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Managing Tacit Knowledge in Strategic Outsourcing

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1. Introduction

The globalization of modern economies and transition to integral knowledge society brings along complex issues of mastering outsourced activities, especially in managing tacit dimensions of knowledge transfer that takes place in outsourcing relationships. Relationships can be divided into several groups, among which the traditional and strategic ones are the most distinguished (Reuvid & Hinks, 2001; Espino-Rodriguez & Padron-Robaina, 2004; Linder, 2004). Traditional outsourcing is interpreted as a relationship in which the outsourcing provider can perform only well-controlled activities. This mindset has changed over the time due to fact that outsourcing providers usually have significant capabilities and a higher level of knowledge than outsourcers. Consequently, traditional outsourcing has evolved and transformed into problem solving (strategic) outsourcing (Linder et al., 2002), which seeks to achieve major changes in the company's performance (e.g., changes in business processes, access to new technology, innovation, productivity improvements) and is mostly based on long-term cooperation between companies that often develops into a business partnerships. Such outsourcing also enables companies to fully exploit investments of external providers, their innovations, and specialized skills and knowledge that would otherwise be very costly and almost impossible to replicate within company. In strategic outsourcing objectives and relationships between participants become very important; consequently, tacit knowledge dimensions (Polanyi, 1958, 1966; Howels, 1996; Rebernik & Širec, 2007) should be appropriately managed.

This chapter discusses some fundamental issues related to the importance of knowledge management in the outsourcing relationship. Managing the outsourcing relationship is incorporated primarily in the outsourcing process itself, and no special attention is paid to it, although it is crucial for the effectiveness of the outsourcing relationship. Such an approach neglects the importance of governing, supervising, and developing the relationship with the outsourcing provider, particularly because the outsourcing literature relates mainly to large companies (Rebernik & Bradač, 2009). A considerable number of organizations have had negative experiences with outsourcing because no relationship management had been established; this is an area in which a great deal of effort should be applied during the outsourcing process (Embelton & Wright, 1998). Rather, organizations have tended to establish teams of employees who govern the outsourcing process. In this process, participants involved in outsourcing activities share various information and exchange different types of knowledge and skills. Not only do they learn from each other,

but they also need to unlearn some previously used procedures, routines, and ways of doing business that have become obsolete in newly established outsourcing relations.

In particular, in a knowledge society aimed at sustainable development, the exchange of knowledge among different agents is becoming increasingly important. To embrace the knowledge and use it productively, a critical mass of knowledge and skills has to be present already in the company. Without an appropriate knowledge base, new knowledge cannot be absorbed (Cohen & Levinthal, 1990; Zahra & George, 2002; Schmidt, 2005). In this knowledge exchange, learning and unlearning are continually taking place in all knowledge areas and with all types of knowledge. It makes the phenomena of strategic outsourcing very complex and hard to comprehend. The processes are not only mutually dependent on social, cultural, economic, and political contexts, which differ from country to country, but are also concealed by tacit knowledge (Tominc & Rebernik, 2007).

We will investigate problems of managing tacit knowledge together with the importance of unlearning it. We will also examine possible opportunistic behavior in strategic outsourcing relationships and indicate possibilities for avoiding it. Based on surveys in the literature, we will discuss several types of knowledge and issues related to sharing, learning, and—most importantly—unlearning obsolete tacit knowledge dimensions as well as several important aspects of managing successful outsourcing relationships. When we take into account the needed collaboration, the holistic perception of business processes demonstrates that participants must be interdependent, be aware of their interdependence, and have a long-termed strategic interest in cooperative relationships. As the main problem of managing tacit knowledge lies in the fact that it escapes observation and measurement, an adequate framework that would make some dimensions of tacit knowledge visible and manageable has to be developed. To overcome the perpetual elusiveness of tacit knowledge, we present a framework that could help highlight dimensions of tacit knowledge that can be mobilized and observed through the manifestation of different behaviors. It is to a certain degree possible to make explicit some dimensions of tacit knowledge that not only contribute to successful sharing and mutual learning, but also enable the identification of those parts of knowledge that hinder the ability to accept novelties and should be unlearned. The better we understand the process of creating and using new knowledge and discarding obsolete knowledge, the more likely it is that companies will foster innovative behavior in companies and that the outsourcing processes will be sustainable in the long run.

This chapter contributes to a better understanding of the importance of knowledge management related to managing tacit dimensions on the level of cooperation between companies. The aim is to develop a model for managing different types of knowledge in strategic outsourcing relationship in such a way that it will develop into a sustainable outsourcing partnership. First, we introduce the strategic outsourcing relationship and its major management areas among which knowledge management is in the focal point. Furthermore, we explore the complexity of different types of knowledge and the learning/unlearning process of tacit knowledge dimensions in the management of the outsourcing relationship. In the turbulent and ever-changing business environment, tacit knowledge dimensions grow obsolete very rapidly and hinder change processes, so ways of unlearning this obsolete knowledge have to be found. To develop a sustainable outsourcing partnership in the long term, it is necessary to recognize possible opportunistic behavior that might occur at both parties in the outsourcing relationship and find ways to avoid such behavior.

2. Strategic outsourcing relationship

Outsourcing is a widely accepted business tool for transferring part of the business activities to another company to achieve different business goals. Commons (1931), Coase (1937), and Williamson (1983) explained that companies outsource when costs of in-house activities are higher than buying products and services on the market. According to Sharpe (1997), outsourcing is a management tool that affects the competitiveness of a company in such a way that its business strategies are based on core activities while non-core or supportive activities are outsourced. The concept is to have the management and/or day-to-day execution of one or more activities performed by a third outsourcing provider who is internally providing those same activities. We suggest classifying the outsourcing concept into three main parts regardless of its type, each with its own specifics and characteristics (Rebernik & Bradač, 2009): (1) the decision to outsource or not, (2) the outsourcing process, and (3) management of the outsourcing relationship. We focus primarily on the third part, in which problems of managing tacit knowledge are especially important.

Widely spread knowledge about outsourcing and its permanent growth has led to the extension of its use in all business areas. Based on the review of the literature, authors have classified outsourcing according to its effects; the commonly used classifications are traditional, which some authors call tactical (e.g., Espino-Rodriguez & Padron-Robaina, 2004), as well as strategic and transformational. The conventional concept of outsourcing indicates that the outsourcing provider can perform only well-controlled activities. Activities that could cause problems must be carried out in the outsourcer's company (Reuvid & Hinks, 2001). This mindset has changed over time as outsourcing providers may have significant capabilities and even higher levels of expertise. Consequently, the traditional outsourcing has evolved into more sophisticated problem-solving outsourcing. Other authors have similarly defined the traditional form (e.g., Greaver, 1999; Linder, 2004; Linder et al., 2002) and believe that this type of outsourcing focuses on cost reductions in order to achieve control in those areas in which the company does not achieve sufficient quality. Its foundation is to improve capacity at the operational level through the implementation of the same activities but better, faster, and cheaper. In such cases, the impact on the fundamental changes in the company is small.

Strategic outsourcing differs from the traditional outsourcing, which is based on the concept of performing the same activities at a lower cost while cooperation is static and unchangeable. Strategic outsourcing is based on changes in the management's perceptions and on continuous adaptations to needs and changes on the market (Reuvid & Hinks, 2001). The fundamental differences between traditional and strategic outsourcing lie in their objectives and in the relationship between the participants (Capgemini, 2004). The traditional form is typically used for outsourcing support and simple activities in order to lower costs due to economies of scale. Meanwhile, the strategic outsourcing focuses on core and supportive activities; it seeks to achieve further major changes in the company's performance (e.g., changes in business processes, access to new technology, innovation, productivity improvements). Its aim is predominantly to make a company more competitive by enabling it to stay focused on its core competencies. Strategic outsourcing—the core of our discussion—is focused on innovation and business improvements. Its main characteristic is a long-term relationship in which both parties stimulate and facilitate continuous and mutual business change in order to create value, develop capabilities, and manage uncertainty (Capgemini, 2004). As the strategic outsourcing relationship develops

over time, it relates to a deepening partnership and an increasing range of skills and has a more fundamental and significant business impact. Companies increasingly outsource activities that are crucial to the competitive advantage of the firm. In itself, this type of outsourcing can be beneficial if rents can be obtained from the relation (Mol, 2007).

Two main criteria for defining outsourcing as strategic are (1) strategic policy at the company level concerning outsourcing and (2) preparation to consider the outsourcing of core activities (Alexander & Young, 1996). Strategic outsourcing offers the possibility to manage step-by-step changes in the organization. It focuses on three main areas: technology, business, and finance. The essence of strategic outsourcing is the strength of an outsourcing provider that can take on existing services, implement new technology and business processes, and bundle these initiatives in an appropriate management of the relationship with the outsourcer to develop common knowledge and innovation.

In the management of outsourcing relationships, several issues need special attention. Power et al. (2006) classify these into six major areas: work administration, communication management, knowledge management, personnel management, training and education, and financial management (see Figure 1).
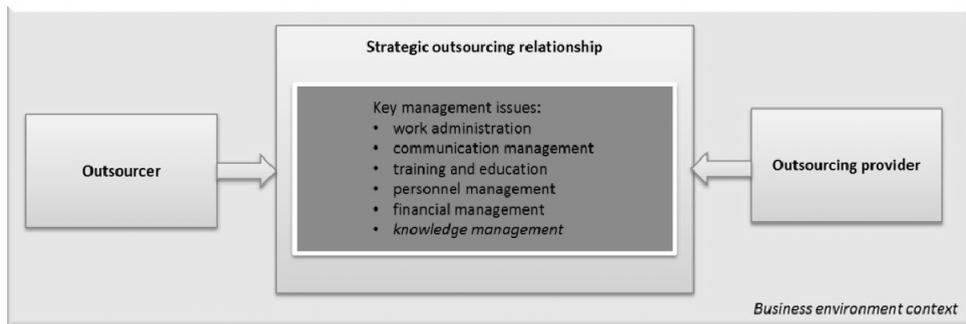

Fig. 1. Strategic outsourcing relationship management framework

Work administration ensures that the work undertaken is done and involves tracking work assignments, deliverables, and resource consumption as well as ensuring that the timeline is reached (Power et al., 2006). Communication management is especially crucial in the early stages of the relationship, when partners do not know each other. However, managers and entrepreneurs often believe that, when the contract is signed, their work is done. Over time, communication is simplified as the partners get to know each other. Training and education (Power et al., 2006) of the leader and involved employees is an inevitable part of process of building successful outsourcing relationships because cooperation with the other company brings about different ways of doing things, as cultures, forms of communication, and other issues are very often different. During outsourcing, the entrepreneur is constrained to gain new knowledge and experiences. Personnel management involves managing the employees involved in the outsourcing process and, when appropriate, establishing different teams (e.g., a governance team, a financial team). Financial management is the area in which monitoring and controlling are crucial, particularly in the early stages of cooperation and particularly if performance standards have not been implemented as agreed. Knowledge management involves sharing best practices, ideas, and innovations and improving processes with the outsourcing provider, which involves establishing new routines (Power et al., 2006); as such,

old routines have to be unlearned, and efforts have to be made to manage different dimensions of tacit knowledge that could hamper the introduction of new routines. As knowledge management is one of the most important areas in strategic outsourcing relationship, we will focus on this dimension of managing relationships.

3. Types of knowledge important in strategic outsourcing

Knowledge is a living asset; dynamic and volatile, it is often difficult to observe and understand. Unlike information, it is not final and stored, but emerging and being constantly recreated and socially reconstructed in particular work contexts. Knowledge may be tangible or intangible by its nature. Know-how, when articulated into the organization's database and operating technologies, is tangible. Similarly, explicit knowledge is tangible because it has been encoded into documents, databases, or some other permanent medium (Meso & Smith, 2000, p. 232).

All kinds of knowledge together, as an emerging synergy, make knowledge a system that, in combination with values, needs, and possibilities, is the starting point of any human action (Mulej et al., 2000). Thus, knowledge is an important part of a more complex system. On the other hand, organizations' knowledge resources have pertinently been described as an iceberg (Svelby, 1997; Haldin-Herrgard, 2000). Structured, explicit knowledge is the visible top of the iceberg; this part of the knowledge resource is easy to find and recognize, and therefore also rather easy to share. Beneath the surface of conscious thought lies a vast sea of tacit knowledge, derived from a lifetime of experience, practice, perception, and learning. This concept is captured in Polanyi's (1958, 1966) often-quoted statement, "We know a lot more than we can express"; therefore, this part of the intangible knowledge resource can be more difficult to share (Haldin-Herrgard, 2000, p. 358).

Tacit knowledge often enables us to perform at a higher level than our explicit knowledge does. For example, novices cannot become experts simply by being exposed to explicit information; they need to experience the activity itself and the cooperation relating to it. For these reasons, the success of a manager is heavily dependent on tacit knowledge. Therefore, supporting the sharing of tacit knowledge throughout the company will be possible with methods like apprenticeship, direct interaction, networking, and action learning that includes face-to-face social interaction and practical experiences. Four categories of tacit knowledge exist (Lubit, 2001, p. 166):

1. Hard-to-pin-down skills. "Know-how"; the word *skill* implies tacit knowledge. People need to repeatedly practice skills, receive feedback, and get a feel for them.
2. Mental models. We draw on mental models or schemas when trying to make sense of a situation; they determine how we understand and analyze situations—that is, how we understand cause-and-effect connections and what meaning we attribute to events. The schemas we use are often subconscious abstractions rather than explicit models we consciously employ; therefore, they belong to tacit knowledge. They affect whether or not we see people as trustworthy, whether we see opportunity in a situation, and how we judge risk.
3. Ways of approaching problems. Tacit knowledge underlies the decision trees people use.
4. Organizational routines. Much of a company's tacit knowledge is stored in its routines. This tacit knowledge embedded in routines includes an intuitive grasp of what data to focus on and of the relative priority of competing demands. In time, managers leave, but the routines remain as a legacy of their knowledge.

The difficulty of expressing, codifying, and transmitting tacit knowledge makes it easier for a company to protect it than explicit knowledge. Moreover, tacit knowledge may only be effective when embedded in a particular organizational culture, structure, and set of processes and routines. The difficulty of copying tacit knowledge enables tacit knowledge to be the basis of an inimitable competitive advantage (Rebernik & Širec, 2007).

In many industries, success in today's markets depends on the ability to learn about emerging market opportunities and rapidly develop and spread the knowledge necessary to exploit them, rather than the ability to engage in careful long-term planning. The key driver of superior performance today is the ability to change when the business environment calls for it and to find the shifting sources of advantage. As a result of these changes, the ability to acquire, develop, and spread new knowledge has become an indispensable core competence. When considering strategic outsourcing, such abilities are of special importance.

The ability to create new and valuable breakthroughs offers companies an unambiguous competitive advantage. Therefore, it is vital for a company to enable an organizational environment that will encourage unique, original, and unexpected innovations that are far more valuable from a competitive standpoint than innovations that are predictable, incremental, or mundane (Lynn et al., 1996).

Such an imperative requires a shift in the role of management in the strategic outsourcing relationship. Managers have to manage the organizational environment or context in which the relationship is performed rather than control the workers themselves (Stewart, 1997; Svelby, 1997). The management of the outsourcing relationship has to serve as a coach and facilitator, a boundary-buster, and head cheerleader. His or her role will be to eliminate the barriers that prevent individuals from performing at their optimum levels. Success in the strategic outsourcing relationship requires a new form of vision-based leadership (Davenport, 1993, pp. 117-37). This problem is multidimensional in its nature. Outsourcer and outsourcing provider have to consider a number of factors simultaneously. These factors, which exist at different levels, are presented in Figure 2.
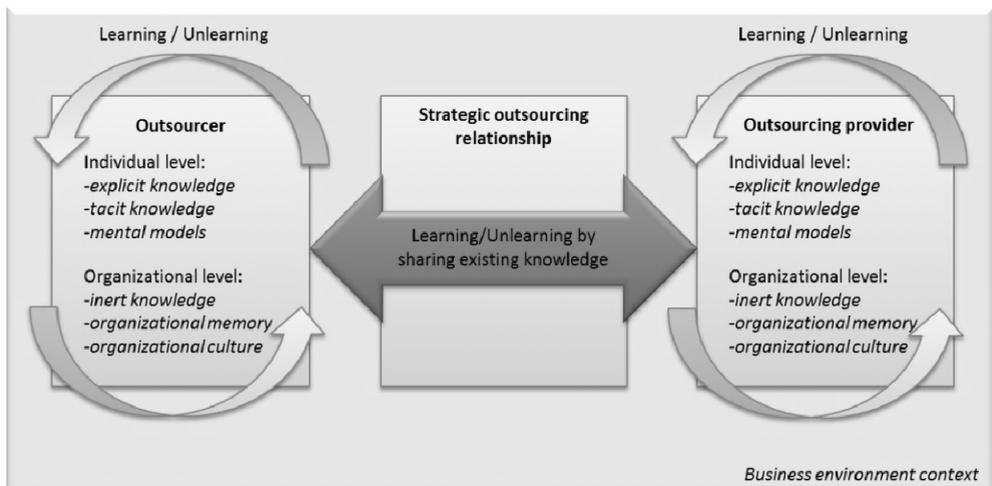

Fig. 2. Knowledge management attributes in the strategic outsourcing relationship

In the strategic outsourcing relationship, the outsourcer and outsourcing provider should get closer and closer in terms of common knowledge base, which requires sharing existing knowledge on individual, organizational, and environmental levels together with learning and unlearning obsolete knowledge. However, a particular problem always occurs when the knowledge must become visible to the other company.

At the individual level, researchers and writers have identified the difference between explicit and tacit knowledge. Explicit knowledge is widely accepted as knowledge that is recognized by the individual and therefore easily expressed or articulated (Nonaka & Takeuchi, 1995; Durrance, 1998; Newell et al., 2002; Roy & Roy, 2002). Explicit knowledge is sometimes referred to as codified knowledge. Tacit (or implicit) knowledge entails information that is difficult to express, formalize, and share. It stands in contrast to explicit knowledge, which is conscious and can be put into words. People experience tacit knowledge mostly as intuition rather than as a body of facts or instruction sets they are conscious of having and can explain to others. Tacit knowledge is obtained by internal individual processes, such as experience, reflection, internalization, or individual talent. Therefore, it cannot be given in lectures and found in databases, textbooks, manuals, or internal newsletters for diffusion. It has to be internalized in the human body and soul (Haldin-Herrgard, 2000, p. 358).

The third level considered within the model focuses on the individual level's mental models (Kim, 1993) and the organizational level's culture. In addition to mental models, many other terms can be found in the literature, such as frames of reference (Mezirow, 2000, as cited in Becker, 2006), cognitive maps (Huber, 1991), schemas (Barrett et al., 1995), theories of action (Hedberg, 1981), and paradigms (Markoczy, 1994 as cited in Becker, 2006). We follow the definition of Mezirow, who describes mental models as those deep-seated underlying values and belief systems that guide, shape, and dictate the individual's everyday attitudes and behaviors. Culture has long been seen as the shared or commonly held beliefs, assumptions, values, and taken-for-granted norms and behavior that govern organizations (Becker, 2006).

At the organizational level, explicit knowledge is generally captured in a static form. This knowledge, which is easily articulated and documented, can be found in organizational policies, procedures, and processes as well as in documentation such as performance management systems and position descriptions (Becker, 2006). At the organizational level organizational memory in many ways reflects tacit knowledge, although more has been written about organizational memory in the field of information technology than in the general management literature. Many authors propose different definitions and explanations for organizational memory (Argyris & Schon, 1978; Levit & March, 1988; Stein, 1995; Paoli & Principe, 2003), and they all recognize that organizational memory is not just explicit knowledge that is captured, but more importantly also has a tacit dimension.

At the business environment level, companies face the challenge of exchanging knowledge among different agents. Social, cultural, economic, and political contexts in which companies operate and undertake outsourcing activities differ from country to country. The knowledge gained in one business environment context is therefore not easily transferred (Rebernik, 1997; Tominc & Rebernik, 2007) and is very often of limited usefulness.

4. Learning and unlearning explicit and tacit knowledge

An abundance of literature has examined organizational learning (see, e.g., Hedberg, 1981; Cummings, 2003; Argyris, 2004; Esterby-Smith & Lyles, 2005), and many concepts

and theories of learning exist. By definition, an organization learns in only two ways: (a) through the learning of its members or (b) by incorporating new members who have knowledge the organization did not previously have (Simon, 1991, p. 125). We should also pay attention to the individual level, as learning and unlearning take place at both levels. When a company outsources, it has to adapt on two levels: the company and the individual. This adaptation takes place with the help of learning—namely, the acquisition of new knowledge from persons able and prepared to use acquired knowledge in decision making and influencing other organizations (Miller, 1996). Adaptation also takes place at the organizational level because new organizational routines have to be created and performed so that newly established outsourcing ties and deployment of activities can take place. Successful learning results in modified behavior (MacDonald, 1995); in other words, the result of learning is adaptation. Furthermore, in the process of adaptation, the entrepreneur and organization have to unlearn many previously set rules and ways of doing business.

Looking at organizational learning from this perspective and understanding outsourcing as a learning process, one can expect a company to outsource if the entrepreneur is willing and able to learn and is capable of delegating some business tasks to the outsourcing partner. When current knowledge and required new knowledge are closely related, learning is not difficult; however, when a wide gap exists between current knowledge and new knowledge, individuals and organizations have to invest in the learning process. An important part of investment is unlearning obsolete knowledge and values that impede our ability to absorb new information and exploit it.

Any understanding involves both learning new knowledge and discarding obsolete and/or misleading knowledge. Sometimes the unlearning may be as important as the acquisition of new knowledge (Hedberg, 1981). Organizations' conceptual understanding as information-processing systems draws our attention to experiential knowledge that is stored in organizational memory (Andersen et al., 2003). Although experiential knowledge is often equated with tacit knowledge, in reality not all of it is tacit; indeed, some of it can be articulated and shared. The real problem is that much of the experiential knowledge collected in the "pre-outsourcing period" may have become obsolete and should be disposed of because it has become useless and impedes the accumulation of new knowledge as well as the creation of sustainable relationships. The presence of certain knowledge may constrain learning or even encourage ineffective learning (Cummings, 2003). It has been suggested that the proponents of experiential knowledge may be the worst at unlearning, as the accumulation of such experiential knowledge requires considerable investment of time and resources. Knowles and Saxberg (1988) also suggest that those who have invested heavily in their current knowledge may not be willing to unlearn. It would stand to reason that long-held views and knowledge acquired and reinforced over time may be considered more difficult to unlearn than recently acquired knowledge, to which the individual has less of an emotional attachment. This viewpoint contrasts with that which relates to absorptive capacity, which claims that—without an appropriate knowledge base—new knowledge cannot be absorbed. Nonetheless, regardless of whether previously acquired knowledge helps unlearning or hinders it, previously acquired knowledge is recognized as having some influence on unlearning. Tacit knowledge, in particular, raises issues in relation to unlearning due to the fact that it is less easily identified or articulated, meaning it may be less easily challenged as part of the unlearning process (Becker, 2006).

Similarly, as a company must "disorganize" some part of its knowledge store (Holan et al., 2004), disorganization must take place at the individual level as well. For unlearning to take place, intentional unlearning of some parts of existing individual and organizational knowledge is needed. Cohen and Levinthal (1990) coined the term "absorptive capacity" to describe the observation that prior related knowledge enables the recognition of the value of new information, its assimilation, and its application to commercial needs. They emphasized that "the ability to assimilate information is a function of the richness of the pre-existing knowledge structure: learning is cumulative, and learning performance is greatest when the object of learning is related to what is already known" (Cohen & Levinthal, 1990, p. 131). Thus, learning is more difficult when individuals and organizations are faced with an unfamiliar situation.

If sharing tacit knowledge is a demanding task, its unlearning is even more difficult. To study non-expressed knowledge, an adequate methodology has to be developed. To summarize our understanding on managing tacit knowledge, we propose a theoretical framework on how the process that will enable long-term viability of business systems should occur (Rebernik & Širec, 2007):

1. recognition of the tacit dimension on an individual as well as organizational level;
2. observation of the behavior deriving from individuals as well as organizational teams according to possessed tacit knowledge;
3. the making of the behavior explicit by sharing it;
4. learning of the new knowledge and simultaneous unlearning of obsolete and inadequate knowledge.

Although tacit knowledge constitutes a major part of what we know, it is difficult for organizations to fully benefit from this valuable asset because tacit knowledge is inherently elusive; in order to capture, store, and disseminate it, it first has to be made explicit. However, such a process is difficult and often fails for three reasons (Stenmark, 2001, p. 9):

1. we are not necessarily aware of our tacit knowledge;
2. on a personal level, we do not need to make it explicit in order to use it; and
3. we may not want to give up a valuable competitive advantage.

Our understanding of the phenomena derives from the fact that tacit knowledge in its entirety is very difficult to recognize and benefit from. Thus, we propose bringing forward tacit knowledge that can potentially be mobilized and observable through different manifestations of behavior in order to make it explicit as only its explicitness would enable us to share it as well as learn what needs to be learned and unlearn those things that are outdated and obsolete. At this point, it should be stressed that not all dimensions of tacit knowledge foster processes of introducing novelties. Thus, an important knowledge management task would be to separate the tacit knowledge dimension, which both supports and contradicts the introduction of novelties—in our case, newly established outsourcing routines. Having done this, it should be less difficult to incorporate different management efforts into the learning processes of those who support the learning processes and those who are against the unlearning processes for novelties to be introduced (Rebernik & Širec, 2007).

5. Problems with opportunistic behavior

In the outsourcing partnership, both parties have to work together, but they can either cooperate or participate. The distinction between cooperation and participation is described

by Webster's Dictionary (1999), where *cooperate* is described as "to act, work or associate with others especially for mutual benefit" and *participate* is described as "to engage or have a share in something in common with others". Indeed, a difference exists between participative and cooperative relationships; a relationship could be participative but non-cooperative or both participative and cooperative at the same time. Cooperative participation occurs if all participants have a common benefit. In non-cooperative participation, individuals do not cooperate to achieve a mutual benefit, but rather an individual one—even at the loss of other participants (Rebernik & Mulej, 1999).

A successful strategic outsourcing relationship requires both parties (client and the service provider) "to be on the same page" (Karen & Black, 2004). The most significant obstacles that could prevent an efficient (principal-agent) outsourcing arrangement are:

1. misunderstanding of client's objectives, policy and culture;
2. client disagrees with the provider's objectives and policy;
3. communication and monitoring problems; and
4. both sides controlling.

Cooperative participation presumes information exchange. Cooperation is impossible if participants do not share their internal information (Rebernik & Mulej, 1999). According to this process, bounded rationality, information asymmetry, and opportunistic behavior (Williamson, 1983; Barney & Ouchi, 1986) become influential. The concept of bounded rationality indicates that the human mental capabilities are limited and humans cannot rationally define and solve complex problems. For this reason, we have to cooperate because individually we are not capable of solving complex problems on our own. Information asymmetry means that two parties involved in a transaction do not have equal information about things that are important for the transaction. Between the two contracting parties, information asymmetry means that one party has private information, which brings about the so-called information rent.

Information asymmetry can cause pre- and post-contractual opportunistic behavior. Pre-contractual or ex-ante opportunistic behavior is also known as adverse selection (Akerlof, 1970). It shows up when one party in a potential transaction owns private information about something that can cause damage to the other party in the course of contract implementation. Post-contractual or ex-post opportunistic behavior is known as the moral hazard. It shows up when one of the contractual parties, because of its own benefit, does not undertake the agreed activities and the other party in the transaction cannot control the contract implementation in its entirety. If we observe participation in strategic outsourcing as an information sharing or exchange, it can imply the chance of both the moral hazard and adverse selection.

Cooperation needs to include sufficiently shared, common (public) information, making the platform for cooperation able to be initiated in the first place. In the case of cooperative participation, every participant will make available all required private information. Some participants may behave in an opportunistic way and disclose less private information than the others do; they may not own the information, or they may be only fictitious team members. They may also tend to hide their private information because they expect to attain some information rent.

An important learning objective is to prevent the outsourcing partner from possible opportunistic behavior. In business relationships, it is impossible to foresee every relevant possibility or incident that could happen during a relationship. It is reasonable to be prepared for possible opportunistic behavior. This does not mean that participants

in outsourcing have completely different goals, but rather that their interests in some circumstances may be contradictory. Because of information asymmetry and the possible worst-case scenario of the outsourcing contract being a failure, one must admit not only the possible opportunistic behavior of participants, but also any unintentional harmful actions arising from bounded rationality. Therefore, some safeguards to prevent the outsourcing partner from acting opportunistically have to be established in advance (Rebernik & Bradač, 2006).

6. Managing tacit knowledge in strategic outsourcing relationships

The sub-consciousness of tacit knowledge and the difficulty of expressing it are commonly found as the main problems in tacit knowledge diffusion. It is not only that we have difficulty expressing and articulating what we know; we may not even be conscious of what we know or how tacit knowledge connects to our explicit knowledge. In this section we present some of the most influential elements that effective management of tacit knowledge in strategic outsourcing relationship has to overcome.

The most important elements of managing tacit knowledge in strategic outsourcing relationship are:

1. time for internalization of tacit knowledge;
2. powerlessness;
3. emotional commitment and deep personal involvement;
4. procedural justice in decision making;
5. effective communication and common culture development;
6. distance vs. personal contacts; and
7. an appropriate rewards system.

By successfully managing these elements, partners in a strategic outsourcing relationship create the platform for the disclosure of tacit knowledge and can jointly create a common knowledge thesaurus that can be shared. A conceptual framework of managing tacit knowledge in strategic outsourcing relationships to create and share the thesaurus and achieve sustainable outsourcing partnership is provided in Figure 3.

The consumption of time that the internalization of tacit knowledge requires is the first element to be considered in the sharing process. In today's business world, time is a scarce resource, and the internalization of new experiences or knowledge is a process over time (Halding-Herrgard, 2000, p. 361). The dimension of time is attributed to personal tacit knowledge as well as to more organizational forms. In the strategic outsourcing relationship parties face time-consuming constraints regarding the reflection of gained experiences. For both parties, the time allotted for the introduction of such experiences is often insufficient. The rapid rate of change in today's business environment calls for continual learning as well as unlearning. However, few organizations reserve sufficient time for these processes to jointly create a common knowledge.

We should also point out the problem of powerlessness. Knowledge is a basis for power and respect, and people are often hesitant to share knowledge lest their power decreases. Moreover, sharing knowledge requires that time be taken away from other responsibilities that have a higher priority. People are hesitant not only to share what they have, but also to use the knowledge of others. This has been referred to as the "not invented here" syndrome. Perhaps, the most important step toward harnessing the tacit knowledge of individuals and teams is to allow it to flow from the pull of emotional commitment and deep personal

involvement (Glynn, 1996, as cited in Mascitelli, 2000, p. 185). Therefore, the challenge for managers is to inspire, guide, excite, encourage, and shape without overwhelmingly imposing arbitrary structures that might destroy the fragile essence that has to be built and nurtured in strategic outsourcing relationship.
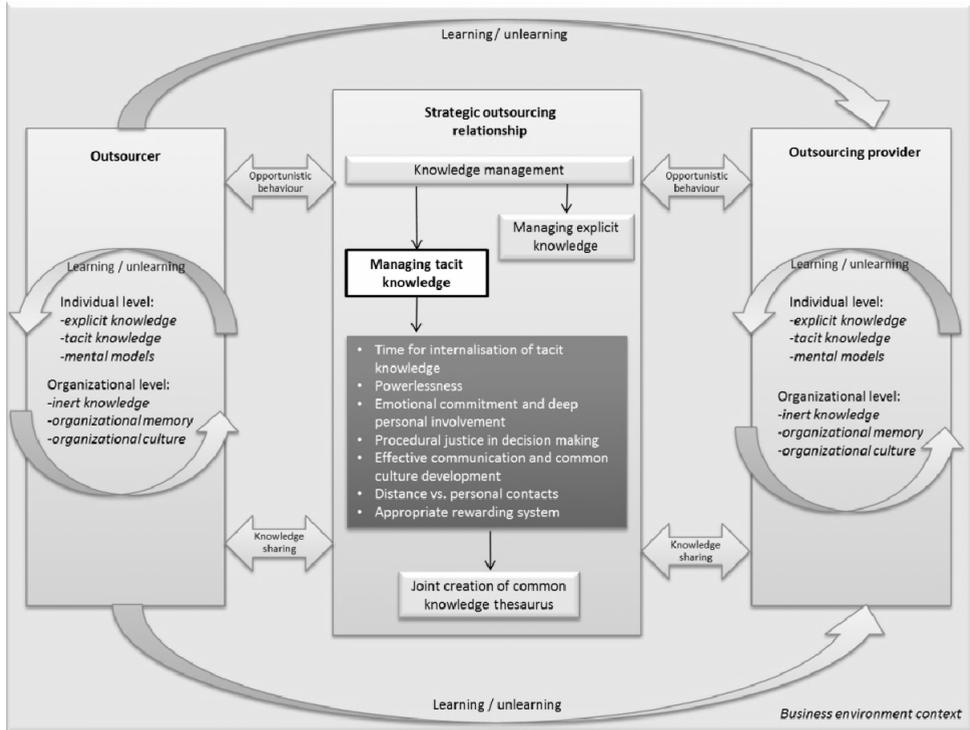

Fig. 3. Conceptual model to manage tacit knowledge in strategic outsourcing relationship

For example, managers can foster the genuine commitment of design team members on three different levels (Mascitelli, 2000, p. 187) by:
1. crafting a "culture of innovation" for the company as a whole;
2. establishing a strong sense of group identity, importance, and purpose among project team members; and
3. creating a generative environment for knowledge sharing, in which learning—as well as unlearning—occurs.

Another element for encouraging knowledge sharing is procedural justice in decision making. Research (Lubit, 2001, p. 175) has shown that, when managers feel strategic decision-making processes are fair, they tend to cooperate voluntarily. Procedural justice has three aspects: engagement, explanation, and clarity. When these three aspects of procedural justice are fulfilled, company employees are most likely to both share their ideas and carry out decisions that are made.

Effective knowledge management includes dealing with the defensive mechanisms that impede communication. Common defensive mechanisms include avoiding the discussion of

important issues, ambiguous messages, and distorted information. Avoiding these phenomena is critical for developing a culture that values openness, tolerates failures, encourages questioning of the way in which things are conducted, and permits workers to challenge their superiors (Lubit, 2001, p. 175). The limited efficacy of most knowledge management efforts has come about because they have overwhelmingly focused on creating electronic means to capture and store information and improve communication. Far more attention needs to be given to the task of convincing people to effectively use the information system (Lubit, 2001, p. 173).

Further constraints in managing tacit knowledge in the strategic outsourcing relationship stem from the distance. Social interaction is often seen as a necessity for the diffusion of tacit knowledge. As such, the globalization, diversification, and virtualization of business that obstruct face-to-face interaction are a threat to tacit knowledge diffusion. Tacit-to-tacit exchanges are greatly enhanced through close personal contact, which is why physical co-location and face-to-face interaction can be important catalysts for innovation (Nonaka & Takeuchi, 1995; Holtshouse, 1998; Mascitelli, 2000, p. 193). Modern ways of doing business that have become completely intertwined with global and outsourcing networks do not improve the conditions for the exchange of tacit knowledge. In the "flat world" (Friedman, 2007) with overnight global deliveries, there is no time for sharing tacit knowledge. This is contrary to the popular notion that information technology can eliminate barriers to knowledge exchanges across oceans and time zones. However, if we accept the concept that tacit knowledge is fundamentally based on bodily experiences and emotional involvement, it is hard to imagine that something so personal can be digitized and downloaded. This is not to say that groupware and intranets are not essential tools for strategic outsourcing; their effectiveness in the sharing of explicit knowledge is undeniable. Rather, we are suggesting that simple steps can be taken to achieve important results in this regard. The frequent use of brief "stand-up meetings" for example, can help ensure continuous interaction among team members and encourage socialization and collaboration in outsourcing relationship.

The authors of the book *Enabling Knowledge Creation* (Von Krogh et al., 2000) go even further in their discussion about effective knowledge creation within an organization. They argue that groups of people working together are more than just teams; they are micro-communities of knowledge. This is an important distinction because "larger communities of knowledge can share certain practices, routines and languages, but for new tacit knowledge to emerge through socialization, the group must be small" (Von Krogh et al., 2000, p. 162). These teams are in a better position not only to create competitive position-enhancing knowledge, but also to communicate and integrate this knowledge back into their own areas and across the organization. One major challenge is that these micro-communities are typically not stable or perpetual. Unfortunately, through the dissolution of such micro-communities, most tacit knowledge gained and developed by them is lost. This knowledge can be retained only through the interactions that exist within the micro-community itself, not through documents or manuals (Allred, 2001, p. 162).

Finally, the implementation of new knowledge and best practices must be measured and rewarded, supported by the culture and recognized by promotion decisions. Without attention to the implementation of knowledge, people are likely to learn information, but then fail to change their behavior in beneficial ways.

In the strategic outsourcing relationship, the nature of the relationship is based on knowledge sharing; participants take a more active role and assume more responsibility and risks in developing the relationship. The successful strategic outsourcing relationship

depends on forging strong links among the management, system, and process functions that lead the organization to cooperate. The collaborative relationship is closer and broader with more teams working together on a wide range of functions; as a result, the contract is typically longer. Managing an effective strategic outsourcing relationship requires commitment from all included parties. The success of the relationship depends on cooperation among participants, who must share their business information and knowledge; otherwise, cooperation is not possible. In this process bounded rationality, information asymmetry and opportunistic behavior manifest. Viewing cooperation as information sharing implies the possibility of both the moral hazard and adverse selection. As we have already underscored, cooperation needs private information and a requisite minimum of shared, common, public information, making the platform establish cooperation. In the case of cooperative participation, every participant will also make his or her private information available. There is always a possibility that some participants may behave in an opportunistic way and put less private information on the table than others, they may not own it, pretend to be team members, or tend to hide their private information because they expect to benefit from it later in the process.

As in strategic outsourcing, the ownership of intangible assets of cooperating companies can be challenging to define; thus, it is important that cooperating parties "contractually specify who will have control over each dimension of each asset in each particular future contingency" (Grossman & Hart, 1986, p. 716). A theory of the firm provides a conceptual background for understanding the strategic outsourcing relationship. A successful relationship requires that the outsourcer and the provider disclose all information to ensure mutual benefits. To make the relationship efficacious, all parties need to exchange all relevant information. A provider is not only a performer of services, but also a partner who is included in the joint development of processes and products in both companies.

7. Conclusions

Over the years traditional outsourcing has evolved into long-term problem-solving strategic outsourcing focused on changes in business processes, productivity improvements, technology, and innovation. Instead of delegating simple routine tasks aimed at cost–effectiveness, today's outsourcing is concentrated on long-term cooperation between companies, developing it into business partnerships. The specialized skills and knowledge of outsourcing partners that would otherwise be very costly and almost impossible to obtain within a single company can be shared and exploited. Two main problems appear in such partnerships: the tacit dimension of knowledge in each company and the possibility that outsourcing partners will behave opportunistically. For a sustainable outsourcing relationship, these issues must be managed effectively.

The most important element of the strategic outsourcing relationship is knowledge management as both parties must share their knowledge to jointly create and exploit a common knowledge thesaurus. As any knowledge base consists of tacit and explicit knowledge and the explicit knowledge is relatively easy to share, special attention must be paid to tacit knowledge. The main prerequisite for sharing tacit knowledge is to make it clear to the partner what can be done by investing enough time for the internalization of tacit knowledge, taking care of powerlessness, appreciating emotional commitment and deepening personal involvement, ensuring procedural justice in decision making, establishing effective communication and common culture development, cultivating personal contacts despite the distances, and establishing an appropriate rewards system.

Participants involved in outsourcing activities not only learn from each other, but they also need to unlearn obsolete knowledge and skills contained in procedures, routines, and ways of doing business from the pre-outsourcing period. Sharing tacit knowledge is a demanding task, but its unlearning is far more difficult. In the era of ever-increasing globalization and transcontinental outsourcing, the management of knowledge—especially its tacit dimension—is becoming one of the key drivers of competitiveness. To overcome the perpetual elusiveness of tacit knowledge, we presented a conceptual model that could help manage the outsourcing relationships and contribute to the creation of a common knowledge thesaurus for outsourcing partners. In any relationship where information asymmetry exists, opportunistic behavior can arise. Policy makers and strategy developers should pay attention to such a possibility; otherwise, no sustainable relationship can be established among outsourcing partners.

Investigating strategic outsourcing in light of managing tacit knowledge raises many issues that future research should examine, especially in the area of opportunistic behavior in the outsourcing relationship and the creation of appropriate policy measures and strategic moves to prevent such behavior. The unlearning is another field in which appropriate models for immediate use in business practice still have to be developed. There is also a lack of empirical research on tacit knowledge, which could prove a number of findings and theoretical constructions that many authors have already developed.

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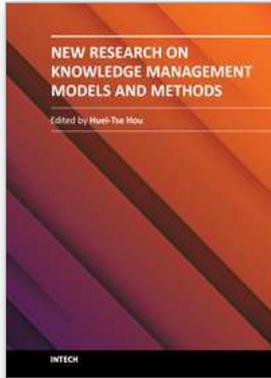
New Research on Knowledge Management Models and Methods
Edited by Prof. Huei Tse Hou

Due to the development of mobile and Web 2.0 technology, knowledge transfer, storage and retrieval have become much more rapid. In recent years, there have been more and more new and interesting findings in the research field of knowledge management. This book aims to introduce readers to the recent research topics, it is titled "New Research on Knowledge Management Models and Methods" and includes 19 chapters. Its focus is on the exploration of methods and models, covering the innovations of all knowledge management models and methods as well as deeper discussion. It is expected that this book provides relevant information about new research trends in comprehensive and novel knowledge management studies, and that it serves as an important resource for researchers, teachers and students, and for the development of practices in the knowledge management field.

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