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Accelerating Shared Services Acceptance

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Learning objectives:

- An understanding of the available governance options for IT shared services and what each entails.
- Selecting the option right for your organization.
- Maximizing the net benefit of your shared services implementation.

Shared Services: A Growing Trend

- Shared services allow multiple business units to use a single IT service capability. They aim to maximize utilization of resources, increase efficiency, and reduce costs. Shared services also create opportunities for quality improvements.
- The ongoing need to control costs while increasing quality drives interest in shared services.
- However, ineffective governance can undermine the benefits that organizations seek from shared services.

Shared Services: Governance

- Implementations deliver substantial cost and quality benefits
- **One third** of shared services implementations **increase IT expenditures** and 11% worsen service quality.
- Ineffective governance is a major role for failure. Common problems:
  - failure to encourage participation in the implementation,
  - lack of accountability for implementation success,
  - no reconciliation of interests and business practices of the various participants.

Three Governance Models

- The appropriate choice of approach is a key contributor to success.
  - *Entrepreneurial*: ideal for small organizations.
  - *Mandated*: ideal for larger organizations with a few business units involved in the shared services implementation.
  - *Market-based*: ideal for larger organizations with many business units involved in the implementation.

Shared services increase efficiency and improve service quality

Shared services continue to garner interest as organizations try to control ever-increasing IT costs without sacrificing quality.

Why:

Shared services reduce duplication of function
For example, a state government may have two IT functions currently housed in separate state agencies. The two IT departments perform similar functions and use similar human resources and technology. Combining the IT departments in a separate entity and requiring the agencies to share the IT service allows for cost reduction.

Why:

Shared services allow multiple business units (BUs) to share a single, high-quality service provider
For example, one BU may have a more advanced data center operation than the other. It makes sense for both business units to share the more advanced service.

Typical areas for shared services deployment
- Data center
- Network infrastructure
- Service desk
- Server hosting

Caution!
Do not implement shared services when the nature of the services differs greatly between BUs. For instance, a language difference would cause a shared service desk to fail.

Ineffective governance will undermine the benefits of shared services

The participant resistance and service underperformance that IT managers experience is often the result of poorly planned and executed governance.

Ineffective governance leads to:

- **Resistance.**
  - With poorly defined incentives, business units (BUs) resist sharing their capabilities due to fear of unfair treatment.
  - Failure to align BU interests with organizational strategy results in limited participation.
  - Performance failures due to unspecified benefits cause BUs to lose faith in the implementation.
- **Service underperformance.**
  - Failure to align individual incentives with the broader organization.
  - Lack of accountability causes performance disappointments.

Info-Tech research shows that 33% of shared services implementations increased IT expenditures and 11% worsened service quality, in part due to governance failures.

"I would absolutely agree that [stakeholder resistance] at the senior level is the number one issue."

- Al Povoledo, Partner, Canadian Project Partners

Effective governance overcomes resistance by defining clear benefits, service levels, and penalties

Effective governance creates clear accountability and incentivizes participants to share benefits and define expectations.

Categories of resistance	Reason for resistance	Resolved by effective governance because:
Differential benefits	• Shared services provides a range of benefits to business units depending on the quality of their existing service. • BUs who have invested heavily in IT resist sharing with departments that have weaker IT departments.	• Ensures that all participants receive either cost or quality benefits.
Loss of control	• Some BUs fear that shared IT will threaten their ability to obtain the services they want when they want them. • They may believe that the needs of other departments will take priority. • Or they may fear that the chargeback on services will exceed their willingness to pay.	• Clearly defines service levels to ensure stability of service quality.
Lack of trust	• BUs lack trust in other BUs or the organization's commitment to living up to its promises.	• Defines specific service requirements and penalties for failure to achieve.

Effective governance manages expectations, resource demands, and customer needs to prevent failure

Clear accountability reduces shared services failures.

Categories of failure	Reason for underperformance	Resolved by effective governance because:
Excessive speed to implement	• Strong pressure exists for management to implement shared services quickly. • Software development and employee training cannot always keep up with the implementation speed.	• Ensures expectations are managed throughout the process.
Insufficient capacity	• Processes do not scale with the size of the implementation, making it impossible to serve all participants.	• Ties resource allocation to the demands placed on the shared service.
Varying customer needs	• Business units demand very different services, making it hard to accommodate the needs of all. • The end result makes no one happy or is delivered late due to scope creep.	• Methodically prioritizes customer needs according to the importance to the overall organization.

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An early failure of shared services can dramatically affect your ability to gain support for later implementations. Implement effective governance early on to increase your likelihood of success.

To achieve success, ensure your governance plan defines key elements of shared services governance

Elements of governance		Shared services governance defines…	So that it can…
Management and participation		• The reporting structure for the shared service. Within which BU will the service reside and who will manage it? Who holds accountability for monitoring the ongoing performance of the service? • The criteria for participation in the shared service. Who decides which departments participate?	• Motivate participation in the shared service despite inevitable objections from independent business units.
Scoping and service definition		• Responsibility for determining the types of services that are in scope for the implementation. • Responsibility for defining the level of service that will be provided.	• Find the best set of functions to maximize the overall benefit of the service to the organization.
Support and funding		• How the organization will allocate resources to the project including human resources, technology, and cash funding. • Determine service costs for participants.	• Provide incentives for effective service provision.

Engage the key players in shared services governance

These players are important:		Because they:	Who are they?
The Driver The senior executive who has issued the directive to investigate cost saving through shared services		Define the expected result and determine the amount of pressure placed on potential participants.	Typically CEO or CIO
The Innovators The team that identifies specific opportunities		Identify viable approaches to achieving the driver's objective.	Senior IT managers
The Investors The organization that provides the investment financing for the shared service		Provide the funding for the initial investment and working capital for an initiative and expect a specific return on their investment.	Heads of business units
The Participants The leaders of the organizations that become clients of the Shared Service		Want cost-effective IT services for their organization.	Heads of business units
The Service Provider Establish timelines and staffing on a shared service project		Must deliver value to both the participants and the investors.	IT manager and staff

Successful governance relies on having all of these individuals contribute in their assigned way to the project.

Evaluate the trade-off of centralization and independence for shared services governance

Governance models are distinguished by two key characteristics: the degree of independence of the shared services unit and the degree of centralization.

Increasing Independence of Shared Service

Entrepreneurial
In the entrepreneurial model, the organization encourages BUs to make bilateral agreements to share services. The agreements are voluntary.

BU #1 → BU #2

Market-based
In the market-based model, the organization creates a centralized IT business unit and allows it to contract with individual BUs to provide IT services.

BU #1 ← Service BU → BU #2

Mandated
In the mandated model, the organization mandates how a business unit should share its own IT services with other business units: the service type and level it will provide and the chargebacks it will receive.

Organizational mandate

BU #1 → BU #2

Increasing Centralization

A note on the word "corporate"
This solution set uses the term to refer to the high-level organizational authority, in either the public or private sector.

Mandated models involve varying levels of centralization but the element of strong corporate control is the key element.

Choose the appropriate governance model for your organization

Relative importance of the pros and cons will depend on the implementation characteristics, particularly the size and number of participants.

Since the administrative cost of a new BU is largely fixed, it will appear smaller for larger organizations with larger BUs.

Increasing Independence of Shared Service

Entrepreneurial

Pro — Low governance costs and some level of sharing between BUs.

Con — Low level of centralization discourages participation, limiting benefits.

Market-based

Pro — Market forces drive efficiency in service selection and participation.

Con — Running a separate BU imposes an administrative burden.

Mandated

Pro — Increased participation in the implementation due to corporate mandate.

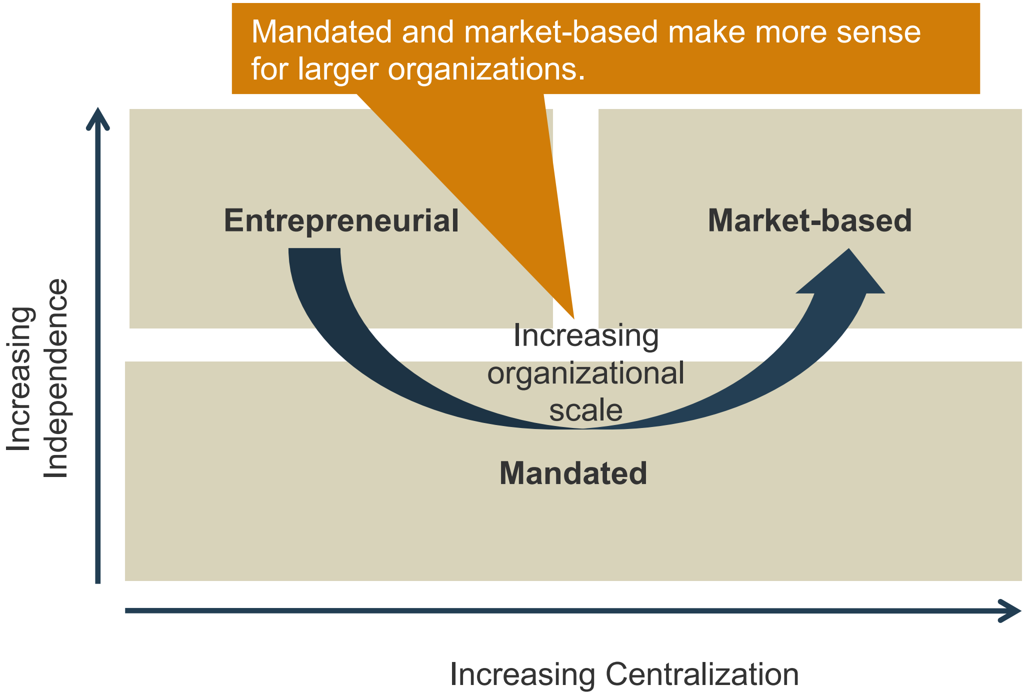
Con — Governance must coordinate requirements of all participants by way of consensus. With a large number of participants, that can become a very time-consuming activity.

Increasing Centralization

With a large number of participating BUs, the mandated model becomes difficult to orchestrate. However, the size of the BUs themselves is less important here.

Find the ideal combination of shared service independence and centralization

The ideal state for shared services governance depends on organizational size and service characteristics.



- Each model will produce **differing costs and benefits** for your organization. The highest net benefit determines where you should target your governance plan.
- The benefits of the mandated and market-based models increase with the **size of the organization**. In larger organizations, these benefits will outstrip the fixed costs of governance that these models impose.
- The market-based model makes the most sense for services that serve a **large number of individual business units**, regardless of the size of the individual BUs.

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The size of the organization and the number of participating departments are the primary determinants of which governance model you should choose.

To find the optimal path to shared services governance, use the *Shared Services Governance Strategic Roadmap Tool*

Input your organizational characteristics and the parameters of the shared services to find out how to govern your implementation.

Start with the roadmap tool.

- Info-Tech's *Strategic Roadmap Tool* will provide the key steps you should take right now to determine which shared services governance model is right for your organization, plus a high-level overview of the steps you need to take to get there.

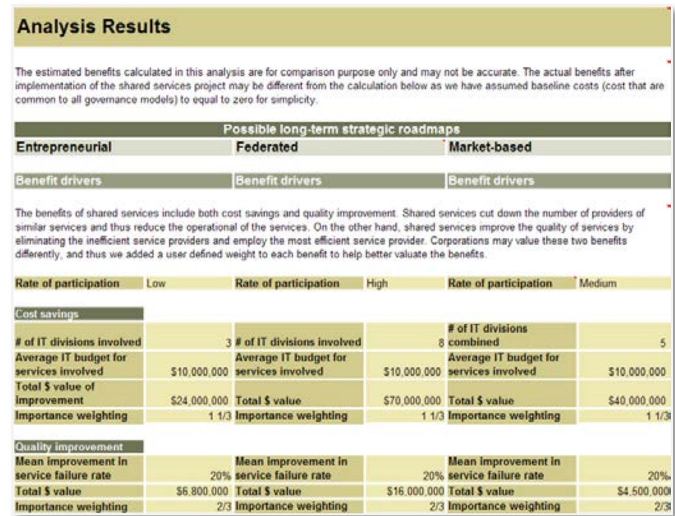
Then jump to the appropriate section in the storyboard.

- The next three sections show the detailed steps each individual needs to take for the governance program to succeed. Jump to the appropriate section for advice.

The optimal governance path will:

✓ Maximize the incremental benefit of the shared service.

✓ Align IT with the overall organizational governance direction.



Analysis Results

The estimated benefits calculated in this analysis are for comparison purpose only and may not be accurate. The actual benefits after implementation of the shared services project may be different from the calculation below as we have assumed baseline costs (cost that are common to all governance models) to equal to zero for simplicity.

Possible long-term strategic roadmaps					
Entrepreneurial		**Federated**		**Market-based**	
Benefit drivers		Benefit drivers		Benefit drivers	

The benefits of shared services include both cost savings and quality improvement. Shared services cut down the number of providers of similar services and thus reduce the operational of the services. On the other hand, shared services improve the quality of services by eliminating the inefficient service providers and employ the most efficient service provider. Corporations may value these two benefits differently, and thus we added a user defined weight to each benefit to help better valuate the benefits.

Rate of participation	Low	**Rate of participation**	High	**Rate of participation**	Medium
Cost savings					
# of IT divisions involved	3	**# of IT divisions involved**	8	**# of IT divisions combined**	5
Average IT budget for services involved	$10,000,000	**Average IT budget for services involved**	$10,000,000	**Average IT budget for services involved**	$10,000,000
Total $ value of improvement	$24,000,000	**Total $ value**	$70,000,000	**Total $ value**	$40,000,000
Importance weighting	1 1/3	**Importance weighting**	1 1/3	**Importance weighting**	1 1/3
Quality improvement					
Mean improvement in service failure rate	20%	**Mean improvement in service failure rate**	20%	**Mean improvement in service failure rate**	20%
Total $ value	$6,800,000	**Total $ value**	$16,000,000	**Total $ value**	$4,500,000
Importance weighting	2/3	**Importance weighting**	2/3	**Importance weighting**	2/3

The *Shared Services Governance Strategic Roadmap Tool*.

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The tool uses a range of organizational and process characteristics to calculate the relative benefits of each governance model (in relative terms).

Identify key characteristics of your organization and shared services to determine the appropriate governance model

Locate your organizational and service characteristics in this table to gain a sense of which model will work best.

	Entrepreneurial	Mandated	Market-based
Organizational characteristics			
Size	Small	Medium-Large	Medium-Large
Tendency toward centralization	Highly independent	Trend toward centralization	Trend toward centralization
Current level of collaboration between BUs	High level of collaboration	Any level	Some existing collaboration
Service characteristics			
Number of participating business units	Fewer than ten	Fewer than ten	More than ten
Risk tolerance for service delivery	High tolerance	Low tolerance	Medium tolerance

Use the strategic roadmap tool when multiple characteristics dictate differing governance models for your organization. The tool will weigh the characteristics to arrive at a unified recommendation.

Example scenario: sharing IT services in a small manufacturing firm

A small manufacturing firm wants to share ERP services between its hats, shoes, and gloves business units.

Entrepreneurial	Pro	Low governance costs.
	Con	No guarantee that the business units will actually share.
Mandated	Pro	The business units share the services exactly as the driver specifies.
	Con	Have to run a governance board including heads of hats, shoes, and gloves.
Market-based	Pro	A separate shared services unit caters to the needs of the BUs.
	Con	The shared services unit requires its own VP, directors, and support staff.

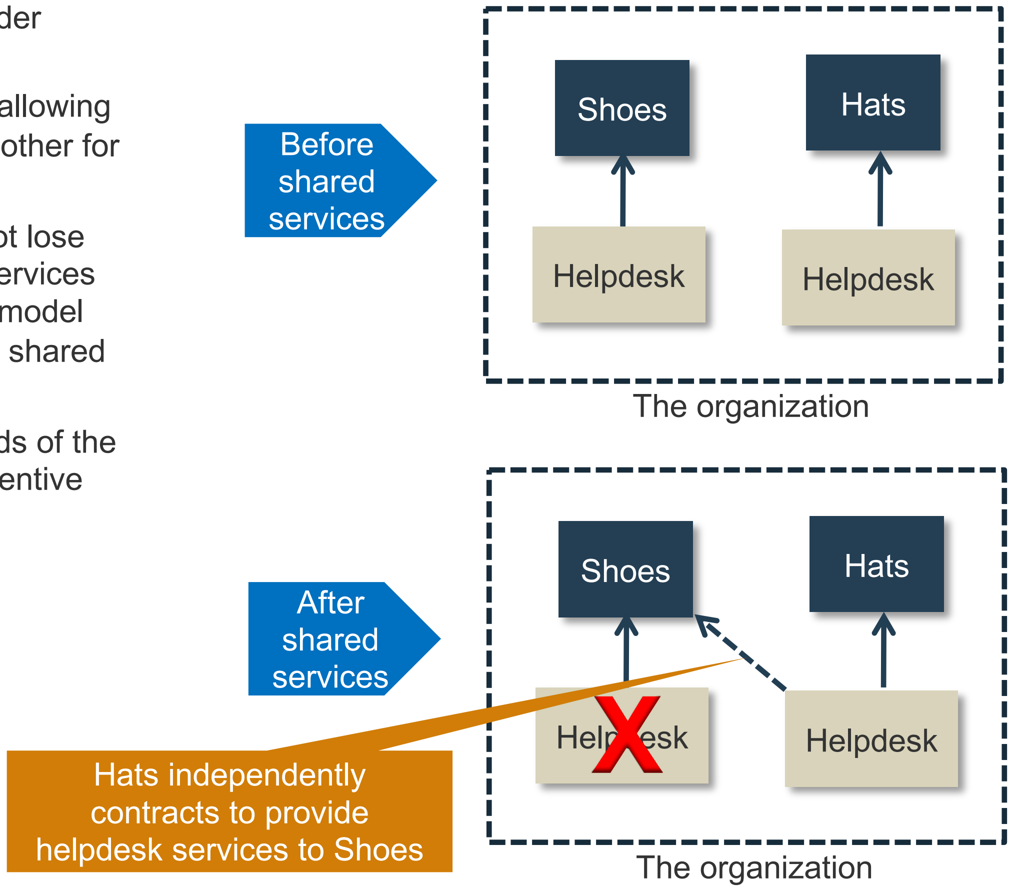
The *Shared Services Governance Strategic Roadmap Tool* points toward the entrepreneurial model. The next three sections will show how the tool arrives at this decision.

In the entrepreneurial model, participants voluntarily contract for services

Independence with ownership to the business unit

- In the entrepreneurial model, the service provider continues to reside within a business unit.
- The organization takes a hands-off approach, allowing individual business units to contract with each other for sharing of services.
- Because individual business unit leaders do not lose control over their IT, nor do they have to use services from other business units, the entrepreneurial model overcomes the central reasons that BUs resist shared services.
- The quality of service delivery rests in the hands of the BUs. The ongoing chargeback provides an incentive for competent administration of the service.

The entrepreneurial governance model



Leverage the initiative of business units using the entrepreneurial model

In entrepreneurial governance, you provide a framework in which business units can independently agree to provide services to one another.

Elements of governance

Management and participation

- Each business unit maintains ownership over its own IT services.
- Business units voluntarily participate in shared services.

Criteria for use

- Works best for coordinating sharing between a multiplicity of departments in a small organization.
- Limited participation makes it unattractive for large-scale services.

Scoping and service definition

- Business units arrive at bilateral agreements as to service level and define the type and quality of services to be provided.

Support and funding

- The chargeback is determined as part of the negotiation between the two business units.

Use the entrepreneurial model to overcome key objections & risks of shared services

Key objections	Entrepreneurial model overcomes because…
Differential benefits	• Service providers can insist on a chargeback that will compensate them for sharing their investment in high-quality IT capabilities.
Loss of control	• Business units can choose not to use an external service for mission-critical capabilities.
Lack of trust	• Participants agree on penalties for underperformance and the driver holds these against P+L.

Key risks	Entrepreneurial model mitigates these risks because…
Excessive speed to implement	• Service providers are bound by SLAs that invoke penalties for overpromising and under-delivering. That leads to realistic expectations for delivery time.
Insufficient capacity	• Service providers add customers gradually, allowing for a gradual ramp-up of capabilities.
Varying customer needs	• Service providers prioritize service features according to the value in chargeback dollars this generates for the business unit, which roughly correlates to the feature's importance to the overall organization.

Weigh the key benefits & costs of the entrepreneurial model

The entrepreneurial model imposes few governance expenses, but its key limitation lies in a low participation rate that limits savings.

Benefits

Reduced costs

Cost of running each IT department × (# of business units involved – 1)

Improved IT quality

(Failure rate of service provider – average failure rate) ×
Cost of failures ×
# of business units involved

# of business units involved = total # of BUs × **participation rate**

Costs

Costs of service implementation and maintenance are common to all governance models. There are few administrative costs above this.

The entrepreneurial model has the lowest participation rate of the three models.

- The IT service **resides in the serving business unit** and its primary goal is to serve that business unit.
- While collecting chargebacks helps the service provider's P+L, the service provider has **other strategic objectives** as well, for example, increasing market share or brand awareness.
- These **other considerations** will tend to **shape the service provider's capabilities** more than the desire to provide services in exchange for chargebacks.
- Faced with services that cater to them only as a second priority, participants will **use the service less** than in other governance models.

Use the entrepreneurial model in a small organization

The entrepreneurial model makes sense for organizations that cannot amortize governance expenses over large IT budgets.

- Entrepreneurial model **is a low-cost option**.
  - As the shared services are provided by existing IT divisions in different business units, less investment is needed to create this shared service.
  - There is no additional cost to set up a shared services committee or other structure.
- For small organizations, the **simplicity** of the entrepreneurial model will play an important part.
  - The cost of investing in a large-scale governance model can outweigh the benefit that a small organization experiences from shared services.
- This holds particularly true when the small organization is divided into a **large number of business units**.
  - Then it becomes expensive and difficult to coordinate between the departments, and the benefit of large-scale governance appears small.

Governance model	Key expenses
Entrepreneurial	Implementation costs
Mandated	Implementation costs + governance board
Market-based	Implementation costs + business unit admin

Cultural factors also play a part.
In organizations that have a cultural emphasis on independence, the entrepreneurial model provides an easy entrée into shared services. Rather than swimming against the cultural tide, the entrepreneurial model encourages independence and individual responsibility.

A small IT organization in this context would mean fewer than 100 IT personnel. A large number of business units would mean over 15 individual business units.

Example scenario: weighing the benefits & costs of the entrepreneurial model

In this scenario, the Hats department contracts with Shoes to provide ERP services. Gloves does not choose to participate.

Benefits

Reduced costs

	Cost to run ERP system
Hats	$20,000
Shoes	$80,000
Gloves	$10,000

Combined cost before shared services (including Gloves) $110,000 − **Combined cost after shared services (including Gloves)** $50,000 = **Savings** $60,000

+

Improved IT quality

	Failure rate
Hats	2/year
Shoes	3/year
Gloves	2/year

(**Combined failure rate before shared** 7/year − **Combined failure rate after shared** 6/year) × **Cost of each failure** $2,000 = **Savings** $2,000

Total savings $62,000

Low participation limits savings…

Costs

	Cost
Implementation	Common to all models
Dispute resolution	$2,000

…but costs are limited too.

Other factors
- Organizational trend toward decentralization
- High level of existing inter-BU collaboration
- No previous shared services failures

And other factors favor entrepreneurial

In the entrepreneurial model, provide a framework for service negotiation

The driver and innovators should mediate interactions between the BUs to reduce the risk that service providers will fail to live up to agreements.

Key responsibilities

The driver
(e.g. CEO)

Enable negotiation between business units.

- As the driver, you should cultivate an environment that fosters good relationships between business units such that collaboration is possible.
- Make sure that agreements have the force of law within the organization and allocate charges for underperformance as SLAs dictate.

Arbitrate disputes.

- Clarify to participants and service providers that they have the option of keeping their own metrics.
- Use whatever metrics the BUs have available in investigating complaints of service failures.
- In cases where provider and participant metrics consistently disagree, have corporate IT create its own metrics for that particular service. For data infrastructure, see *Develop a Data Infrastructure SLA*. For apps, see Info-Tech's *Internal Service Level Agreement for Application Maintenance*.

The innovators
(e.g. senior IT managers)

Provide template internal service agreements.

- Service agreements should include all the necessary components for regulating service provision and chargebacks, and be devoid of loopholes or "gotchas." Start with the *Internal SLA* template.

Generate awareness of available options.

- The innovator should publish a list of available services within the organization. Advertising for the services will make it easier for buyers and suppliers to find each other. See Info-Tech's solution set *Document the IT Service Catalog* for more information about how to make these important listings.

Allow business units to negotiate rules for quality control & pricing

Business units must form agreements that advance their own strategic objectives and must monitor performance.

Key responsibilities

The service provider
(e.g. IT manager)

The participants
(e.g. head of BUs)

Decide on a service level and penalties for underperformance.

- Both the participants and the service provider must take responsibility for evaluating the value of agreements for achieving their own strategic objectives. For metrics you can use for monitoring data infrastructure, see *Develop a Data Infrastructure SLA*. For apps, see Info-Tech's *Application Maintenance SLA* template.

Monitor performance.

- The driver would want to stay out of most disagreements, thus participants and service provider together have to monitor the quality of the shared services.
- Good communication between the participants and the service provider is essential to foster trust between business units.
- However, both parties should check performance of the service provider against the list of metrics mentioned in the SLA, on an ongoing basis. For help with monitoring of data infrastructure services, see Info-Tech's *Data Center Infrastructure Service Level Monitoring Tool*.

Devise a fair & effective chargeback scheme through negotiation

Support the investors and service providers in creating a chargeback scheme that motivates participation from both sides.

Key responsibilities

The service provider
(e.g. IT manager)

The participants
(e.g. heads of BUs)

Draw up a chargeback scheme.

- Chargebacks can appear as operating expenses in the budget of the investors and as revenue for the service provider. Alternatively, the organization may pick up the costs as a corporate expense.
- Either way, the chargeback scheme needs to work for both the service provider and the participants, and the driver needs to provide final approval.

The driver
(e.g. CEO)

Ensure that the chargeback is fair.

- Chargebacks should be reasonably close to the market value of the services.
- The chargeback allows for optimal allocation of funding to the shared services and ensures that both sides benefit after the implementation of shared services.

Key points about chargebacks.

- Avoid excessive detail: establish a composite charge for those items which only the service provider controls. Do not over-complicate the chargeback formula.
- Avoid volatility: exclude costs that change frequently. These will reverberate throughout the organization if included in SLAs.

More Info-Tech research on chargebacks:

- *Take Back IT Chargebacks*
- *Why Chargeback Systems Go Bad*
- *Use Chargebacks and SLAs to Wean Business Units Off the Box*

Case scenario: failure to enforce agreements leads to a lack of participation in an entrepreneurial model

The driver must remain vigilant to arbitrate disputes that can undermine confidence in the entrepreneurial model.

Situation

- A large telecommunications company has three business units: telephone, internet, and cable TV.
- The corporate CIO encourages the three BUs to share server hosting services through bilateral agreements.
- Telephone starts hosting cable TV's servers in its own server farm.
- After several months, a dispute arises between telephone and cable TV with regards to a power failure that led to a 5-second server downtime.

+

Action

- Not wanting to take sides, the CIO tells the two business units to come to an amicable solution.
- The dispute festers and eventually becomes public knowledge inside the company.
- With the expiration of their SLA, telephone and cable TV let their agreement lapse and telephone moves its servers back in house.
- Worse still, internet pulls out of a deal with cable TV to host its servers, fearing that a similar dispute could arise with respect to its own servers.

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Lesson Learned

- With respect to shared services governance, the driver is the law.
- Conflicts must be resolved promptly and fairly.
- The impact of effective governance goes beyond the relationship involved in the dispute: ineffective handling can reduce confidence in shared services across the organization.

In the mandated model, the corporation determines which BUs participate

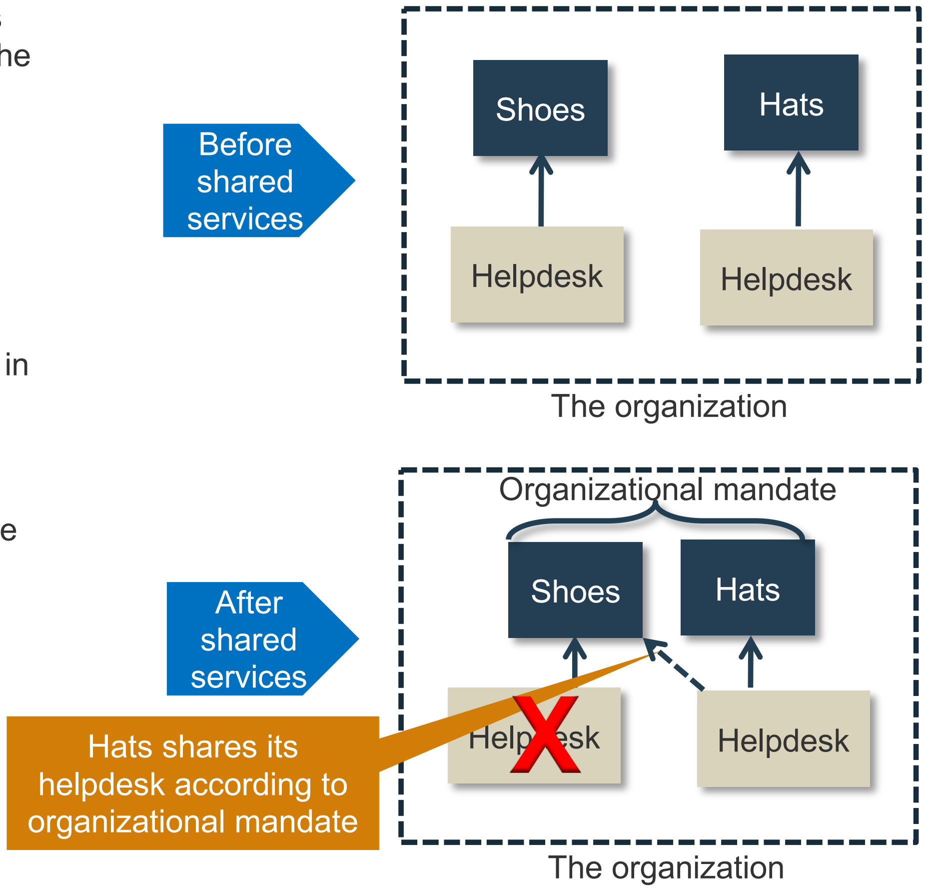
Sharing by consensus and corporate mandate

- In the mandated model, one business unit maintains ownership over its own shared service, much as in the entrepreneurial model.
- The corporation mandates sharing of services as it sees fit.
- Internal business units do not have the option of contracting with external service.
- That said, the driver must involve all the business units, both the service provider and the participants, in deciding what services the provider will offer and at what chargeback levels.
- The need to arrive at a consensus, under corporate guidance, drives the benefits but also the costs of the mandated model.

"*They are not allowed to compare the shared services to that provided by external vendors.*"

\- IT Director, Manufacturing (construction)

The mandated model for shared services



Use the mandated model to exercise control over the shared services implementation

The mandated model emphasizes the involvement of the corporate parent in the shared services implementation.

Elements of governance

Management and participation

- The corporation mandates the participation of all or nearly all business units in the shared service implementation.

Criteria for use

- Appropriate for large organizations that want to share services between a moderate number of business units (fewer than ten).
- Also appropriate when high levels of resistance to shared services will make voluntary participation unlikely.

Scoping and service definition

- Participants and service providers arrive at a consensus for service levels.
- The corporation arbitrates and ultimately signs off on the service level and penalties for underperformance.

Support and funding

- Chargebacks and corporate funding are negotiated by the participants in concert with the investors and the driver.

In the mandated model the driver must structure the governance model

The driver determines the participants and sets up the governance board.

The driver
(e.g. CEO)

Choose the participants in the service.

- Include the largest business units that have a need for the service. Consider excluding smaller BUs that require a highly differentiated service.
- Invite all participants to discuss the necessary elements of the service in a collaborative setting.

- **Create a governance board.** Once the service is up and running, create a governance board that will manage the performance and upgrade requests. For details about creating governance boards, see Info-Tech's solution set, *Establish an Effective IT Steering Committee*.

Members of the governance board:

- The driver or another senior executive.
- One representative from each of the participating business units.
- Representatives from the service provider.

Mandate:

- Allow participants to raise issues related to service quality and performance.
- Negotiate improvements to the service.

Frequency of meetings

- Monthly

"*[The driver needs to] work closely with the senior VPs who have the most influence.*"

- Al Povoledo, Partner, Canadian Project Partners

Start with participants that have prior experience working with the provider

Early success reduces concern about new initiatives.

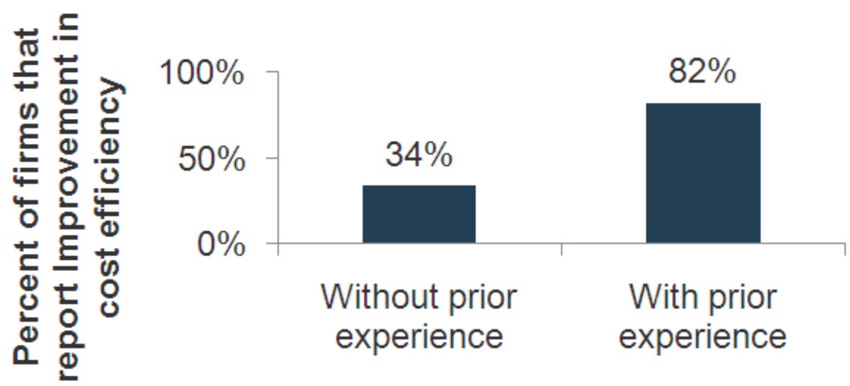
Start with participants who have experience working with the service provider.

- Prior experience between the service provider and participant improves trust and mutual understanding.
- The enhanced working relationship enables a higher chance for **improvement in cost effectiveness** through increased information-sharing and decreased need for monitoring.
- Improvement in cost efficiency will lead to more savings from implementation of shared services.

“*The executive director of the shared services organization is an employee of one of the BUs using the shared services.*”

- Shared service manager, public sector

Business units with experience using the service, experience greater cost efficiency



Source: Info-Tech Research Group; *N*=46

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While the driver can mandate participation, early successes will prevent a hailstorm of protest. Start with participants with whom the service provider has prior experience to increase your chances of early success.

The mandated model overcomes key objections with the driver's help

Key objections	Mandated model overcomes because…
Differential benefits	• Near-universal participation ensures that some BUs will come out ahead on some services, while giving ground on others. The net effect will even out.
Loss of control **Lack of trust**	• Involvement of the driver as a responsible overseer reduces the risk of over-promising and under-delivering by service providers.

Key risks	Mandated model mitigates these risks because…
Excessive speed	• Driver actively participates in setting implementation timelines in partnership with the service provider and the participants.
Insufficient capacity	• The driver can allocate capital as needed to support the shared service's operations.
Varying customer needs	• The driver prioritizes service needs according to overall corporate objectives.

Weigh the key benefits & costs of the mandated model

In the mandated model, governance costs scale with the number of business units involved. However, participation is high, resulting in greater benefits.

Benefits

Reduced costs

Cost of running each IT department × (# of business units involved -1)

Improved IT quality

(Failure rate of service provider – average failure rate) ×
Cost of failures ×
# of business units involved

# of business units involved = total # of BUs × **participation rate**

- The participation rate in the mandated model will be high, since the corporation mandates participation of BUs.
- In cases where the BUs resist, dismissal of some BU heads may be necessary.

Costs

Governance board

# of business units involved ×
frequency of meetings ×
duration of meetings ×
cost of executive time

- Other costs, such as staffing and asset needs, are common to all models and not included.

Avoid using the mandated model to coordinate across many BUs

The cost of running the governance board increases rapidly with the number of participants.

- The purpose of the board is to coordinate the differing needs of service participants.
- Coordination becomes rapidly more difficult as the number of participants increases, since the driver has to reconcile each participant's requirements against those of all other participants.
- As the number of participants increases, the need to reconcile increasingly divergent requirements introduces delays.

The complexity of coordinating between participants increases rapidly with the number of participants.

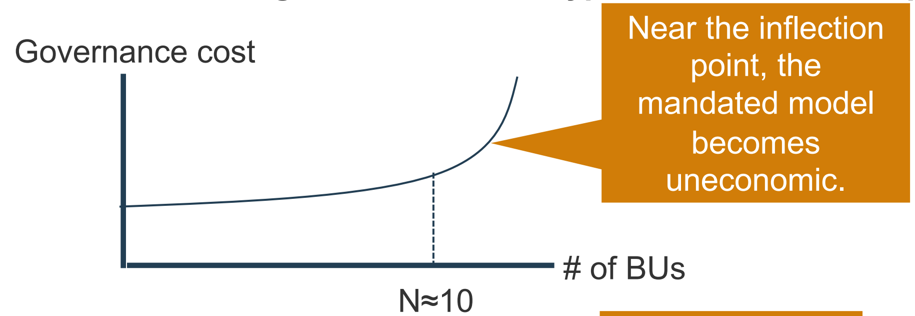
The mandated model makes most sense for larger organizations with fewer BUs

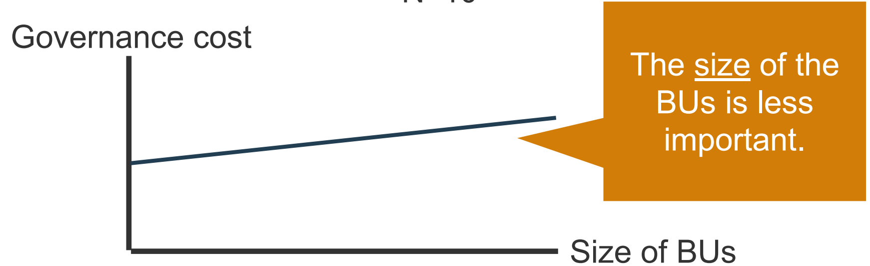
Large organizations can amortize governance expenses over a larger IT budget.

- **Higher participation rate.**
  - The mandated model forces business units to get involved, leading to a high participation rate.
  - The benefit of that participation (in absolute terms) is greater in larger organizations.
- **Increased governance expense.**
  - Unlike the entrepreneurial model, the mandated model incurs the expense of a governance board that includes members from each of the participant business units.
  - This is the cost of coordinating service across multiple business units.
- **Scaling with the number of participants.**
  - The cost of the governance board grows rapidly with the number of participants, making this governance method expensive for organizations that serve a large number of business units.
  - However, the mandated model can make sense even for large organizations if there are only a few BUs participating, even if the BUs are also large.

The mandated model leaves little to chance.
• The corporation takes a direct role in mandating the use of shared services.
• This makes it an appealing choice in risk-averse environments where BUs might resist using services.
• Examples might include services that operate in a highly regulated environment or are customer-facing.

Mandated model governance cost: hypothetical relationships





Example scenario: weighing the benefits and costs of the mandated model

In this scenario, the Hats department contracts with Shoes and Gloves to provide ERP services to both.

Benefits

Reduced costs

	Cost to run ERP system
Hats	$20,000
Shoes	$80,000
Gloves	$10,000

Combined cost before shared services $110,000 **-** **Combined cost after shared services** $40,000 **=** **Savings** $70,000

+

Improved IT quality

	Failure rate
Hats	2/year
Shoes	3/year
Gloves	2/year

(**Combined failure rate before shared** 7/year **-** **Combined failure rate after shared** 6/year) **×** **Cost of each failure** $2,000 **=** **Savings** $2,000

Total savings $72,000

Savings are large due to high participation…

Costs

	Cost
Implementation	Common to all models
Dispute resolution	$10,000
Governance board	$30,000

…but so are the costs of governance, making it less attractive than entrepreneurial

Other factors

- Organizational trend toward decentralization
- High level of existing inter-BU collaboration
- No previous shared services failures

And other factors favor entrepreneurial

Start the mandated model with simple, undifferentiated services

Early successes with undifferentiated services will encourage participants to embrace services with varying features and service levels later on.

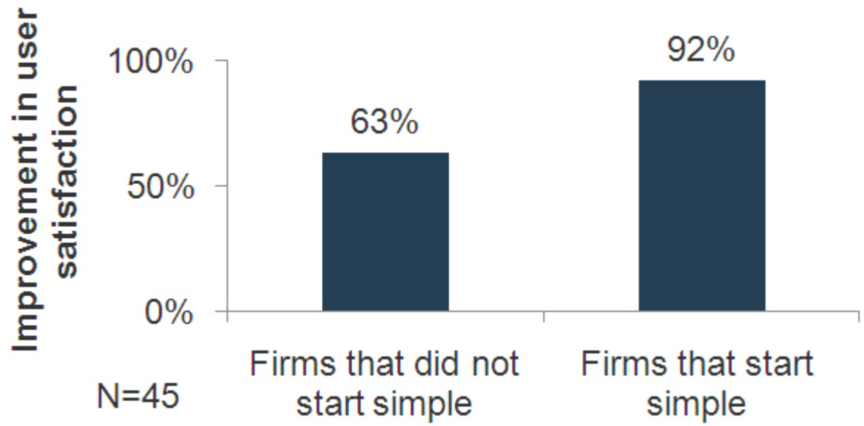
Start with undifferentiated services.

- Undifferentiated services allow the service provider to provide the **same service for every participant**. Some services only come in one size and color.
- An undifferentiated service creates the **greatest cost savings**, since the economy of scale for the process that drives the service exists across a large number of participants. With many service flavors, each process only serves a small number of participants.
- The **initial success** of an undifferentiated service will drive interest in more complex services.

Characteristics of an undifferentiated service:
- A single service level is provided for all participants
- There are few or no variations in service features
- All participants pay the same price per unit

Examples of common undifferentiated services:
- Data center housing
- Network infrastructure

Firms that start with simple services are more likely to improve user satisfaction



The mainframe was the second bundle because it's small and controlled.

- Glen Sustrik, Finance Officer, Service Alberta

Scoping Support

The driver must coordinate a consensus on service levels and price

Build a consensus based on current expectations for the service.

The driver
(e.g. CEO)

Build a consensus.

- Poll the business units that will use the shared service to discuss appropriate service levels. Most importantly, get a sense of the service level that the business units are currently used to.
- For metrics appropriate to data infrastructure, see *Develop a Data Infrastructure SLA*. For apps, see Info-Tech's *Internal SLA for Application Maintenance* template.

Decide on a service level and penalties for underperformance.

- The service level should be at least as high as the service each of the BUs is used to receiving in the majority of metrics.

Regulate and enforce service level agreements.

- As the driver—together with the investors, participants, and service provider—monitor the quality of the shared services.
- If participants raise complaints with service quality, check metrics against the SLA and take steps to rectify any lapses.

The participants
(e.g. heads of BUs)

The service providers
(e.g. IT managers)

Define a service level and a chargeback scheme.

- The services delivered should satisfy the business unit's standards and the chargeback should not exceed the costs they would otherwise incur for a similar service.
- However, the final decision is left to the driver. For more information on negotiating SLAs, see *Develop a Data Infrastructure SLA* or the *Internal SLA Application Maintenance* template.

Case scenario: mandated should not mean dictatorial; enlist the support & opinions of participants

The governance board must remain involved at all times in decisions regarding the service offering.

Situation

- The CEO of a large hardware manufacturer mandates the creation of a shared services unit that will provide helpdesk services to monitors, mice, and keyboards.
- He creates a governance board and seats a vice-president from each of the BUs on the board.
- Marshalling resources from the individual helpdesks, the CEO orders the corporate CIO to create a unified helpdesk that provides 80% of the needs of the individual business units.

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Action

- The governance board continues to meet, but the corporate CIO attends only occasionally. The board has limited power over the actual running of the helpdesk.
- With the acquisition of a small keyboard manufacturer, the keyboard BU starts to need dramatically quicker helpdesk service than the current SLA provides for.
- After failed attempts to influence the CIO and the helpdesk, keyboards secretly hires three helpdesk professionals from outside the company.

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Lesson Learned

- The governance board plays an important role in the success of the mandated model.
- The board must have power or the participants will lose confidence.
- While the driver can mandate participation, participants will find ways around the corporate mandate if they lose confidence.
- The driver or their representative must attend the board meetings to ensure the board has power over the provider.

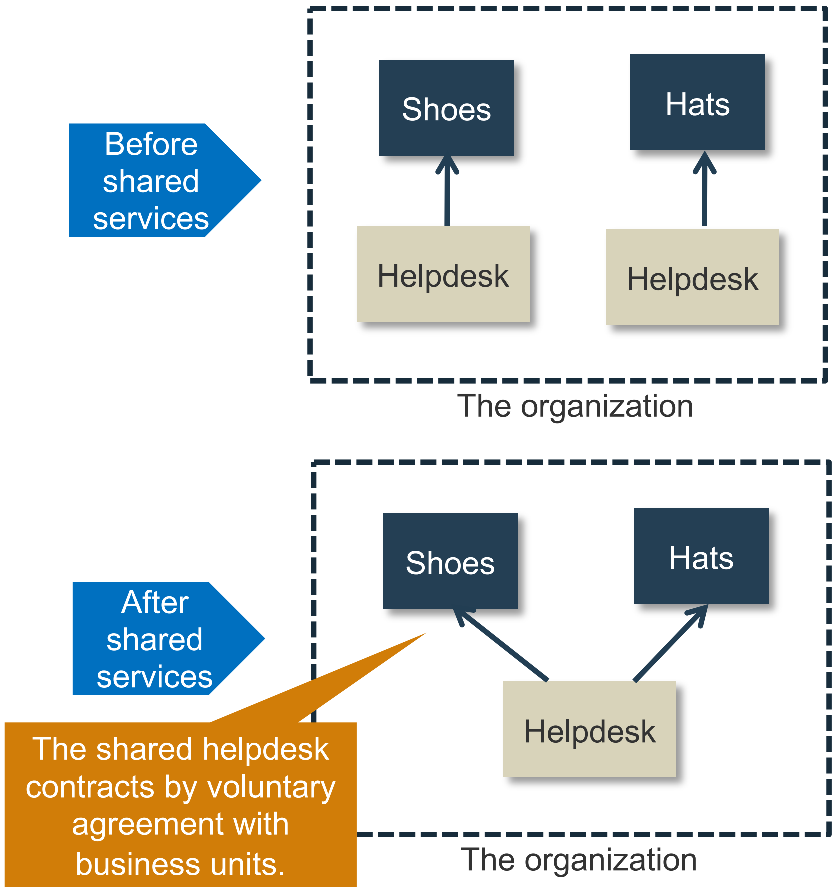
In the market-based model, a separate BU is established to provide shared services, and participation is voluntary

Total independence and separation from the BU

- In the market-based model, the shared services reside in a separate BU.
- The shared business unit contracts on an as-wanted basis with the internal business units.
- Internal business units also have the option of contracting with external service providers, so market forces will shape the terms of the agreements that business units make.
- The business unit heads do not lose control over their own IT; they can opt-out of using the shared service if they prefer to run their own IT or use external vendors.

> *IT is a service organization of its own. At Barry-Wehmiller, Corporate IT fosters leadership qualities in its people. Since we have no manufacturing at Corporate, we share our talents and services in supporting our business units.*
>
> \- Claude Stoltz, Manager of Enterprise Applications, Barry-Wehmiller

The market-based governance model



Select the market-based model if you have a broad customer base

The market-based model creates a separate shared services business unit and allows for voluntary participation.

Elements of governance

Management and participation

- The shared services reside in a separate business unit.
- Individual business units contract with the shared services business unit for services.

Criteria for use

- Appropriate for large organizations.
- Appropriate when the number of participating business units is high.

Scoping and service definition

- The shared services business unit provides IT services to all participants.
- The shared services business unit and individual business units come to an agreement regarding service levels.

Support and funding

- The chargeback is determined through negotiation between the BUs. Either party has the option of walking away from the deal.
- Internal market forces shape the price and service levels, albeit with an awareness of the need to remain competitive with external options.

The driver must lead the creation of the shared services business unit

The driver should put the administrative pieces in place to get the shared services BU off the ground.

The driver
(e.g. CEO)

Create the shared services business unit.
- Hire a business unit VP and directors. See Info-Tech's job description for the *Director of IT* role.

Decide whether to designate as a profit or cost center.
- The profit-center model is better, since it encourages the shared services BU to seek out new areas in which it can provide services and functionality.
- However, the cost-center arrangement can provide an easier transition if migrating from a mandated model with clearly defined service requirements.
- In this case, you can migrate to the profit-center model further down the road.

Provide start-up funding.
- If designated a profit center, then the shared services BU will eventually fund its own budget using chargeback capital.
- However, the driver must also provide capital for the growth of the BU, especially at the beginning.
- At the very least, the parent organization should fund the BU's first year of operation. See Info-Tech's solution set on *budget planning and negotiation*.

The service providers
(e.g. IT manager)

Generate awareness of available options.
- The innovator should publish a list of services available from the shared services unit. Advertising for the services will make it easier for participants to get involved. See Info-Tech's solution set on *service catalogs*.

Use the market-based model to create a framework for voluntary participation

Key objections	Market-based model overcomes because…
Differential benefits	• The shared services business unit uses best practices from across the organization, allowing it to offer services at a quality and price similar to that enjoyed by the best BUs.
Loss of control	• The voluntary framework allows for staged adoption. Highly risk-averse business units can wait for the service provider to prove itself before signing on.
Lack of trust	• The desire to generate revenue on an ongoing basis motivates the shared services unit to develop a strong internal “brand.” Internal SLAs provide additional motive for quality delivery.

Key risks	Market-based model mitigates these risks because…
Excessive speed	• The desire to build a strong brand inside the organization motivates the service provider to set responsible timelines, since long-term compensation of shared services managers depends on long-term chargeback revenue.
Insufficient capacity	• The shared BU can scale up its operations over time, starting with just a few customers.
Varying customer needs	• The shared services BU optimizes the offering to serve as many clients as possible. Since continued participation depends on high customer satisfaction, the unit tries to ensure that at least most of its customers achieve a satisfactory level of service.

Weigh the key benefits & costs of the market-based model

The market-based model has a high cost of administration. Unlike the mandated model, the cost does not scale with the number of participants.

Benefits

Reduced costs	Cost of running each IT department × (# of business units involved – 1)
Improved IT quality	(Failure rate of service provider – average failure rate) × Cost of failures × # of business units involved

# of business units involved = total # of BUs × **participation rate**

Costs

BU executive cost	# of executives and support staff involved in running shared services BU × Annual salary

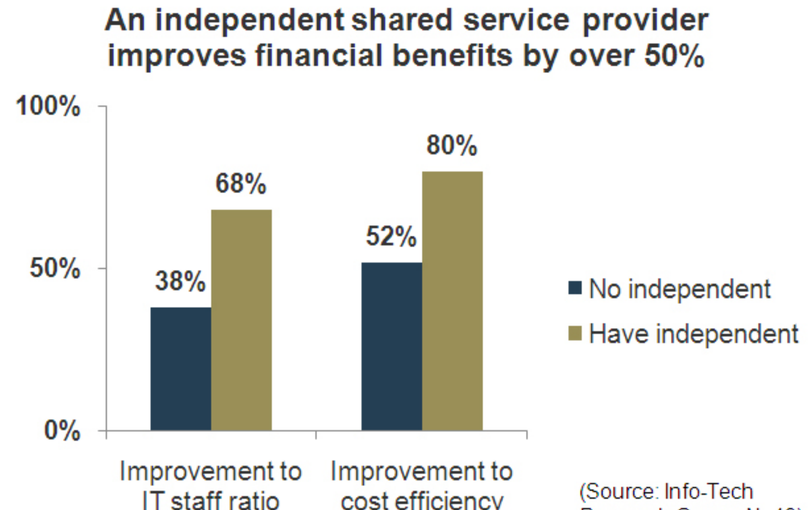
Other costs, such as staffing and asset needs, are common to all models and not included.

Market-based has a higher participation rate than the entrepreneurial model

- The incentive of increased revenue motivates the service provider to seek out internal customers.

The independent BU produces superior efficiency

- Having consolidated IT services enhances the efficiency of service provision beyond decentralized arrangement of the entrepreneurial model.



(Source: Info-Tech Research Group; N=43)

Criteria

Use the market-based model when business unit needs for services are very different

The market-based model enables groups within the service provider BU to specialize in services to different business units.

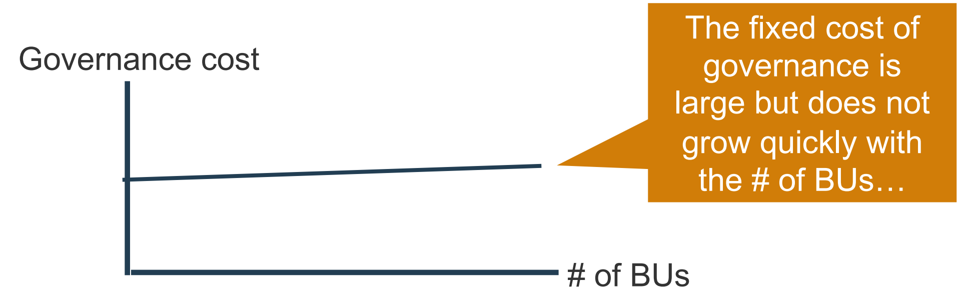
- **Service to a large number of customers.**
  - The centralized, independent approach of the market-based model makes it effective for serving a large number of customers.
  - Unlike the mandated governance approach, the administrative cost of the shared BU does not increase directly with the number of participants.
  - This is because the feature set is determined through the decision of the service provider, not through direct negotiation.
- **Specialized groups for service flavors.**
  - When the IT department is a separate business unit, it can create sub-divisions specialized in handling services for specific business units.
- **Fixed cost of administration.**
  - The shared BU has a fixed cost of administration that is best amortized over a large IT budget.

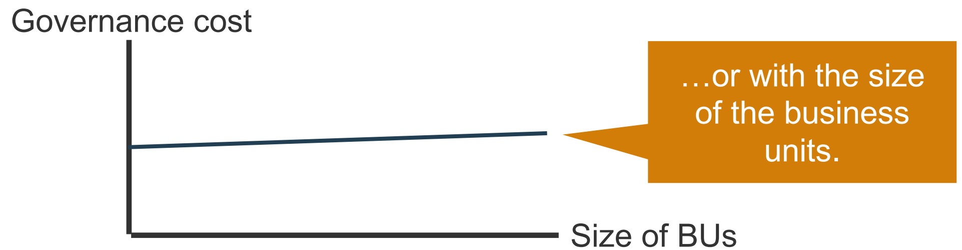
“*They send us to the [user-specific] helpdesk.*”

- User of shared service, public sector

Existing trend toward centralization. Shared services cannot swim against the general corporate tide. The market-based model will likely work best in organizations that have an existing preference toward centralization.

Market-based model governance cost: hypothetical relationships





Example scenario: weighing the benefits & costs of the market-based model

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	Cost to run ERP system
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Combined cost before shared services $110,000 − **Combined cost after shared services** $40,000 = **Savings** $70,000

Improved IT quality

	Failure rate
Hats	2/year
Shoes	3/year
Gloves	2/year

(**Combined failure rate before shared** 7/year − **Combined failure rate** 2/year) × **Cost of each failure** $2,000 = **Savings** $2,000

Savings are large due to high participation…

Total savings $72,000

Costs

Sample costs of running IT BU (beyond operational costs):
- Strategic planning
- Marketing
- Finance and accounting
- Human resources management

	Cost
Implementation	Common to all models
Dispute resolution	$7,000
Running independent BU	$45,000

…but so are the costs of governance, making entrepreneurial more attractive

Allow market forces to shape the service offering and ensure effective decision making

As a functioning business unit, the service provider must find opportunities to bring new services to the internal market.

The service providers
(e.g. IT manager)

Assess market opportunities.
- Like any business unit, the service provider should carry out market research to assess potential services it can offer within the company.
- As a profit center, the service provider has the normal incentives to provide services with benefits (in chargeback revenue) that outweigh its cost.
- Evaluate a range of service options to choose the one line-up that maximizes profit for the shared services BU, based on the expected subscribership, price level, and cost to provide.

The participants
(e.g. heads of BUs)

Decide on a service level and chargeback price levels.
- Depending on its market analysis, the service provider may offer a range of service levels and chargeback prices.
- The participants should pick the option that works best for them, or they can opt to continue providing the service for themselves.

The driver
(e.g. CEO)

Regulate and enforce service level agreements.
- As in the entrepreneurial model, the driver plays an important regulatory role in the internal market.

Hats, shoes, and gloves: a comparison of three models

In this scenario, the entrepreneurial model comes out ahead because of the limited benefit of increased participation.

	Entrepreneurial	Mandated	Market-based
Benefits	Reduced costs: $60k Quality: $2k **Total: $62k**	Reduced costs: $70k Quality: $2k **Total: $72k**	Reduced costs: $70k Quality: $2k **Total: $72k**
Costs	Implementation cost: common to all models	Disputes: $10k Gov board: $30k **Total: $40k**	Disputes: $10k BU admin: $45k **Total: $55k**
Net benefits	**Total: $62k**	**Total: $32k**	**Total: $17k**

The entrepreneurial model wins when additional participants are not available or add little value

Other factors
- Organizational trend toward decentralization
- High level of existing inter-BU collaboration
- No previous shared services failures

The existing trend toward decentralization and the high level of existing collaboration promise a high level of participation, reinforcing the choice.

Fictional scenario: XYZ Computer Manufacturing Firm

In this scenario, the mandated model comes out ahead because of the benefit of increased participation.

Before shared services

Number of BUs	5
Average budget on ERP service	$7 Million
Average failure rate	6%
Failure rate or best performing BU	2.50%

Other factors
- Organizational trend toward centralization
- Low level of trust or previous collaboration between BUs

Suitability factors favor mandated.

	Entrepreneurial (2 units participate)	Mandated (5 units participate)	Market-based (3 units participate)
Benefits	Costs: $3M Quality: $350k **Total: $3.35M**	Costs: $5M Quality: $1.1M **Total: $6.1M**	Costs: $2M Quality: $400k **Total: $2.4M**
Costs		Disputes: $10k Gov board: $1M **Total: $1.01M**	Disputes: $10k BU admin: $200k **Total: $210k**
Net benefits	**Total: $3.35M**	**Total: $5.1M**	**Total: $2.2Ms**

The mandated model wins because it manages five participants at reasonable cost.

Fictional scenario: ABC Financial Institute

In this scenario, the market-based model comes out ahead because of participation and the benefit of avoiding a large governance board.

Before shared services

Number of BUs	30
Average budget on ERP service	1 Million
Average failure rate	7.50%
Failure rate or best performing BU	2.50%

Other factors
- Organizational trend towards centralization
- High level of trust or previous collaboration between BUs

Suitability factors favor market-based.

The market-based model wins when many participants make mandated participation expensive.

	Entrepreneurial	Mandated	Market-based
Benefits	Reduced costs: $1.25M Quality: $500k **Total: $1.75M**	Reduced costs: $4M Quality: $1.05M **Total: $5.05M**	Reduced costs: $2.75M Quality: $800k **Total: $3.55M**
Costs		Disputes: $10k Gov board: $2.84M **Total: $2.85M**	Disputes: $10k BU admin: $300k **Total: $310k**
Net benefits	**Total: $1.75M**	**Total: $2.65M**	**Total: $3.24M**

Govern effectively to gain shared services value

- Three models for governance of shared services. Pick the one that works best for your organization and service scenario.
- The entrepreneurial model offers a low cost of governance but can limit participation in the shared service.
- The mandated model has high participation due to corporate mandate. The cost of negotiating service levels among a large number of participants can become prohibitive, especially as the number of participant business units increases.
- The market-based model leads to an optimized service offering for many participants. The administration of an independent shared business unit imposes a large, but mostly fixed, cost.

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