

Avoiding Shared Services Pitfalls

by [Karen M. Kroll](#)

[Verizon](#) Services in Basking Ridge, New Jersey, is helping its parent company, Verizon Communications Inc., save upwards of \$500 million annually. How? Verizon Services, a shared services center launched in 2005, provides financial, real estate, and supply chain services to Verizon's [business](#) groups and corporate departments. Previously, some of these functions were handled through outsourcing; others were handled by various business units, says Holyce (Holly) Hess Groos, vice president of finance and chief financial officer with Verizon Services.

Groos's group handles financial operations, including payroll, accounts payable, and remittance processing, for Verizon; it also collects past due accounts. In all, about 5,000 [employees](#) process more than \$140 billion in transactions annually. They were able to cut costs by about 15 percent in 2006 and anticipate another 15 percent reduction in 2007.

While some savings are a result of head count reductions (mainly by not filling positions when employees left or were promoted), most of it comes from more effective sourcing and expense [management](#), Groos says. For example, her group has brought back the bill printing function for one business unit; previously, Verizon contracted with an outside vendor for the service. Moving the function to internal has resulted in an 80 percent savings.

Moving to a shared services approach also has allowed Groos and her team to streamline processes. "Small work groups won't necessarily be as efficient as a larger work group in a production environment," she says. Moreover, by bringing together various work groups, Verizon Services has been able to cull and implement the best practices from each.

Verizon's experience illustrates the findings of a study done by JPMorgan and McKinsey in 2004. Researchers found that about 60 percent of the cost reduction opportunities generated by shared services centers result from process reengineering. Twenty percent comes from economies of scale, while moving operations to a lower-cost area typically accounts for 10 to 20 percent of savings.

This is not to say that Groos advocates moving all functions in-house. "It doesn't always make sense," she says. When an outside service provider is more effective, she'll use one. Moreover, by consolidating purchasing power in the shared services center, Groos typically is able to cut 20 to 25 percent off the cost of the service.

While it's difficult to say whether more companies are moving to a shared services center

approach, many are trying to establish "centers of excellence," or best-in-class operations for different functions, says Christine Allen, vice president and senior consultant with JPMorgan Chase & Co., New York. A shared services center can be one way of achieving this.

Most shared services centers that handle financial functions start with accounts payable and payroll, says Allen. A growing number are adding liquidity management functions, such as concentrating and investing cash, as well as foreign exchange management, to their list of services, she adds. In her experience, some companies decide not to move accounts receivable to a shared services center, for fear of disrupting the customer relationship.

On the other hand, Kathleen Brumme, worldwide manager of [marketing](#) for business process outsourcing with Hewlett Packard in Palo Alto, Cal., says that many companies do move to a shared services approach for accounts receivable. This is particularly true for companies that process many customer payments, as the savings can be substantial.

No matter which functions are included, establishing a shared services organization requires more than simply bringing numerous support groups under one roof. "Just centralizing an organization or function is not shared services," says Allie Young, research vice president with Gartner, Inc., Stamford, Conn. Young also is a co-author of *Multisourcing: Moving Beyond Outsourcing to Achieve Growth and Agility*.

A shared services organization, Young says, should act like an external service provider. That is, it should focus its people, processes, [technology](#), [funding](#), and governance to meet specific expectations for the value it will bring the business, she adds.

This is the approach that NASA's Shared Service Center, which launched in March 2006, has employed, says Kenneth Newton, deputy director of service delivery. NASA's shared services center currently processes about 70,000 travel vouchers and benefits for 20,000 employees annually. Early in 2008, the center, which is in Bay St. Louis, Mississippi, will begin processing about 145,000 invoices, and add several other functions as well.

Previously, NASA had consolidated various services, such as payroll and travel expense processing. Newton explains the difference to the shared services approach. "With consolidated services, the customer doesn't have a lot of say in the processes or performance," he says. "And, there's not a lot of ability to change the culture of the customer base."

In contrast, under the current shared services approach, the Center's internal customers have a say in how service is provided. Newton and his colleagues also work with their customers to help them change their processes to reduce costs.

For example, early on, about one-quarter of travel vouchers processed by the Center had to

be reworked. In most cases, the employee hadn't included the correct code indicating the account against which the trip was to be expensed. (By law, funding has to be available before a trip can be taken.) "We would process the voucher and find that funding wasn't where it should be," Newton says.

Not only did this cause rework, but also it could hold up employee reimbursements beyond the four-day turnaround time frame that the Center was aiming for. Newton helped his colleagues to analyze and change their internal processes so that travel vouchers were less likely to be coded incorrectly. In addition, the Center began charging departments for rework caused by their mistakes. "It wasn't fair to have everyone bear the cost," Newton says. Since then, the failure rate for travel vouchers has plummeted to 2.9 percent.

As the experiences of Verizon and NASA illustrate, a shared services center can bring about tremendous efficiencies and also improve service. However, several steps are key to achieving these goals:

- **As with any major corporate initiative, sound project management is critical.**

Those in charge need to set clear goals, gain senior management support, and sell the concept internally, says Allen.

Management within Goodrich Corporation, a \$5.9 billion supplier to the defense and aerospace industries, went on a "road show" to explain the change to a shared services center to employees at the affected locations, says Jeannot Jonas, director of global foreign exchange and international treasury with the Charlotte, North Carolina-based firm. This helped to allay resistance to the shift, which occurred in 2007.

- **Look for individuals with relevant experience** to oversee the shared services center, says Newton. Several of the top managers at NASA's shared services center previously held top positions within other centers. "We have a great leadership team," Newton says.

- **Management also needs to consider the culture of the organization**, says Scott Coffing, senior vice president of the Americas with Sungard in Charlotte, North Carolina. If it's highly decentralized with largely autonomous operating units, making the move to a shared services approach probably will be more challenging than it is when the company already has some degree of centralization. A change in incentives can help. For example, business unit leaders may get some bonus or incentive when they comply with requests to stop holding excess cash.

- **The functions chosen to come under the shared services umbrella should have enough volume** that the company will gain economies of scale by consolidating them, Brumme says. "You need scale to overcome the start-up costs." No clear formula can determine the point at which a shared services approach clearly will lead to economies of

scale. However, the break-even point tends to drop as the costs for the employees doing the transaction processing rise. The functions also should be ones that can be adequately served remotely.

- **The shared services center should have a specific method of charging for the services it provides**, says Young. While a shared services center typically isn't charged with making a profit, it still should strive to operate effectively and efficiently, as any external service provide would.
- **Management needs to consider the level of technical integration** across the various business units, Brumme notes. The less integrated a company's information systems are, the greater the work and cost required to make a shared services approach pay off. However, it's increasingly feasible to use middleware to make the connections between different software applications, she says.

Verizon, for example, had not completely consolidated its financial systems before moving to a shared services center approach, says Groos. "We still have varying degrees of PeopleSoft and SAP." So, Verizon uses tools, such as Common Desktop, to interface between different financial applications.

At the same time, it's important to recognize that "you can't do this without technology," Coffing says. "I've seen people scrap around with emails and spreadsheets. They may tell themselves that they've got a shared services organization, but they're not achieving it." For instance, the business units may transfer excess cash balances to a centralized corporate account at the end of each month or quarter. This is good, as far as it goes. However, without adequate reporting tools, it may not be obvious that some units hold large sums of money that doesn't earn interest for several weeks.

- **Obtain input from tax and legal professionals** before deciding which functions and entities to include in the shared services center, recommends Jonas. For instance, commingling funds from foreign and domestic entities may raise red flags with the tax authorities.
- **"Avoid decisions that pacify,"** recommends Newton. That is, you don't want to leave some pieces of a process out in the field just to get people to go along with the shift. For example, when a NASA employee dies, another employee from the agency discusses with the family the benefits for which he or she eligible. Initially, personnel at many of the sites lobbied to retain this function, saying that they could provide the information with a more personal touch. Newton and his colleagues discussed the issue with the field personnel, reminding them that just because an employee is remote doesn't mean that he or she won't be able to handle this situation with compassion.

At the same time, Newton works hard to keep the Center employees in touch with the people they support. He arranges for scientists and engineers to speak to the staff and sends Center employees to other NASA sites around the country. "In this way, they understand the people we're serving," he says.

Groos also spends a great deal of time nurturing relationships with the business units. "I spend a lot of time with my customers, making sure that they know the value we're delivering and the initiatives in place to drive results even further," she says. A hands-on approach can help win over business unit employees who might not want to give up control of a particular function, Groos notes.

- **Finally, "avoid the big bang theory,"** advises Allen. It's most effective to move to a shared services approach in stages, rather than trying to convert all departments at one time, she adds.

When companies go through the steps required to effectively move to a shared services approach, they can drive great efficiency. According to Newton, at NASA, the move to a shared services approach will save about \$10 million this year. This compares with the \$6 million originally forecast. Much of the savings is due to staff reductions and reassignments. Concludes Newton: "I think that this is a great thing for this agency."

Shared Services: A Prelude to Outsourcing?

Is moving to a shared services center usually a precursor to outsourcing functions altogether? Young says that this often is the case, particularly if the functions handled by the center allow the organization to operate effectively but don't drive competitive advantage.

However, Allen says that few companies actually take this step, because it is not automatically a clear money-saver: "You're just moving functions from one environment to another."

Managers wondering which path to take need to realistically assess whether they have the skills needed to operate the shared services center at a world-class level, Brumme says. They also need to decide whether they want to invest in technology and people at the level required to maintain world-class operations.

When the functions aren't key to a company, outsourcing can make a great deal of sense. Emerson Group provides [sales and marketing](#) expertise to small companies that want to sell to mass-market retailers, says Patrick Gibbons, partner with the Wayne, Pa.-based firm.

Emerson's clients face an uphill battle in getting retailers to even consider placing orders, given that they supply a limited number of inventory items. The retailer's cost of processing a small order from a vendor selling a handful of products is no different than if they're buying thousands of items from Procter & Gamble.

So, Emerson brings its clients under a single vendor number for shipping, fulfillment, and accounts receivable; applies any deductions taken by the retailers to the proper company; and reconciles the accounts. In offering these services, Emerson's management team had to decide whether to develop its own staff or outsource the functions. "We are sales, marketing, and logistics," Gibbons notes. "Do we want to get bogged down in that?"

They decided that they didn't, and engaged Fesnak and Associates, LLP, an accounting and consulting firm in Blue Bell, Pa., that offers back-office shared services. "Fesnak's ability to expertly focus on cash management, deduction reconciliation, and cash disbursements has enabled us to offer an entirely unique business solution" and allowed Emerson to focus on providing sales and marketing expertise, Gibbons says.

Originally printed in the [November 2007](#) issue of *Business Finance*