Offshore Outsourcing: Weighing the Risks of Data Protection and Security

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Overview of Outsourcing

- “Outsourcing is the transfer of internal business processes and capabilities to an external service provider”
- The basic commercial proposition is that the service provider will do:
  - what the customer currently does
  - at the same or a better level of performance
  - for the same or a lower price
- Key indicators/drivers of business transformation
  - Highly skilled labour arbitrage
  - Dramatically lower costs
# Offshore Outsourcing – The New Paradigm

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<th>Traditional Outsourcing</th>
<th>Transformational Outsourcing</th>
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<td>Key motivation for offshore relationship</td>
<td>Cost</td>
<td>Long Term strategic value</td>
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<td>Definition of Goals and Objectives</td>
<td>Tactical</td>
<td>Strategic</td>
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<td>Activity focussed</td>
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Types of Outsourcing: What is being outsourced?
Global Outsourcing Market: Continued Growth

Billions US$

<table>
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<tr>
<th>Year</th>
<th>BPO</th>
<th>ITO</th>
<th>TOTAL</th>
</tr>
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<tr>
<td>2001</td>
<td></td>
<td>44.6B</td>
<td></td>
</tr>
<tr>
<td>2002</td>
<td></td>
<td>86.0B</td>
<td></td>
</tr>
<tr>
<td>2003</td>
<td></td>
<td>120.0B</td>
<td></td>
</tr>
<tr>
<td>2004</td>
<td></td>
<td>182.1B</td>
<td></td>
</tr>
<tr>
<td>2005</td>
<td></td>
<td>242.0B</td>
<td></td>
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Global ITO Market - 2001: $44.6B
Global ITO Market - 2005: $86.0B
CAGR% = 17%

Global BPO Market - 2001: $92.7B
Global BPO Market - 2005: $182.1B
CAGR% = 18%

Source: Gartner
‘Offshored’ Global Financial Services: IT Spending

External IT Spending is Rising Rapidly, From 50% of Total IT in 1996 to Nearly 60% in 2006

Global FSI IT Spending (in US$ Billions)

Source: TowerGroup
Reasons for Offshoring

The Costs of Offshore Outsourcing Dramatically Change the Savings Equation

<table>
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<tr>
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<th>Potential Savings</th>
<th>The Cost of Effective Offshore Outsourcing</th>
<th>Actual Savings</th>
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</thead>
<tbody>
<tr>
<td><strong>ITO</strong></td>
<td>35–50%</td>
<td>3–5%</td>
<td>20–27%</td>
</tr>
<tr>
<td><strong>BPO</strong></td>
<td>45–60%</td>
<td>7–9%</td>
<td>18–26%</td>
</tr>
</tbody>
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**Source:** TowerGroup
Assessment Outsourcing & Relative Threats

- Strategic Planning
- Due Diligence/Assessment
- Human Resource Strategy
- Technology Strategy
- Risk Mitigation Strategy
- Compliance Issues (HIPAA, Gramm-Leach Bliley)
- Service Level Agreements
- Negotiating the Agreement
- Business Process Management
- Conflict/ dispute resolution
- Exit strategy

- Reviewing physical &
  - Logical security
  - Access, vulnerability
  - Internal and external threats

- Technology oriented threats
  - Cyber fraud, Phishing
  - Authentication
  - Risk assessment

- Compliance issues
  - Operational/transactional risks
  - Legislations and regulations
  - Watchdogs of Law
Offshoring Threats

- Hackers and crackers
- Industrial/ corporate espionage
- Trusted Insiders
  - Employees
  - Consultants
- Organised crime, Phishing, identity thefts
- Political stability and socio-economic impact
- Terrorism?
Offshoring Risks

- Country Risk: political, socio-economic, or other factors may amplify any of the traditional threats

- Outsourcing risks, including those listed below:
  - **Operations/Transaction Risk**: weak controls may affect customer privacy
  - **Compliance Risk**: offshore vendors may not have adequate privacy regulations
  - **Strategic Risk**: different country laws may not protect “trade secrets”
  - **Credit Risk**: a vendor may not be able to fulfill its contract due to financial losses
What Should be Protected?

- Personal Information
- Sensitive Information
- Health Information
Case Study 1 – e-Banking Services

- “The Tower Group estimates that the banks outsource 85% of their IT services”

- Reviewing Physical and Logic security controls:
  - Intrusion detection, location security and response capability
  - Network, system vulnerabilities and unauthorised access
  - Back-up databases and disaster recovery

- Reliable customer authentication mechanism:
  - Electronic agreements, digital signature
  - Secure access and transactions (e.g., Encryption, biometrics)
  - Prevent fraudulent transaction, identity theft, computer crime
  - Promote legal enforceability

- Periodic compliance and legal reviews
Key Threats to e-Banking Services

- Vendor management and risk issues
- Security, data integrity and confidentiality
- Authentication, identity verification, and authorization
- Strategic and business risks
- Business continuity planning
- Permissibility, compliance, legal issues, computer crimes
Case Study 2 – e-Healthcare Services

- “The U.S. healthcare market alone will touch $800 million for the Indian BPO companies in 2005” - NASSCOM report
- Involves emerging interactive technologies (i.e. interactive TV, kiosk, interactive voice response systems)
- Provides various products & services in Healthcare Management:
  - e-Health Services category includes:
    - Customer (Patient) Content (e.g. Transcription, telemedicine)
    - Medical supply distribution
    - Medical claim processing
    - Pharmaceutical outsourcing
    - Transplant Services
  - Health Insurance
Key Threats to e-Health Services

- Technology upgradation crucial - IT and health care
- Translation of results (eg. Remote diagnosis, remote hosting)
- Tension between innovation and sustainability
- Quality and the effects of technology on health care industry
  - Risk of loss of control, quality, and customer good will
- Internet-based Physician Portals (eg. quacks, fraud, liability, e-prescriptions)
- Support provider adherence to evidence based care
Data Privacy

- Privacy has various interpretations associated with it.
- In the EU it means an individual's (or a group's) right to determine what information about them is stored by, and passed to, whom.
- In the USA it tends to mean the individual's right to be left alone, free from interference or surveillance.
- There are legal implications, particularly in the EU where the Data Protection Directive prevails.
Privacy Strategy Spectrum

Act on Opportunity
- Enhance and protect brand and reputation
- Implement responsible customer relationship management
- Assure trust and confidence by consumer and business partners

Avoid Risk
- Legal liability
- Reputation risk
- Fines/penalties
- Adverse publicity

Enhance Operations
- Standardize processes
- Uninterrupted data flows

Stakeholder Value Enhancement

Operating Performance

Compliance and Prevention
Privacy and Outsourcing

- Securing communications in external environments
  - What laws govern?
    - Can offshore vendors satisfy Gramm-Leach-Bliley/HIPAA?
  - EU Privacy Directive
  - Technological security and testing
    - Are all reasonable and necessary steps being taken?
- Is vendor contract agreements sufficient to protect privacy rights?
Procedural Safeguards and Compliance Obligations

- Regulatory compliance obligations are generally non-delegable.
- Liability for non-compliance and reputational damage falls primarily on customer, not service organization.
- Requirements often evolving and still unclear; new additional requirements may emerge.
- Compliance may be costly both for customer & service organization.
Conflicting Priorities?

- European law on business transfers
  - Acquired rights directive - and “TUPE”
  - Data protection directive
  - Work council directive
  - Information and consultation framework directive

- Commercial Imperatives
  - Best solution
  - Knowledge transfer/ acquisition
  - Business continuity
  - Time frames

- Combined impact on the outsourcing relations
Thanks for your attention

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