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Creating value from uncertainty

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Discussion paper: **Shared services risks**

Drawing on Broadleaf's experience with many shared services projects in the public and private sector, this paper summarises recurring sources of uncertainty and issues concerning risk management in such projects.

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1 Background

Shared services arrangements seek to achieve economies of scale by having one service provider meet the needs of several organisational units. Centralised provision of IT systems to government departments, instead of each having its own IT function, is a common example. The principle can also apply to entire business processes, such as payroll, procurement, facilities management, vehicle maintenance and other services.

Shared services offer many apparent benefits, yet attempts to implement them often strike serious difficulties. In some cases, projects are cancelled before implementation is complete.

While it is a common belief that shared services lead to more efficient business outcomes, assessing the benefits that shared services appear to offer and the costs of delivering them can be challenging. There are many uncertainties surrounding what a shared service will deliver and how well it will operate. Even greater challenges can arise in understanding how shared services will be established and how stakeholders will make the transition from existing operations.

Straightforward risk management, informed by an understanding of the common pitfalls associated with shared services in the past, can improve the chances of success in future shared services implementations. This white paper sets out some of the factors arising in design, procurement and transition to operation that can affect any shared services project and the realisation of the benefits it should deliver.

2 Context

Although the basic concept of shared services is simple, it provides scope for a lot of complexity. There are generally two organisational levels involved on the client side of a shared service provision:

- The business units, departments, agencies or other operations that will make use of the shared services (the client or customer units); and
- The organisation, or part of the organisation, that acquires, manages, monitors and acts as the unified 'purchaser' of the shared service on behalf of the client units.

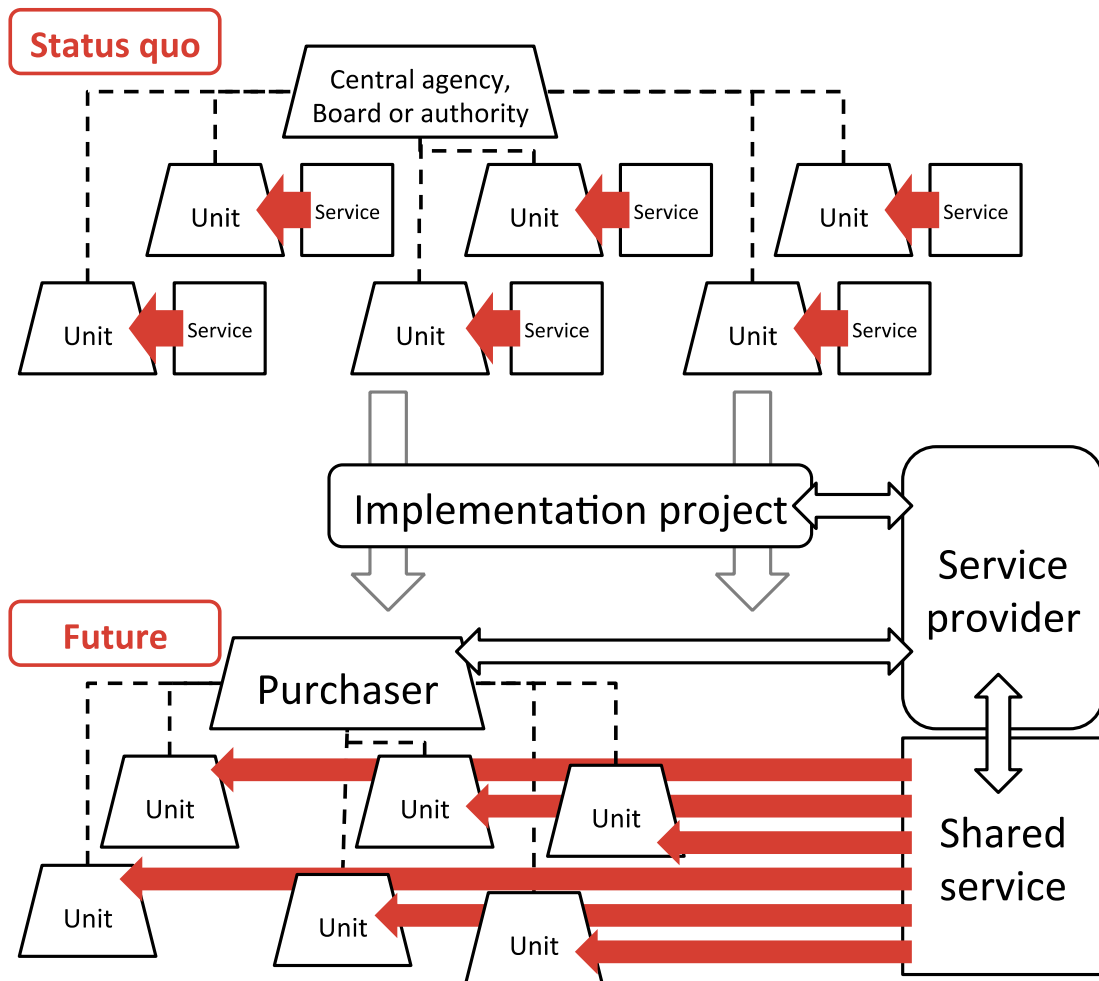
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Examples of recent shared services implementations, not all of which have been successful, include:

- Multinational businesses' financial, purchasing and payment systems;
- Higher education institutions' student record management and, separately, financial systems;
- Driver's licence and identity document issuing and management;
- Government departments' IT support and, separately IT security systems;
- ICT services for schools; and
- Public sector asset management.

Each of these can be described in terms of the elements shown in Figure 1. This shows several operating units currently obtaining services independently of one another moving to a shared service from a single provider. The change is implemented by means of a project.

Figure 1: Generic model



Shared services risks

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3 The Starting Point

In practice, a great deal of emphasis is placed on where a shared service implementation will end and on the benefits it is hoped to deliver, but many of the most important challenges have their roots in the status quo, the starting point for the project. Three themes capture many of these challenges:

- Diversity among the operating units;
- Motivations of their management and personnel; and
- Information about the present situation, processes and operations.

3.1 Diversity

Differences between operating units can have a significant impact on the implementation of shared services. The challenge they represent is often overlooked or underestimated. This allows potentially catastrophic tensions to build up within a project and disrupt its implementation.

While they will share some characteristics, operating units do not all enter into a shared service arrangement on the same terms. No matter how mundane the service might be, there are invariably differences between operating units.

Some of the most common include:

- The scale and complexity of each unit's operations;
- The political influence of each unit within the larger entity;
- Procedural details of existing service operations;
- Sensitivity to service level measures such as availability and quality of service;
- The priorities governing trade-offs when time and resources are constrained;
- How strongly they are bound into existing service delivery contracts, how successful these contracts have been, and how long these contracts have yet to run;
- The technology they currently use to deliver services;
- The extent to which their activities are integrated with or rely upon processes that are not within the shared services' scope; and,
- Staff and management skill levels and the maturity of management processes.

These and other differences are generally clear for all to see at the outset although they might not be addressed directly. It might be assumed that they

are relatively unimportant because all the units are expected to adopt a single service delivery model. Some important differences might have to be preserved though. Among these, special security and legal or regulatory compliance obligations are common.

What is perceived as one implementation project has to deal with separate issues for each unit. Ideally, the project will address this diversity and provide a program management function to bind it into a coherent whole. If the project adopts a single central focus, it may fail to recognise crucial distinctions between the separate units that can undermine the entire project.

3.2 Motivations

There are fundamental conflicts built into shared services implementations: between the personal interests of the individuals involved and the interests of the overall project, as well as between the operating units as they compete with one another to get the most out of the new arrangements.

By their very nature, shared services initiatives are almost always driven centrally but they rely on the commitment of personnel in the operating units for their success. In addition, shared services projects often have extended timescales, so changes in staff, management roles and organisational priorities are to be expected as shared services are implemented. Three common challenges to the effective engagement of personnel are resistance to change of any kind, a desire to protect independence and influence, and competition between units to each gain the most from the shared services arrangements.

Change can be disturbing. The environments with most scope to produce improvements will tend to be those that have remained unchanged for the longest time. This is a straightforward change management challenge made more complicated by its interaction with the issues surrounding information, discussed in the next section, as well as with a project's ability to engage personnel in the transition. Operations that were last updated a long time ago are often those with the poorest documentation of their current processes and staffed by the personnel least interested in change; perversely, these may be the units in greatest need of improvement.

Local managers of existing services will reasonably see a move to shared services as a loss of influence. They might not wish to be seen to be obstructing the change but they will often resist supporting it. Simply getting all the stakeholder representatives to attend project meetings at the same time can be

a challenge and it may prove impossible to reach agreement among them on all aspects of the work.

Where agreement cannot be found or decisions are being delayed, there may be a natural central authority, such as the board of a company or the head of a government department, that can, in principle, step in and mandate a way forward. Such intervention might strengthen passive resistance to the project.

Where there is no central authority providing clear leadership, or the units enjoy some level of autonomy, as with a group of higher education institutions, overcoming local management resistance can be even more difficult. Governance arrangements that appear sound but lack efficacy can actually prolong project disruptions by masking the absence of consensus and hiding the need for stronger measures to break a deadlock.

Even if personnel within the units recognise that change is inevitable, differences between their separate needs may lead to competition. Each unit may seek to have the new arrangements match their business needs as closely as possible, often at the expense of meeting the needs of other units. If they are in competition with one another in their normal activity, as arises with some tertiary education institutions, competition within the project is likely to be significant. Conflict and political manoeuvring can only exacerbate the other challenges standing in the way of implementing the shared service.

3.3 Information

Information about existing operations is the foundation on which the design of a new system is based. It is an essential input to planning the development of and transition to the new system and an important part of the baseline against which success will be measured. Significant information about the existing services may be undocumented, documented but out of date or misleading, held in the heads of a small number of people or even unknown to anyone remaining at work.

To ensure that a new shared service provides an adequate replacement for existing operations, it is necessary to understand how those operations work. To optimise the transition to new ways of working, it is necessary to know what assets and infrastructure are available currently, what can be re-used, where parallel working may be required during transition and how the old systems can be phased out.

Many processes rely on undocumented knowledge held by those who operate them. Formally-documented processes are often augmented by undocumented practices made on a pragmatic basis to deal with changes and smooth out inefficiencies. Establishing a baseline in such circumstances is very difficult, even if the people involved are all motivated to help.

Documentation of some processes and infrastructure will often be incomplete or even completely absent. Systems and even physical infrastructure may have developed over time, being extended and reconfigured without the changes being documented. For instance, ICT systems might include a mix of new hardware and software, old software running on new machines using emulators of old operating systems and old software running on old unsupported hardware. The older elements of the system might rely heavily on a small number of personnel who have operated it for many years.

4 The Business Case

The goals of a shared services project usually include cost reduction, flexibility, operational scalability, and process standardisation among the major drivers. While these may be fairly well understood, at least at a high level, some aspects may have to be worked out and negotiated prior to implementation. An important key performance indicator is generally some form of net present cost, net present value or internal rate of return measure, often purely based on costs and savings but sometimes including revenue.

Shared services business cases often face particular challenges in relation to:

- Governance and the integrity of decision making;
- Knowledge of existing systems and processes;
- Understanding management costs;
- Attribution of benefits;
- Non-financial objectives; and,
- Preoccupation with the end state to the exclusion of the implementation.

4.1 Governance and integrity of decision making

The decision to embark on a shared services project might never be tested properly.

It is remarkable that some shared services projects proceed without formal financial justification, let alone a proper business case. Not only does this lay the exercise open to having a negative financial effect, it can set a poor example for the way the entire exercise is managed. Even if a shared services project could have been beneficial, setting out with weak controls is likely to result in higher costs and lower benefits than might have been achieved. Risks that might affect the stakeholders can be built into an organisation's management systems through poor decision making. This might drag it down for years to come.

4.2 Knowledge of existing systems and processes

In addition to problems with the availability of information, analysis of existing systems and processes may discover gaps that the new system will need to fill and places where the boundary between the systems to be replaced and other systems are unclear. These present both technical challenges in preparing a business case and potentially time-consuming policy issues.

This matter has been discussed earlier under the heading of information about the status quo, but some details are especially important when establishing a business case.

Understanding infrastructure and processes used to deliver existing services can be difficult, especially where documentation is sparse, out of date or absent. Additional challenges can arise when the services to be replaced coexist with services that are to be retained. It may be that some services are under separate control or are too sensitive to be incorporated into a shared service, yet they are carried out by the same people whose work is to be transferred to the new arrangement or they share the same infrastructure.

Identifying the boundaries, understanding the implications of proposed changes for the processes that are not to be transferred and accounting for the impact

that the changes will have on them can all be difficult technically. They can also raise complex policy issues about cost allocation and responsibility for continuity of service that will affect the cost-benefit analysis of the business case and possibly draw additional stakeholders into the project.

Analysing existing systems and processes can uncover gaps that will need to be covered by the shared services. It is not uncommon to find irregularities in the management of software licences, record keeping and data management that have fallen into poor practices, dependence on inputs and sources of support that have not been formally recognised to date, and other areas where a straight replacement of the existing conditions is either not possible or not desirable.

Substantial effort can be required to expose all these inputs and some, such as unresolved boundaries between services, might raise significant policy issues. Policy issues may have to be escalated through individual units' management structures as well as the central agency to find a resolution, which can be time consuming at the very least.

Analysis of existing systems and processes may also identify opportunities for business improvement in individual units, particularly where existing systems limitations may have restricted units from making their processes more effective or efficient. Such opportunities for business improvement should be included in the business case.

4.3 Understanding management costs

The complexity and cost of managing a shared services contract often exceeds the expectations and experience of current contract management personnel.

An organisation that has managed external service providers often expects economies of scale and reduced costs when it transitions to managing a single shared services provider. These expectations are not always met.

A single large contract may have a simple commercial interface, one client and one provider, but the service delivery interfaces and relationships are bound to be more complex. There is a constant need to ensure that individual operating units do not inadvertently commit the client to contract changes in their day to day working with the service provider without this being considered by the contract management function. The special requirements of each individual

operating unit, centrally managed standards, and the interpretation of service levels across diverse operations are just a few of the fresh challenges that the contract management function must manage.

Accurately reflecting the complexity of shared services in a contract and managing that complexity across multiple stakeholders is a major challenge. Contract management personnel experienced in simpler or smaller contracts may not have the skills or capacity to effectively manage a large shared services contract. On their side, the service provider's personnel are generally established to suit the scale of the job and have a greater amount of relevant experience with which to ensure that their interests are protected. In these circumstances, it is not surprising if variations and waivers are raised by the service provider and add unplanned costs once the system is in place.

4.4 Attribution of benefits

Some benefits attributed to a shared services implementation might be gained by simply cleaning up existing processes and systems.

At the outset, existing processes, data, systems and infrastructure usually contain gaps, weaknesses and inconsistencies that need to be resolved before a new service is defined. The benefits of the proposed new system will be assessed on the basis of a clean implementation that fills any pre-existing gaps, anomalies and business improvement opportunities. There may be circumstances in which simply streamlining existing systems and processes would yield significant benefits in their own right.

We know of at least one case where adjusting existing services to allow greater flexibility and standardisation was recognised as highly worthwhile, but the required changes could not be made easily. A shared services implementation was used to provide the impetus.

4.5 Non-financial objectives

Non-financial goals can be a major driver for shared services. The business case must integrate these with the financial analysis.

A shared services project might have objectives outside the scope of the services that it is to deliver and the financial impact it will have. These could include improving an organisation's flexibility by allowing services to be scaled

up and down in response to changing demand, or making it easier to move between geographical locations. Restructuring staff employment arrangements and skill sets and bringing about cultural change and business improvements in response to external conditions may also be important.

Some of the effects of a move to shared services might not be readily included in a strict financial assessment. It may be necessary to include recognition of non-financial factors as well. Care is required to integrate non-financial measures with simple cost-benefit and NPV analyses to create a meaningful assessment of benefits.

4.6 Preoccupation with the end state

Over-emphasis on the possible improvement that a shared services project might offer can take the focus away from understanding the current situation and effective management of the implementation.

Focusing on the outcome of a shared services project is natural. The benefits are the motivation for the effort required to make it happen. However, problems that have surfaced with several shared services projects suggest that in many cases insufficient attention is paid to understanding the current situation or the challenges that arise during implementation.

Transitional arrangements during the move from old to new systems are routinely underestimated. In some cases, significant, sustained peak loads arise from the need to maintain both systems in parallel for extended periods, placing a burden on staff, systems and budgets.

Analysis of the human and systems resources employed by the existing service is crucial to understanding the baseline against which proposed changes will be measured and the scale of the effort required to implement them. Superficial impressions and assumptions about the integrity of existing documentation and procedures, and the ease of transition to shared services, often prove incorrect.

5 Maximising the Chances of Success

All the challenges outlined here, and more, are threats to the success of a shared services project. Projects have even been cancelled or deferred indefinitely where these challenges have not been recognised or addressed.

Shared services projects often face more human and behavioural risks than other projects. They usually affect a large number of people directly on both a professional and a personal level. This is compounded by the many organisational boundaries the projects span. They need to work between separate units, the central authority, the project team and the new service provider. This brings a degree of complexity that many projects do not traditionally face. Unfortunately, the risks associated with human and organisational factors frequently go unidentified, are glossed over, or are given little more than superficial consideration.

It is our experience that sound risk management is essential in the early stages of thinking about and preparing for a shared services project if major pitfalls are to be avoided. Many of the generic challenges of shared services are well known, and effective risk management should be straightforward even if it might not always be simple. Structural challenges such as the involvement of multiple stakeholders and systems crossing several organisational boundaries can be accommodated within a risk assessment process, and successful treatments can be implemented if the challenges are addressed early and pursued diligently.

There are several extensions to simple risk assessments that assist managers who must make decisions about shared services projects.

With care, a sound risk management framework can be designed to ensure that the initial approach to shared services is realistic, see Table 1 on the following page. It can ensure that plans include measures to control risks where it is beneficial to do so and that controls are sustained and effective through implementation.

Table 1: Risk analysis to support shared services projects

Topic	Form of analysis	Decisions supported
Major risks in a shared services arrangement, from initiation and transition through to the end of the contract life	Qualitative	Treatment actions in each stage of the project, including establishment of controls and monitoring regimes across all aspects of the project Requirements to be included in request for tender documents
Uncertainties in the benefits and costs of a shared services arrangement, from inception through the life of a contract	Quantitative	Whether or not to embark on a shared services project and in what form
Major risks that should be addressed by potential shared services providers	Qualitative	Evaluating tenders Selecting a preferred provider Identifying necessary controls and monitoring processes Negotiating specific contractual terms and conditions
Scenarios in which the organisation may suffer loss if a shared services provider fails to perform as required	Quantitative	Guidance on the associated limits of liability that might be included in a shared service contract

6 Contacts

If you require more information on risk management as it is applied to shared services and the associated uncertainties, please contact one of the members of Broadleaf shown below.

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