

Optimizing Your Shared Services Strategy

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By Rob Cooke

Organizations worldwide have been leaping on to the shared services bandwagon since the early 1990's. What is this strategy that has been embraced by major organizations such as Xerox, IBM, Hewlett Packard, Whirlpool, Texas Instrument Europe and Consignia, and what has made it successful?

Large corporations started adopting shared services as a strategy for the delivery of internal staff functions in the early 1990's. Since then the number of organizations who have implemented shared services has grown substantially. It is estimated that over 50 % of the Fortune 500 companies and over 80% of the Fortune 100 companies have now implemented shared services.

The need for shared services arose as the costs of internal services and processes escalated. In the late 1980's and early 1990's the trend in large corporations was to decentralize staff functions to subsidiaries and business units leading to the establishment of duplicate functions in HR, IT and financial services. This inevitably led to increased costs due to duplication, inconsistent processes and differing technology applications. With the implementation of shared services these functions are consolidated into service centres that provide the services back to the subsidiaries or business units.

Although initially thought of as simply the consolidation of backroom transactional processing, true shared services is far more about establishing a service business within a corporation. It is about redefining the value proposition of internal service functions. Long referred to 'low value-added and non-core', through the shared service approach these units can reinvent themselves as high value-added service providers. This does not occur through consolidation alone, but as the result of a combination of factors which include dramatic shifts in the organizations culture.

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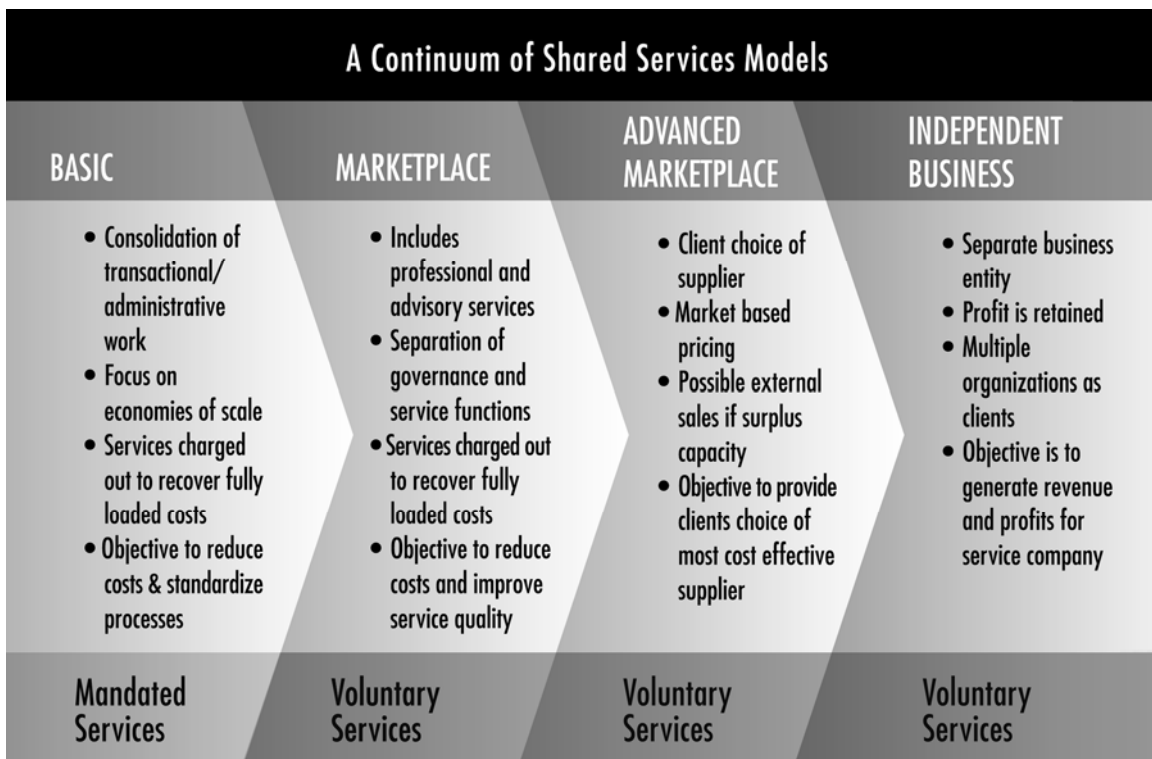
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The range of shared services models

It is important to emphasize that there is no single template for shared services.

Organizations have developed different models to suit their individual goals, structures and the state of their service functions. Table 1 outlines a range of models. The initial and basic concept of shared services revolves around the consolidation of mandated financial processing functions, such as accounts payable, travel and expense payments and payroll, into a shared services centre (SSC). Consolidation achieves cost reductions from economies of scale, standardized processes and the application of common systems.

Table 1



While some organizations never move beyond this basic model, others evolve their shared services to include professional and advisory services operating in a market-based framework. In these marketplace and advanced marketplace models, many of the services are ‘voluntary’ in that clients have choice whether to use them or not. These

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services could include IT applications development, financial analysis and consulting. As companies gain experience in shared services and move on to an advanced marketplace model, clients are given increased choice of supplier: they can use the internal shared services group or go elsewhere, for instance.

While service pricing in the basic and marketplace models are typically based on full cost recovery, in the advanced marketplace model services are priced at market rates. It is in the marketplace and advanced marketplace models where significant and sustainable shifts in organizational culture occur. A great deal of the success of shared services is based on customer satisfaction with the services being provided and the customer focus of the service provider. The establishment of a service-focused culture is a key factor to longevity and success.

Table 1 shows one final stage – a move to setting up an independent service business. The establishment of independent service businesses to delivery shared services has met with mixed results. When shared services is set up as an independent business it is expected to generate revenue from additional clients. This creates two dilemmas. First, the focus of the service-providing organization shifts from internal clients to external ‘real’ revenue generating clients and internal service levels can drop accordingly. Second, setting up a new independent service business defines a new core business for the corporation, which may not fit with its planned strategic direction.

For example, a large multinational oil and gas company established a shared services organization to service business units throughout the world. The shared services organization eventually became an independent entity and not only had to compete for business in its own corporation, but was expected to generate substantial revenue from external clients. Ultimately the executive reconsidered the model, and the shared services organization was reintegrated into the corporation with a focus on internal clients only.

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Shared services and outsourcing

The relationship between shared services and outsourcing requires a clear distinction. Shared services is about consolidating the delivery of non-core services into an internal service business. Outsourcing is the strategy of using external service providers to deliver these services. While complementary there are unique and distinct strategies.

Business process outsourcing (BPO) is becoming one of the fastest growing industries worldwide. Bob Gunn, Vice President Client Relationships for Exult, one of the world leaders in human resources outsourcing, indicates that since 1998 there has been over \$7 billion dollars in human resources outsourcing deals. More and more organizations are outsourcing internal services to external providers such as Accenture, Cap Gemini, Price WaterhouseCoopers and Exult.

For some executives outsourcing services appears to be a more reasonable option than establishing a shared services organization, and for many employees, shared services is often perceived as an interim stop on the road to outsourcing their function. Sometimes there are processes that are immediate candidates for outsourcing and the move to shared services first is not necessary. In most cases, however, the move to shared services is highly recommended before services are outsourced.

To minimize long term costs, organizations are advised to consolidate their services, re-engineer their processes, drive out non-value added costs, move to common best practice processes and common information systems before moving to outsourcing. For some organizations, this may best be achieved through centres that process transactions for multiple sites from one geographic location. Oracle, for example, has established a shared services centre in Dublin that will support operations in over thirty countries.

While it may sometimes be attractive to outsource a service or process because it is not operating efficiently or effectively internally, this typically results in significantly increased revenues for the outsource providers as they charge for 'fixing' the processes

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and it also delays or minimizes cost savings that might accrue to the outsourcing organization.

The decision to outsource should be based on a solid business case that clearly identifies long term costs savings in either operating costs or capital expenditures, or both. Shared services organizations should constantly compare their costs to those of alternative providers, and if their internal costs are not competitive, and cannot be made competitive, then there will be a strong business case to have the service outsourced. In many cases, an eventual decision to outsource may not even be noticed by internal customers, as the shared services organization then changes its role, and becomes instead the internal customer interface for the outsourcer, and retains accountability for ensuring customer satisfaction.

Internal shared services organizations have learned that economies of scale drive costs down and it is only a logical extension that outsourcing to larger processing service providers will drive costs down below what can be achieved inside the organization. Bob Gunn predicts an explosion in human resources process outsourcing and estimates that half of the organizations that have moved to shared services will ultimately outsource their processes.

Inevitably, outsourcing service providers will be knocking on the doors of shared services organizations to convince them that they can delivery services at a lower cost. Our advice is always the same: do the business case and only outsource to world-class providers with best practice processes and a proven track record.

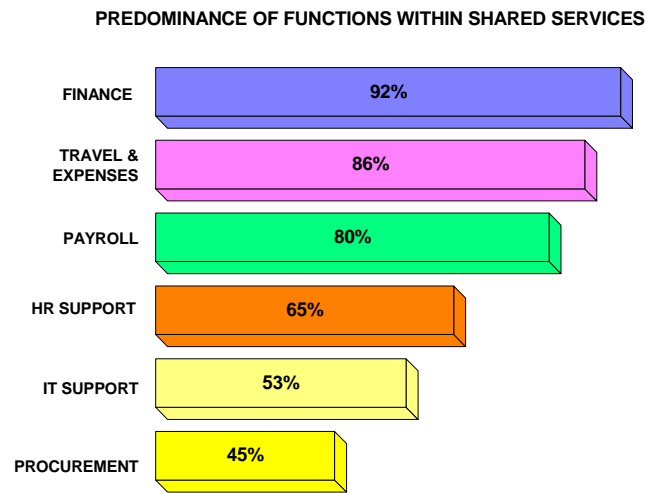
Shared service trends

Although accounts payable, travel and expense and payroll processing still make up the bulk of shared services (see Table 2), as the strategy evolves, more and more internal professional and advisory services are being included (see Table 3).

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Table 2¹



Bywater: Realizing the potential of shared servcies 2001

Table 3

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Scope of Potential Functions for Shared Services in One Company		
	Transactional & Administrative	Professional & Technical
Finance	Accounts payable/receivable Payroll Credit and collections Customer billing Travel & expense Tax filing & reporting General accounting External reporting	Financial analysis Business case Support Capital planning Business analysis
Human Resources	Benefits administration Pension administration Salary administration Employee records Claims Employee inquiries Job Evaluation	Labor relations Organizational development Training and development Compensation & rewards Advisory services Health & safety
Information Technology	Data centre operations Network services Maintenance Help desk Data support	Application development Application architecture Software/hardware installation Strategy & training Telecommunications
Supply or Support	Administrative support (includes: reception, clerical, secretarial Travel arrangements Mail services Microfilming Fleet	Purchasing & warehousing Real estate Material management Logistics & distribution Facilities management Public affairs Communications Graphic services Legal services Security services Communications

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The number of firms adopting this strategy is also expanding on a continual basis, including increasing numbers of public sector and non-profit organizations. For example, in Canada, a number of government departments and crown corporations have used the approach as a strategy for reducing costs and leaving more funds available for public program delivery.

Table 4 identifies a sample of multinational corporations that have implemented shared services and what services have been included.

Table 4

Company	Finance	HR	Procurement	IT	Real Estate	Facilities	Travel	Legal
Aetna	X	X		X	X	X	X	
Alco	X	X	X	X				
Allied Signal	X	X		X	X	X	X	
Amoco	X	X	X	X		X	X	X
Boeing	X		X			X	X	
Citigroup	X	X	X	X	X			
Dow	X	X						
General Electric	X	X		X			X	
General Motors	X	X			X	X	X	
Georgia Pacific	X	X						
IBM	X	X						
Kraft Foods	X	X						
Lockheed Martin	X	X						
Lucent Tech	X	X						
Mobil	X	X	X	X			X	X
Monsanto	X	X		X		X	X	X
Pfizer	X			X				
Rhone Poulenc NA	X	X		X	X	X	X	X
Sears	X	X						
Shell	X	X	X	X	X	X	X	
Texas Instrument Europe	X	X	X	X		X		X

Source: Gunn Partners²

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What are the critical success factors?

From our experience and research there are a number of key elements that need to be in place to ensure that shared services is living up to its' expectations and providing the results required.

- ***Goals must be clearly defined***

The most commonly cited reasons for implementing shared services is reduced general and administrative costs and early advocates claimed dramatic savings of up to 30% to 40%. In a recent Akris/Andersen survey³, however, respondents rated improvements in service quality as equal to cost reduction in the top reasons for setting up shared services. Additional reasons cited in the survey were standardization of business processes and optimization of working capital.

Additional reasons cited by organizations include enabling business units to focus their efforts on core business activities and letting shared services deal with service related non-core activities and increasing the ease of accommodating today's rapid pace of restructuring through mergers and acquisitions

When establishing cost reduction goals it is important to recognize that the returns will be impacted by organizational size, the extent of consolidation, standardization, reengineering and the application of technology. Dramatic decreases in cost will be function of all of these factors. Some major consultancies assert⁴ that shared services is only worthwhile in organizations with turnovers in excess of \$500 million. I believe that shared services can be cost effective in smaller organizations, but realistic financial goals need to be established. The leverage from economies of scale and the impact of best practice processes and technological applications is directly proportional to the size of the enterprise. In smaller organizations the leverage is not as great and the resulting savings will be a smaller percentage of total service costs.

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- ***Shared services need to move beyond centralization***

When an organization first implements a shared services strategy it can look like traditional centralization. Services that had been managed at a local level, will now managed at corporate level, for instance. In the past this has meant reductions in service levels, leading to resentment on the part of line managers. Shared services must quickly move beyond the simple consolidation of resources and reporting relationships or it will ultimately fail. Service levels to clients must be improved immediately, and client service needs must be recognized and met. This is difficult, since during the transition period to shared services, standards typically go down.

Table 5 illustrates some of the fundamental differences between shared services and traditional centralization.

Table 5

SHARED SERVICES:	CENTRALIZED FUNCTIONS:
<ul style="list-style-type: none">- <i>Goal is to provide products & services at a cost, quality and timeliness that meets needs of internal clients and users</i>- <i>Enables internal clients to select service levels based on what they want and are willing to pay for as defined in service level agreement</i>- <i>Shared service groups are not held accountable by stakeholders for ensuring compliance to policies & standards.</i>- <i>Fully loaded costs are either charged to clients or are visible and there is joint accountability to make best value decisions</i>- <i>Accountable for ensuring rates are competitive with alternative service providers and make effective decisions re outsourcing</i>- <i>Emphasis on development of a customer service focused culture</i>	<ul style="list-style-type: none">- <i>Goal is to provide products and services at a reasonable cost, quality and timeliness that meets the organization's needs</i>- <i>Offer a universal set of products and services at a service level deemed reasonable and cost effective</i>- <i>Centralized groups are expected to enforce compliance to policies and standards on behalf of stakeholders</i>- <i>May operate on a cost recovery basis, allocating costs across business units based on established formula or are financed as overhead</i>- <i>Role in ensuring service costs are competitive with external service providers</i>

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- *The governance function must be differentiated from service delivery*

Corporate staff functions have always been faced with two sets of responsibilities. Firstly, the development of functional policies and standards and secondly, ensuring compliance with these while delivering services to clients. This duality of roles creates conflict within the function, and frustrates line management clients who accuse the managers of being ‘corporate cops’ and anything but service-oriented suppliers. The human resources function is most often criticized in this area. They both establish HR policies, and control organizational behaviour through the delivery of their services.

In the shared services model, the staff functions must clearly differentiate the role they carry out on behalf of the executive and board from the delivery of services to clients. Assume, for example, that all services were outsourced. The corporation would set the policies and rules and appoint someone internally to be accountable for the third party’s compliance. The external service provider would then deliver services to the organization that are within the rules defined by their client. This is how shared services groups need to operate. Figure 1 outlines the relationship between service delivery and governance.

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Figure 1

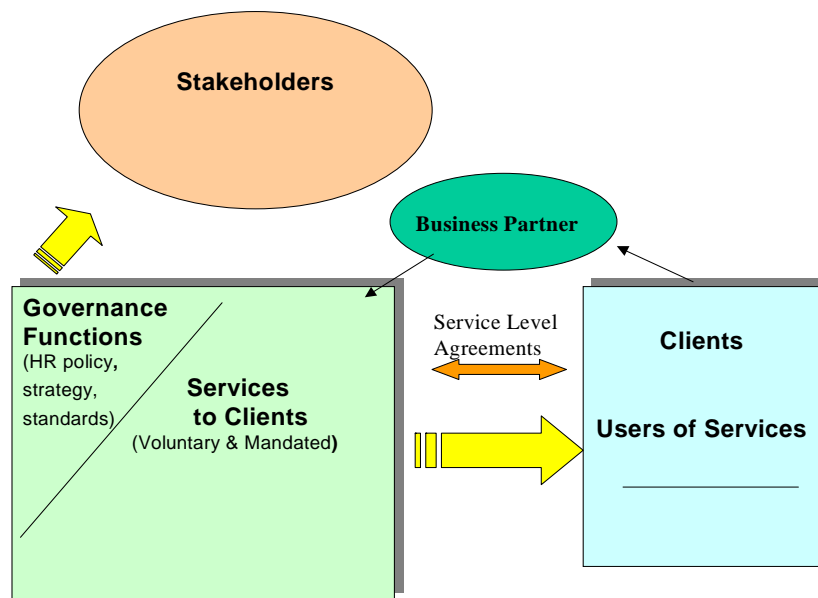


Figure 1 shows how services should be provided to clients as defined in a service level agreement (SLA). Service level agreements define the service relationship between supplier and customer, what services will be delivered, under what conditions and for what price. A surprising number of shared services organizations operate with no formal agreements with internal customers, even though clearly defined and simple service level agreements are considered a key success factor for shared services.

Service level agreements help to minimize misunderstandings and ensure a solid footing for an ongoing solid business/client relationship. The SLA is negotiated between the service providers and the clients with the assistance of a business partner. Business partners are intimate with the strategic and operational directions and needs of the client organization and translate these into service delivery requirements.

Governance functions, which include policy development and compliance monitoring, are carried out on behalf of the executive or stakeholder group. In many cases service

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level agreements define that the services to be provided to service users must be consistent with governance direction or within the established 'rules' of the organization.

- ***Shared services must be led from the top***

Shared services is not a bottom-up strategy. It must be driven from the top of the organization, and requires executives to embrace enterprise-wide thinking as distinct from a focus on business unit or functional focus. Many business unit leaders have established strong functional groups within their organizations to provide high quality responsive services that are highly valued by the business unit. The consolidation of services requires these leaders to relinquish their autonomy and resources for the greater good of the whole organizational entity.

Inevitably, this usually generates a great deal of resistance at first, as the business units fear a reduction in services and service quality due to the loss of control and owned resources. It is extremely important that the leaders of the business units understand and accept the move to shared services and are visible and vocal in their support. In case studies of less than successful implementations, one of the key variables was those business unit executives were never on board with the strategy.

Strong leadership is essential in addressing and overcoming employee resistance. There will be many crises along the road to implementation and strong committed leadership is required to maintain the focus and the pursuit of success.

- ***Recovering fully loaded costs is fundamental to success***

There is no limit to the demand for free services. This applies to the services of internal service functions just as much as any other service relationship. To develop a positive business relationship between shared services and its customers, service costs must be clearly understood. Table 6 outlines the pros and cons of alternative billing strategies.

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Table 6

Billing Strategy	Pros (+) and Cons (-)
No Billing for Services	<ul style="list-style-type: none"> + Minimal negotiation required + Minimal customer pressure to reduce costs or to use outsourced services - No limit on demand for services - No customer consequence for unrealistic expectations since no visible impact on costs
Allocation of Service Costs	<ul style="list-style-type: none"> + Easy to administer + Controlled by service provider - Customers affected by service inefficiencies but no visibility of impact - No relationship between services used and cost to customer - Similar issues to no billing
Fixed Price Based on Past Usage	<ul style="list-style-type: none"> + Easy to administer + Minimal negotiation required - Minimal relationship between current services used and costs to customer - Limited incentive for service provider to reduce costs - Changing or unpredictable volumes can create problems for service provider
Direct Charging Based on Usage	<ul style="list-style-type: none"> + Establishes direct relationship between services used and costs to customer + Customers shares accountability for service costs + Increased pressure on service provider to reduce costs and ensure they are in line with alternative providers - Pricing and billing can be complex and expensive to administer - More complex relationship between supplier and customer

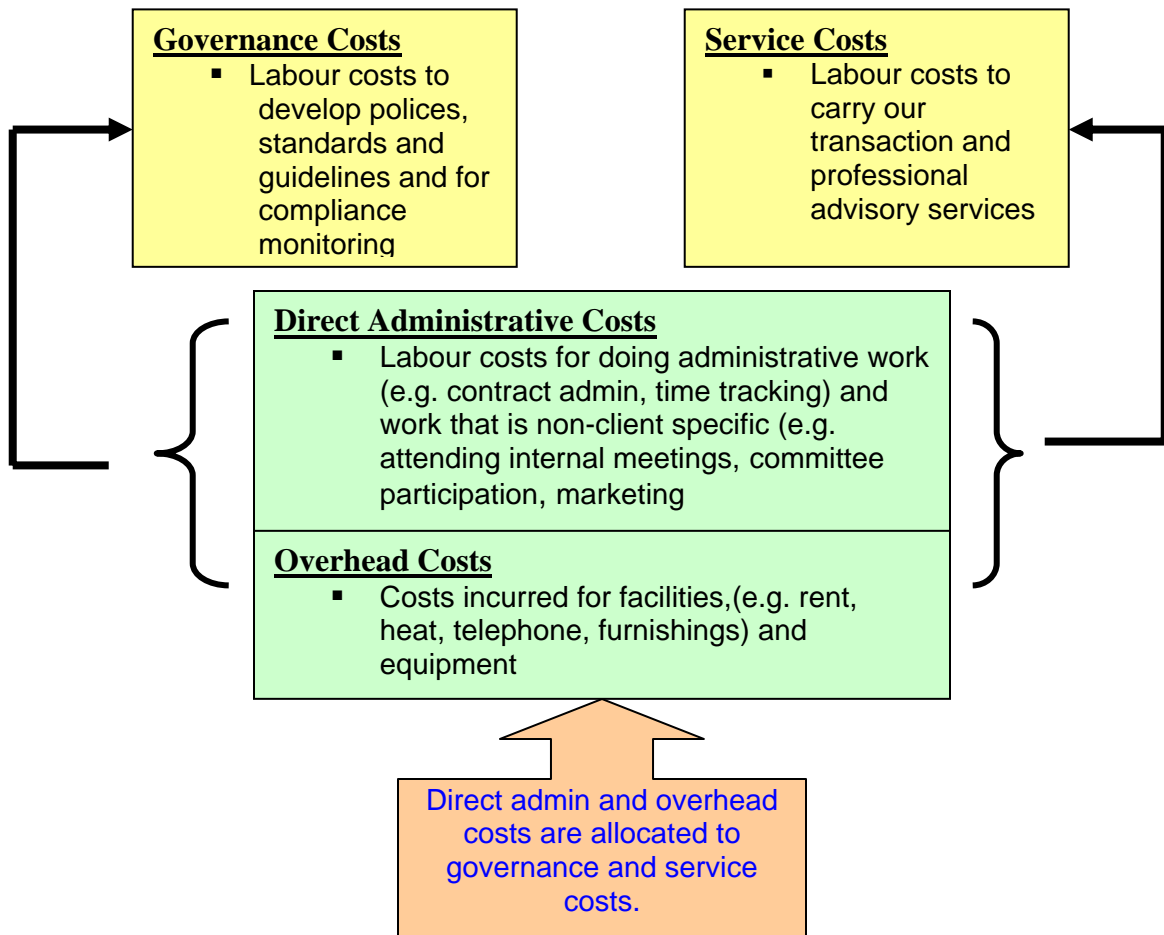
Pricing services and charging customers for services provided is a fundamental tool for establishing business-oriented shared services functions. There must be a direct relationship between services consumed and costs recovered. Whilst direct charging is the preferred strategy for activating this relationship, there are many organizations who are opposed to the internal transfer of funds and internal charging processes. Even without the actual transfer of funds through invoicing there must be a clear visible way to have customers jointly accountable for the cost of services they consume. This can occur through joint budgeting and joint budget approval and high visibility of service costs.

The calculation of service costs is the basis for any direct or indirect charging or joint budgeting of service costs. Figure 2 identifies the specific components for calculating service costs.

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Figure 2



Summary

More and more organizations are studying the feasibility of a shared services model within their organizations. It is important to recognize the scope of alternative approaches and to factor in all the variables that will contribute to success. A full scale feasibility study is highly recommended not only as a vehicle for quantifying costs and benefits but as a way of involving internal service groups, customers and stakeholders is determining if some form of shared services is right for them.

References

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¹ Bywater: Realising the potential of shared services, 2001

² Gunn Partners, Presentation to Shared Services Conference, 2001

³ Shared Services Centres Extend Their Reach, Andersen/Akris.com report 2001

⁴ PWC's Martin Hammer, a partner in their New York office, quoted in an article by Elizabeth Ferrarini, *Computerworld*, November 27th 2000.

⁵ Outsourcing Information Technology Systems and Services, Robert Klepper & Wendell Jones, Prentice Hall, The Business Forum Online, 2001