting up a new company, the ex employee was able to take advantage of the India setting of the vendor who enabled her ex employers clients to be poached without legal redress in UK courts or from the UK chartered accounting institutes. Other aspects of institutional embeddedness are pertinent when accounts are processed in India. The jurisdiction of UK policing does not easily extend to India in the event of extortion.

Control Used to Minimise Relational Risk across Time and Distance

Prior research (Aron et al, 2005; Das and Teng, 2001a) posits that relational risk may be effectively controlled by social control or/and behavioural control. The findings cast further doubt on the effectiveness of output controls in relation to relational risk and we thus concur with Das and Teng (2001a). We found that output control is limited as a mechanism for detection of opportunistic behaviour.

Behaviour control to overcome risk of fraud included contractual clauses for data protection and confidentiality designed to overcome the lack of legal enforcement mechanisms. The use of web based "dashboard" showing key metrics; policies prohibiting non-business email, use of mobile phones and online chat and measures for physical and systems security; auditing and standards demonstrate how behaviour controls may be stretched across both time and space extending the assumption of proximity implied by the theoretical control literature to outsourcing relationships within different embedded contexts (Das and Teng, 2001a; Eisenhardt, 1985, Ouchi, 1979).

The findings of case B, where social control was extensively used, cause us to concur with Das and Teng (2001) that social control may be used to control opportunism. In this case, activities where social control was focussed were of an unstructured nature where output and behaviour control were not easily implemented thus causing us to concur with control choice based on transaction characteristics (Aron and Singh 2005). The contract manager at client B did not use social control for highly structured activities such as payroll where output control was the main control mode. However, it is easy to see considerable tension emerging in case A where the client outsources only transactions contributing to the spectre of high staff attrition in India. This case exposes a limitation of isolated decisions to reduce risk focussing on the characteristics of the transaction in isolation of embedded context (Aron and Singh 2005, Aron et al, 2005). This literature assumes outsourcing to take place in a homogenous environment (i.e. within the same embedded context) and takes no account of the embedded economic, institutional and social differences in context between UK and India. Case A demonstrates that the decision on what activities a client outsources to a vendor has impact on the level of attrition a vendor may experience and the concomitant effects on the client in terms of loss of trained staff. The level of educational attainment for vendor staff across all three cases was to at least bachelor's level and in many cases to postgraduate. Such staff are mobile between the many firms locating in the major Indian clusters around Delhi, Chennai, Mumbai and Bangalore. Clearly, the attributes of the transaction itself are not sufficient to decide management control strategy as the impact on the highly qualified India based staff of outsourcing only mundane transactions is to cause them little enduring job satisfaction, noted as important by Mumford (1991) among others, and to act as an incentive for vendor staff to leave to other client accounts or to another

competing vendor. The unexpected consequence of the decontextualised decision based on transaction attributes alone thus presents a new set of risks and consequences to be controlled by both client and vendor.

Our findings show the importance of bridge actors and secondments in facilitating social control in global outsourcing across country boundaries. The role of bridge actors and secondments within the aegis of an open book contract allowed both clients and vendors to develop a consensus and mutually shared objectives acting as a deterrent against either client or vendor opportunism. These actions of bridge actors in various ways were able to inculcate consensus building, shared views and behaviour; common values and atmosphere of socialisation presented by Eisenhardt (1985) and Das and Teng (2001a). However, implicit in these theories is an assumption of co location within a homogenous environment as opposed to the globalised nature of offshore outsourcing. Thus, a contribution of this paper is to extending this prior work to encompass additional complexities of global outsourcing relationships across multiple embedded contexts. A further example of the impact of embeddedness on control was shown in Case C, where both client and vendor are small firms with limited resources. Client C experienced several instances of renegeing on promises by the vendor, which can be explained by Vendor C facing difficulties in managing high staff attrition levels and in fulfilling expansion plans in India. The problems may be explained by the economic embeddedness of the Indian offshore accounting milieu which is characterised by high attrition. There has been a steep increase in the volume of work from Client C and other UK chartered accounting firms that have outsourced offshore to Vendor C. Far from Vendor C being able to choose from a massive labour pool as they expected, they are a small firm competing

for staff with large multinationals, and this predicament thwarts easy expansion and retention.

Conclusion

We have examined three cases of AF offshore outsourcing and present the relational risks and controls adopted by vendors and clients. This paper enhances our understanding of the globalisation of AF outsourcing; relational risk and control choices taking into account the impact of context on control. Theoretically, this study enriches prior theoretical and empirical studies (Das and Teng 2001a,b; Eisenhardt, 1985; Nicholson et al, 2006, Ouchi, 1979) on relational risk by providing evidence from outsourcing relationships situated across time and space and in different embedded economic, institutional and social contexts. We thus extend established theory on control and relational risk into outsourcing in global domains. This embeddedness emphasis enriches Das and Teng (2001a) on how firms may bridge the embedded economic and institutional differences associated with limited data protection and attrition. Additionally, this study contributes to an improved understanding of embeddedness (Dacin et al,1999) in the domain of risk and the impact of context on control.

The practical contribution of this paper is to a better understanding of the paradox facing many firms contemplating offshore outsourcing that offshoring to India: provision of cheap labour but problems of overcoming high attrition and limited legal protection. We unpack and illustrate the risks and controls taking into account economic, institutional and social embeddedness in control design which is a practical strategy managers could adopt.

A limitation of this study was that we focus only on the relational risks and thus future work in the area could be oriented to performance risks and examining the controls and influence of embeddedness. Secondly, we touch only briefly on the issue of size. Small firms are increasingly 'born global' and contemplate outsourcing offshore early in their evolution. However, they face particular problems in relation to resources and future research could thus focus on this issue.

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