

## **Determinants of Operational Risk in Global Sourcing of Financial Services Evidence from Field Research**

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We investigate the factors that lead to operational risk in offshore outsourcing of business processes. We base our model of operational risk on field research conducted in multiple countries over a period of several years. Our research shows that two principal factors determine the nature and extent of operational risk in offshore outsourcing. The first is the extent to which processes can be codified (or specified exhaustively). The greater the codifiability of a process the lower the extent of operational risk associated with offshoring the process. The second factor is the extent of convergence in understanding of the parameters of process quality between the buyer and the provider of services. The more objectively defined the metrics of process quality are, the smaller the operational risk. We formulate the idea of a “knowledge continuum” and show that the factors that determine operational risk originate in the nature of the information work that is carried out along that continuum. Finally, we contrast the efficiency and welfare levels associated with the three principal modes of offshore production of services and show that an emerging hybrid form of governance that we call the “extended organizational form” is the dominant choice for sourcing many kinds of services.