

“Factory of numbers” as an alternative to the traditional finance departments

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Introduction

The concept of shared service centers (also known as “factories of numbers” for the finance function) has been common used by multinational industrial groups for a few years now. While trying to cut costs, improve quality and focus on key business, it is more efficient to integrate the back-office functions into one entity, while the operative group subsidiaries can focus on their business. The traditional solution, in which each subsidiary has its own finance, payroll and IT department is quite expensive and outsourcing to external partners bears many risks.

Is it possible to compare the processes which are provided by the finance departments to processes performed in a factory? Is it possible to transform the traditional finance departments into effective service providers acting in an organized market?

Let us have a look at the process of preparation of annual financial statements. We can state that this process cannot be compared with the serial production, however, many activities can be performed and repeated according to a certain pattern, and many of them can be defined in form of clear procedures. Booking entries in an ERP system, booking of bank operations or preparing a report in a clear defined form can be a good example. However, there are also activities which cannot be standardized as for instance the implementation of IAS/IFRS or the implementation of new local changes in law. But also the technicians have to deal with creativity...

So, if there are activities in the finance function, which are similar to the industrial activities, why not implement the industrial solutions in relation to them?

What “products” are provided by the finance department? What is their characteristics? These are for instance an invoice, which has been booked and paid

in time or a financial report, which has been prepared according to the requirements set by a client.

A product has some defined characteristics as the quality for example and there is a demand for it. The essence of industrial process is to provide products, which have this characteristics under the criterion of efficiency. The optimal level of efficiency can be reached, while trying to simplify the product, using less resources in the manufacturing process. Also some not necessary sub-activities can be eliminated from the whole process.

The production of a good named “invoice” by the finance departments begins with defining of demand (which means: defining of the product characteristics) and determining, how it will be delivered. The task is to organize a process, which makes it possible to deliver the product in an efficient and quick way. So, the persons responsible for this process should be engaged, the technology used should be determined, the level of automatization should be assured and the quality level is to be taken into consideration. The efficiency can be increased by using of economies of scale, choosing a suitable location and/or investing in additional components (i.e. IT infrastructure). And the decision should be made if the product will be delivered by an internal (insourcing: centralization or shared service center model) or an external service provider (outsourcing).

That is why it is important to determine the advantages and disadvantages of shared service center model comparing with outsourcing and centralization.

Shared service centers and the alternatives

At the end of the 70s and at the beginning of the 80s of the past century, big American industrial groups tried to cut the costs, centralizing certain processes in

the headquarters. The concept is also known as centralization, its advantages and disadvantages are listed in the table below:¹

Advantages of centralization	Disadvantages of centralization
<ul style="list-style-type: none">• cost reduction due to economies of scale,• quality-oriented concentration of certain critical functions,• concentration of certain competencies of the whole group which makes it possible to focus on expansion of the new areas of activity,• using of synergies between the business units belonging to the group	<ul style="list-style-type: none">• costs connected with the central coordination of the business units,• increase of formality due to central defined rules (bureaucracy),• lower efficiency of the service delivered by the decentralized units due to the not-necessary formalization by the headquarters,• central delivery of services, which could cheaper, quicker and better be delivered by the business units,• central delivery of services does not always match the needs of the internal and external customer,• cost increase in the case, when the services of the headquarters are also delivered by the business units (i.e. statistics, optimization of delivery)

At the end of the 80s of the past century the economic processes got a dynamics which was not met before, the same holds true for the markets. Companies tended to be closer to the customer and the market and the activity tended to be diversified. The centralization concept did not meet these needs, therefore the industrial groups decentralized the tasks performed centrally. Such solutions, as shared service centers and outsourcing got very popular for this reason.

Outsourcing is a possible form of decentralization, where external providers do some tasks for the group. When these tasks are provided by an internally

¹ Wißkirchen F., Mertens H., Der Shared Services Ansatz als neue Organisationsform von Geschäftsbereichsorganisationen [in:] Wißkirchen F., Outsourcing-Projekte erfolgreich realisieren. Strategie, Konzept, Partnerauswahl, Schäfer-Poeschel, Stuttgart 1999, p. 89

established provider and parallel an internal market within the group is established, we have to do with the shared service center concept.

The concept of outsourcing and shared service center are similar, as the planning and the control functions are provided by decentralized units. However, an external provider of certain services does not always exist. And the relations of the business units belonging to the group with the internal shared service center base on internal service level agreements, while the relations with the external providers base on client-provider contracts.

One of the strategic questions, why trying to determine “buy or make” is, if the processes or services planned to be decentralized are eligible for it? Such characteristics, as being close to key business, strategic importance and specific know-how are the factors which should be taken into consideration. Many executives tend to outsource operations, however, outsourcing of some of them can have a negative impact on the further development of the group. These are for instance processes, which are information-consuming, which are characterized by high sensitivity during the data processing (for instance, financial data), complex processes and such ones, which generate the strategic advantage.

Except of many advantages, the following disadvantages and risks of outsourcing can be identified:

- dependency on an external provider,
- lack of acceptance within the company,
- cooperation risk (the cooperation can fail),
- loss of know-how,
- increase of the distance,
- transformation costs,

- the service should be eligible to be measured, quantified,
- personnel problems during the process of change.²

The shared service center concept was established in the 90s of the past century as an alternative for centralization and decentralization in form of outsourcing.

Shared services incorporate the best characteristics of centralization and decentralization. The strengths taken from decentralization are as follows: local control and knowledge about the local circumstances. The strengths taken from centralization are: economies of scale and know how concentration. Except of that, the shared service center concept has the following advantages³:

- customer focus,
- service delivered as the key business,
- responsibility for costs and quality,
- independency on the headquarters,
- synergies,
- thin organization,
- geographical independency (greenfield).

As the risks and disadvantages of the shared service center concept the authors: Wißkirchen i Mertens⁴ identify the following ones:

- personnel (different cultures, languages, fears of employees regarding losing the jobs, power, change of company location, control function by the shared service center),

² Ibidem, p. 81

³ Bangemann T., Gehen die Lichter aus im Rechnungswesen? Shared Services als Back-Office der Zukunft [in:] Trends im Rechnungswesen, Management Circle, Wiesbaden 2003

⁴ Wißkirchen F., Mertens H., Der Shared Services Ansatz als neue Organisationsform von Geschäftsbereichsorganisationen [in:] Wißkirchen F., Outsourcing-Projekte erfolgreich realisieren. Strategie, Konzept, Partnerauswahl, Schäfer-Poeschel, Stuttgart 1999, p. 93

- processes (some local processes are incompatible and not standardized),
- technologies (some local technologies are incompatible and it is impossible to combine them with other technologies),
- organization (different legal circumstances).

However, the above mentioned weaknesses and risks can be reduced⁵ if during the implementation of the shared service solution the following success factors are taken into consideration:

- consistent vision, objectives and strategy in all geographical locations,
- moving the vision into the organization,
- key role of the top management,
- global perspective regarding the shared service center,
- suitable investment in the change management and the IT infrastructure and other modern technical solutions.

According to a Deloitte study (2003), the typical functions performed by shared service centers are the following ones:

- bookkeeping (asset accounting, accounts receivable, accounts payable, payment, general ledger),
- travel costs accounting,
- payroll,
- reporting and analyses,
- procurement,
- tax,
- treasury.

⁵ Ibidem, p. 94

Literature

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