



The Public
Manager

*The New Administration's
Shared Services Opportunity*

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EXECUTIVE SUMMARY

What Is/Are Shared Services?

“Shared services” is an operating model used by organizations around the globe to organize and deliver internal support services more efficiently and effectively. It generally involves removing work activities from business units and standardizing and consolidating the way in which those services are delivered to provide value to the business units in the form of reduced cost and increased service performance.”

*-- Finance Shared Services
The Hackett Group, 2007.*

“Shared services” is a transformational business model for managing “back office” administrative services, such as financial management (FM), human resources (HR), purchasing, and information technology (IT). These services support the objectives and missions of any business or government enterprise and are essential for any organization to function. They are also very routine activities with low strategic value, and the work processes and IT systems used to manage them are easily standardized and consolidated into “shared service organizations” (SSOs) that can perform them more cost effectively than most organizations can for themselves. In today’s economy, there is no reason for any government or business enterprise to “own” its own back office when faster, better and cheaper services are available through high performing SSOs.

Shared services are producing impressive business results in leading public and private sector organizations around the world. Their use in the Federal Government has been championed by both Republican and Democratic administrations, but adoption and maturity have lagged behind global pacesetters.

This paper describes the global evolution of shared services and recommends ways to accelerate adoption and realization of benefits in the Federal environment. A stepped-up effort can free up resources currently over-invested in routine, administrative functions for redeployment to urgent national needs such as energy independence, health care reform, and stabilizing Afghanistan. To realize this dividend, the Obama Administration should: (1) articulate an ambitious government-wide vision of strategic intent to drive higher utilization of shared services; (2) develop a robust performance management framework to drive SSO performance improvement; (3) establish Federal SSOs as business-like, high performance organizations incented to compete in a public-private sector shared services marketplace; (4) create a new Office of Federal Shared Services to manage a competitive shared services environment; (5) develop a comprehensive, customer-driven governance framework to drive SSO cost, productivity, transparency and accountability

improvements; (6) make strategic technology investments to complete necessary infrastructure modernization and accelerate service improvements; (7) ensure a significant opportunity for the private sector to invest in the success of a competitive public-private shared services marketplace; and (8) enlist the active support of Congress in driving these reforms.

A focused, accelerated effort could produce 10 - 20% savings in operating costs of shared business processes, freeing up billions of dollars for higher value purposes (the lack of government cost information precludes reliable estimates of potential savings). Additional productivity, transparency and accountability improvements would provide substantial business value throughout the Federal Government.

Origins and Trends in the Private Sector

The shared services revolution began in the late 1980s and 1990s with the adoption of commercial off-the-shelf (COTS) enterprise resource planning (ERP) software packages by leading commercial enterprises. These highly standardized and scalable technology platforms fully integrate administrative functions and entire business supply chains, thereby enabling consolidation of redundant IT infrastructure, business processes and organizations across a large base of SSO customers. The cost and service improvements enabled by SSOs are achieved through:

- Standardization, such as standardized systems and transactions, etc.
- Simplification, such as streamlined processes and fewer disparate systems, databases, and organizations.
- Technology leverage, including processing more transactions electronically, making greater use of partnerships with best-in-class providers and extending to self service.

SSO Purposes

- Achieve cost savings
- Improve customer services
- Make IT services more robust, and secure
- Free up resources to enable improved focus on core mission

SSO Defining Characteristics

- Significant customer role in SSO governance process
- SSO must bill all of its services to customers
- SSO-customer relationships defined by mutually agreed service level agreements
- SSOs managed to continuously reduce costs and improve services

The earliest SSOs were created to serve – at an arms-length, business-like basis -- the business units out of which they were created. Some of these internal¹ SSOs have become so successful that they have transformed themselves into commercial providers of the same services to customers external to their host enterprises. Today, over 80% of the Global 2000 largest companies receive back office support from either an internal or an external third party SSO².

Whether internal or third party, an SSO's sole mission is to provide services to its customers as efficiently and effectively as possible. This relationship creates a “win-win” illustrative of the economic law of comparative advantage: the organization that sheds its back office to an SSO enables itself to focus its resources more squarely on its core mission and the things it does best, while the SSO does likewise.

The following trends in the global private sector shared services environment have important implications for government adopters:

Trend 1: Shared services are driving significant cost, productivity and service gains in the global economy. The following benefits have been reported in the private sector:

- Most shared services initiatives produce cost savings of 15 - 30%³
- 89% of users realized greater than 10% productivity improvement⁴
- 82% realized greater than 10% quality improvement⁴
- 79% experienced greater than 10% customer service improvement⁴

Moreover, these benefits are increasing as SSOs mature and take greater advantage of scale and technology leverage across growing volumes of services, transactions and customers.

Trend 2: SSOs increasingly are becoming multi-functional and encompassing entire business processes⁵. The earliest SSOs managed a few basic transactions processed by ERPs, such as FM, travel and payroll. As they gained acceptance, more services have been assigned to SSOs. They are simultaneously moving up the value chain into higher value, decision-support services such as research and data analytics and encompassing entire business processes such as loan servicing, collections and claims processing in the financial services industries.

Trend 3: Shared services follow a predictable evolution path from consolidation to virtualization. As SSOs mature they get better at using sophisticated management tools to measure and continuously improve productivity, and smarter about using external business partners to drive services to best-in-class performance levels. SSOs mature through four phases: consolidation; standardization; optimization; and virtualization. These phases are described briefly below and in more detail in Table 1 in the appendix to this paper.

Phases of SSO Maturity⁴

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| <ul style="list-style-type: none"> ▪ Consolidation is the initial stage where multiple systems, processes and organizations are combined to perform the same or similar transactions and services under one roof. |
| <ul style="list-style-type: none"> ▪ Standardization focuses on standardizing services and underlying policies, procedures and technologies and beginning to establish governance, pricing and customer management processes. |
| <ul style="list-style-type: none"> ▪ Optimization involves intense focus on improving cost and service performance through continuous process improvement, more sophisticated governance and rigorous performance management through benchmarking and metrics. |
| <ul style="list-style-type: none"> ▪ Virtualization involves the expansion of services, technology innovation and greater use of external business partners to drive further improvements in cost and service performance. |

Trend 4: Internal SSOs are consolidating into larger scale third party SSOs. Due to their larger scale, transaction volumes, and investments in IT, third party SSOs enjoy significant cost advantages over internal SSOs. A 2007 McKinsey study⁶ estimated that the average cost of operation of internal SSOs is 37% higher than third party SSOs. The Tata Group’s acquisition of Citibank Global Services (an internal business process center) is one recent example of this consolidation trend. Experts report that a large number of internal SSOs are failing to meet their business objectives and are ripe targets for consolidation. The consolidation trend is expected to continue into the foreseeable future and drive significant concentration in the commercial shared services environment.

THE GLOBAL GOVERNMENT SHARED SERVICES MOVEMENT

The shared services wave is breaking on the shores of all levels of government in Australia, Canada, New Zealand and the United Kingdom. Global government adoption is following a similar evolution path to the commercial sector, beginning with consolidation of IT infrastructure and applications and gradually moving up the value chain to capture entire business processes. The highest payoff and most widely adopted government shared services, as in the commercial sector, are FM, HR, acquisition and IT. Government adoption rates for next wave shared services, such as facilities, customer service, real estate, supply chain, and legal services, are at about 20% and growing⁷. The following points reflect the current state and trends in the global government shared services environment:

- Global government investment in shared services is increasing at over 20% per year, led by Europe (34%), Australia (27%), Canada (26%), US State-Local (23%), and US Federal (20%)⁸.
- US state-local growth is accelerating due to recession-impacted revenue shortfalls. The National Association of State CIOs has identified consolidation and shared services as top “tough times” strategies for state governments⁹. Over 20 states have consolidation/shared services initiatives underway today.

- The United Kingdom government reports that “...by 2016 the majority of the transactional elements of Corporate Services will be delivered through a handful of professional shared service organizations. Some of these organizations will remain inside the public sector, but many will be outsourced¹⁰.”
- Government SSOs are becoming increasingly multi-functional. A 2007 Accenture survey found that 64% of single function government SSOs plan to become multi-functional⁷.

Expectations are growing around the world that shared services will also enable significant gains in transparency and accountability in government business activities. Queensland, Australia, embraced transparency as an explicit objective that will enable more business-like pricing by service providers through improved benchmarking and performance monitoring, and more predictable budgeting for customers¹¹. The cabinet office of the United Kingdom has identified improved transparency in resource allocation as a leading measure of effectiveness enabled by shared services in the context of transformational government¹². In Scotland, transparency has been championed as a direct byproduct of streamlined and standardized processes enabling improved benchmarking and cost control¹³. Many state and local initiatives in the US recognize transparency gains as a direct benefit or an explicit objective of shared services initiatives.

Shared services initiatives present significant management challenges that cannot be underestimated. Experts report that a significant percentage of government consolidation and shared services initiatives will not achieve their intended benefits. The toughest challenges are associated with leadership, governance, project management and ability to realize savings either by reducing head counts or re-investing into higher value purposes. Most experts believe that the single most important success factor is active, engaged executive leadership at the highest levels.

Another significant success-enabler is structural independence. The record suggests that the most successful government SSOs are created as independent organizations – separate from mission related policy or program delivery organizations.

Three of the more successful global government SSOs are profiled in Table 2 in the appendix: Ontario Shared Services in Canada; Queensland State Government Shared Services in Australia; and the National Health Service/Steria public-private partnership in the United Kingdom. They reflect characteristics and best practices that merit consideration by other government adopters:

- Multi-functional scope, including FM, HR, payroll, and acquisition
- Dedicated SSO structures, independent of competing programmatic or mission influences, and
- Significant to extensive relationships with private partners to achieve best of breed technology leverage (Ontario is one exception to this trend).

SHARED SERVICES IN THE US FEDERAL GOVERNMENT

The Decades of the 1980s and 1990s

Shared services are nothing new to the US Federal government. They have roots in the inter-agency cross-servicing and administrative consolidation initiatives that began in the 1980s as part of the Reagan Administration's Reform 88 management improvement initiative. Payroll was an early target of opportunity, as modernized departmental payroll centers at the Departments of Agriculture and the Interior were promoted for use by external customers. Consolidated financial and administrative service centers were created in several departments, such as the Department of Commerce, where four regional centers were created by consolidating administrative functions from several bureaus. Many of these 1980s era consolidated service centers continue to operate at various degrees of modernization and have the capacity to be leveraged more broadly as government-wide shared services assets.

Common Administrative Support Units (CASUs) were another 1980s innovation that established cross-servicing relationships across smaller agencies and in remote locations where it was not cost-effective for each agency outpost to maintain its own dedicated administrative staff. Today, CASUs continue to flourish under the leadership of a national inter-agency board of directors chaired by GSA and numerous local boards of agency users and a lead agency in each community in which they operate. CASUs provide over 90 administrative services in over 2,000 communities nationwide.

The government reinvention initiatives of the Clinton Administration in the 1990s took these approaches a step further by establishing, with Congressional authorization¹⁴ on a pilot basis, franchise funds – administrative units with explicit charters to cross-service external customers on a competitive, business-like basis. The purpose of the initiative was to promote government-wide competition among common administrative service providers, leading to a more competitive environment, lower cost, higher quality, and more timely services. The pilot authorities were extended permanently in 2005 and remain useful enablers of broader shared services transformation, but the level of franchise fund activities has declined since the late 1990s.

Today, in many large departments and agencies that remain structured in a holding company model -- those composed of large, autonomous operating units -- the centralized departmental or headquarters administrative staffs that serve the entire enterprise are funded through working capital funds and operate -- in fact, if not in title -- as shared services. Examples include administrative functions at the Departments of Agriculture, Energy and Justice. A majority of them meet most recognized attributes of SSOs: they provide fee-for-service financing at cost recovery through working capital funds; they have customer boards of directors; they use some form of negotiated service level agreements; and their services are subject to some degree of improvement effort. If some of the lower-value work performed by these administrative staffs were transferred to SSOs, the resources could be re-purposed to higher-value missions.

The Decade of the 2000s

The Bush-43 Administration's President's Management Agenda (PMA) drove shared services adoption through its e-Government initiative. An initial set of 24 common IT solutions was identified where agencies historically made significant individual investments to address needs they perceived as unique but that were, in fact, common and duplicative of each other. An objective of the e-Gov initiative was to transform this agency-specific behavior into a new model of joint investments in IT designed to meet common, standard requirements shared by numerous agencies ("buy once, use many").

The e-Gov program was expanded to include nine common, but more complex "lines of business" (LoBs) as candidates for standardization and inter-agency collaborative management and investment. Three of the LoB initiatives adopted shared services business models: FM, HR, and information systems security (ISS)¹⁵. The shared service model was also implemented successfully for the e-Payroll initiative (one of the 24 e-Gov initiatives) which consolidated 26 agency payroll centers into four third party SSOs (e-Payroll was the next generation of the payroll consolidation initiative that began in the 1980s). Table 3 in the appendix lists the universe of OMB-chartered third party/government LoB SSOs in the Bush-43 Administration.

The LoB initiatives were driven as government-wide IT initiatives, and their focus was limited to consolidation of the applications and, to a lesser extent, the IT infrastructure supporting the applications. This focus enabled progress toward modernizing management infrastructure -- a necessary first step -- but it did not realize the full measure of cost savings and productivity improvements possible through cross-government consolidation. Moreover, significant infrastructure components, such as the e-Payroll centers, remain served by legacy systems dating back to the 1970s, 1980s and 1990s that remain begging for modernization.

A major issue that stalled cross-government LoB modernization in the Bush-43 Administration was Congressional objection to interagency investments across appropriation accounts controlled by different committees of Congress. These jurisdictional concerns must be addressed directly to enable successful government-wide transformation in the future.

In addition to the Bush Administration's LoB/Third Party/Government SSOs, a large number of internal SSOs emerged and evolved in the 2000s -- not as part of a government-wide program, but through the independent leadership of their host agencies. A few examples include the Internal Revenue Service's Office of Agency-wide Shared Services; the NASA Shared Service Center; and the US Postal Services Shared Services Organization. In fact, most of SSOs designated by OMB as LoB providers were originally internal SSOs created to serve their host agencies that later morphed into third party SSOs. Some of these internal SSOs possess size and scale much larger than leading global government SSOs, and they vary widely in maturity and utilization. Given the nearly unlimited scalability of modern technology, significant over-capacity appears to exist. The government could be served more cost effectively by a smaller number of larger, more mature SSOs. An inventory of over two dozen internal SSOs and other shared services assets known to CGI is shown in Table 4 in the appendix.

A third type of SSO emerged in the 2000s: Third Party/Commercial SSOs. A few IT companies with software and services meeting stringent Federal requirements became eligible to compete with qualified Third Party/Government SSOs to provide FM and HR LoB shared services to Federal agencies. These commercial SSOs are capable of offering services and expertise leveraged from their private sector experience, and they include Accenture, CGI and IBM, as well as software providers Oracle and SAP.

OMB crafted a broadly accepted competition framework to govern competition between government and commercial SSOs for FM and HR LoB services that has avoided many of the pitfalls of the controversial and cumbersome competitive sourcing process governed by OMB Circular A-76. The LoB framework applies only to agency procurements for LoB services that subject a small number of government employees (up to 10 full time equivalent positions) to the risk of competition. Careful attention to these sensitive issues remains necessary to safeguard the rights of Federal employees while promoting the healthy competitive marketplace that is necessary to drive the full measure of benefits throughout the government.

Most of the Federal SSOs identified in this paper reflect a state of maturity in Hackett's consolidation to standardization stages. Moving them to the optimization and virtualization stages requires expertise in sophisticated management tools and technologies that is in short supply inside the government. Ensuring continuing roles for private sector partners and competitors in the Federal shared services environment will be a critical success factor for transformation.

Mixed Results and Other Challenges

Federal shared services initiatives have undoubtedly produced salutary business results, but there is very little reliable data available with which to assess them. OMB has estimated cost savings of over \$5 billion from the HR and FM LoB initiatives over a 10 year period¹⁶. The US Postal Service reports reducing the cost of its finance function by 16% to 18% and annual savings of \$50 million in HR services¹⁷. NASA reports cumulative savings to date of \$43 million¹⁸. Similar results may have occurred in other SSOs, but details are sketchy.

In 2008, the Office of Personnel Management, the sponsoring agency of the HR LoB initiative, conducted a benchmarking study that assessed the performance of the four e-Payroll centers. This study was a good start, but significantly more work is required to establish a comprehensive and robust performance management framework to enable cost and service comparisons and drive improvements across the entire Federal environment.

Customer trust is another issue that must be addressed to enable broader, voluntary adoption. Customers often view shared services as more costly and less responsive than home grown varieties, and they often raise concerns about insufficient transparency in SSO costing and pricing formulas and real or perceived cross-subsidization issues. At their heart, most customer concerns are about loss of control and reluctance to accept standardized offerings.

These common issues present continuous improvement opportunities for all government SSOs.

As noted above, shared services can enable significant transparency gains in the government business environment by eliminating a multiplicity of opaque, program-specific, non-standard transaction stovepipes and concentrating business activities within a smaller number of standardized, consolidated government-wide platforms. A more thorough examination of transparency and shared services will be the subject of a later paper.

THE NEW ADMINISTRATION'S SHARED SERVICES OPPORTUNITY

The Obama Administration has an outstanding opportunity to leverage an inherited base of substantially modernized infrastructure and best practices from the global experience to accelerate Federal shared services maturity and drive significant cost, productivity, accountability and transparency gains throughout the government. An intensive, focused effort can release substantial resources from lower-value back office work for re-investment into more urgent national needs. The following actions are recommended:

1. Create a Comprehensive Government-wide Shared Services Vision and Roadmap

The Administration should develop a comprehensive vision, strategy and roadmap to drive shared service adoption and maturity throughout the Federal Government. The plan should clearly define the desired end state and objectives linked to stages in the maturity path to be achieved along the way. The plan should set ambitious goals for:

- Agency shared services adoption, including migration of non-using agencies to SSOs
- SSO maturity, such as the use of increasingly sophisticated management practices by SSOs relative to industry best practices at each stage of the maturity path
- Improved quality, cost effectiveness and transparency of services and costs to customers, relative to best-in-industry and best-in-government standards (such standards must be developed)
- Consolidation of redundant process, technology and organizational capacity.

The end state should envision a smaller number of larger scale, multi-function third party SSOs (government and commercial) and significantly reduced numbers of internal SSOs and administrative staff throughout the government.

2. Develop a Robust Shared Services Performance Management Framework

Consolidation within the Federal environment should be driven by a fair, objective and fully transparent performance management framework. The framework should identify an appropriate number of generally accepted metrics of SSO effectiveness and enable benchmarking comparisons of Federal SSOs relative to commercial and government performers. All framework methodologies and performance data should be publically available for total customer and stakeholder visibility. The framework should promote competition so that SSO performance relative to objective standards -- and ultimately,

success in a competitive marketplace -- determines the number and scale of government SSOs required to serve the Federal environment.

3. Establish SSOs as Business-like, High Performance Organization

SSOs should be established as independent, business-like entities with explicit objectives to optimize cost and services to customer agencies while achieving realistic productivity and transparency goals. All lifecycle costs of SSO direct services, investments and overhead costs should be fully and transparently identified and charged to customers through commercial-style pricing and service level agreements that specify costs, services and non-performance penalties and allow customers to exit for non-performance. SSOs should be operated through common revolving funds -- similar to existing working capital and franchise funds -- that enable modest retained earnings for various business needs, such as accumulating investment capital for modernization.

4. Create an Office of Federal Shared Services (OFSS)

A central office should be created in the executive branch to drive this effort as a comprehensive government-wide transformation program. OFSS should be funded through revolving funds that capture all OFSS expenses for capitalization and charge-back to SSOs - similar to corporate overhead expenses in the private sector. This chargeback feature will create a market-like efficiency incentive to keep OFSS "corporate" costs to a minimum to reduce "drag" on government SSOs competing in the public-private marketplace. If the politics allow it, legislation should be proposed to divest existing SSOs from their hosts in programmatic agencies and consolidate them into OFSS. Transferring SSOs into OFSS would be controversial because it would be perceived as disruptive to existing agency operations and the Congressional committee structure; however, freeing government SSOs from host agencies where funding, staffing levels, culture and career ladders are dominated by programmatic missions is necessary to accelerate their evolution. Legislation should simultaneously consolidate the Congressional responsibilities for authorizing and funding OFSS and the entire Federal SSO environment within the respective House and Senate standing committees with jurisdiction for government administrative operations and under one appropriations subcommittee in each body. These steps are necessary to provide consistent Congressional support and resolve committee jurisdictional issues that have impeded government-wide transformation.

5. Establish a Comprehensive, Customer-Driven Governance and Accountability Environment

The plan should establish an OFSS customer board of directors to supervise shared services transformation at the government-wide policy level, and operational level customer boards for each SSO. The OFSS policy board should be chaired by the director of OFSS, and its members should include deputy secretaries/chief operating officers from cabinet-level departments. SSO-level boards should be chaired by SSO CEOs, and members should include COOs from customer agencies. Board members should be vested with supervisory responsibilities for business results and accountability comparable to commercial boards of

directors, and their personal performance incentives should be aligned with SSO business objectives to give them personal stakes in SSO success. Boards should have visibility into all SSO business activities and serve as oversight boards for SSO strategic planning and budgeting, capital planning and investments, internal controls and risk management, sourcing, customer pricing and service levels and performance management. Fully engaged, responsible and accountable boards can drive improved SSO services and performance while removing acceptance barriers at customer agencies.

6. Focus Technology Investments Strategically to Modernize the SSO Environment

A significant degree of modernization has taken place over the last two decades that can be leveraged as shared services infrastructure. Most SSOs now have modernized ERP platforms in place, but significant gaps remain in antiquated legacy infrastructure that must be upgraded to support the envisioned transformation. As shared services become consolidated into fewer, higher-power SSOs, the challenges of keeping platforms refreshed and modernized will become increasingly cost effective, lower risk, and transformational – particularly as “cloud computing” and other software-as-a-service offerings become feasible. Investments could then be concentrated surgically upon a few, rather than scattered across a large universe of smaller scale, less powerful Federal SSOs, to drive increasing technology leverage and service improvements. In addition to growing cost and productivity advantages, service benefits of increasingly modernized SSOs would include real-time visibility into all government business activities managed by SSOs readily available to any government employee, citizen or member of Congress through a variety of self-service and “on-demand” access channels.

7. Ensure a Significant Opportunity for Private Sector Investment in the Success of Federal Shared Services

The envisioned end state and road map must provide a significant, attractive and fully competitive market opportunity to attract private capital investment into the success of the Federal shared services environment. The market should envision key roles for technology and professional services firms as risk- and reward-sharing partners, suppliers and competitors to government SSOs. The competition frameworks established to guide public-private sector competitions for FM and HR LoB services are a good foundation and should be continued and expanded. Innovative public-private partnerships, such as the NHS/Steria model in the UK, should be enabled and encouraged.

Final Thoughts

An enormous amount of work is required to achieve a fully transformed, public-private Federal shared services environment. The multi-functional transformation envisioned is a long term proposition -- an order of magnitude more challenging than the landmark single function transformation of payroll that required over 20 years of sustained effort. More than anything else, this transformation will require decisive, visionary and collaborative leadership between the Executive branch and Congress – a combination rarely witnessed in government-wide management reform. Perhaps in the current economic crisis and political alignment of Washington the time has finally arrived.