ENTERPRISE MANAGEMENT

The rise of shared service centres and outsourcing is changing the face of the accounting profession. **Alan Marsden** discusses the key issues.

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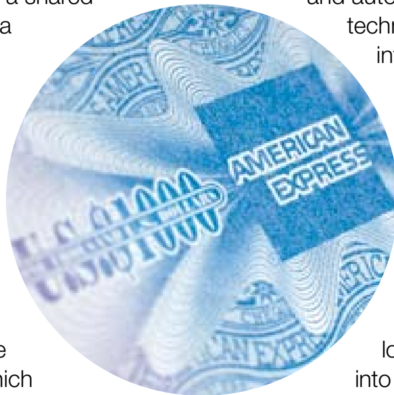
If you glance through the results of recent surveys about the finance function, it's easy to conclude that the profession is in a state of flux. Research reports with titles such as "Brave new world" and "Transforming the finance function" are common.

It's clear from the findings that finance directors are understandably concerned about how they can keep their businesses going through the most serious recession since the Thirties. But a closer analysis reveals a deeper-rooted sense of unease among accountants about their profession's changing circumstances.

Some of the challenges they face stem from incidents such as the Enron and WorldCom scandals in 2001, which resulted in the enactment of strict compliance laws in the US. But others are more long-standing, having arisen from changes in business that began in the late 20th century. They stem primarily from technological innovations, globalisation and the resultant increase in competition. These trends will continue to exert pressure on companies – and on the way the finance function works – for many years to come.

As all finance professionals are aware, advances in IT have provided a range of tools to aid the collection, storage, manipulation, analysis, interpretation and communication of the data that's the raw material of their craft. Financial software packages have substantially improved the efficiency and effectiveness of accountants by removing much of the toil of their everyday tasks. But perhaps more significant for the future of accounting has been the development of enterprise resource planning (ERP) software to the point at which all functions can be integrated into one system. Although many firms are still using older labour-intensive ERP systems that still force accountants to use spreadsheets offline for analysis, the latest packages offer a single database that contains all data for the various software modules that typically address each functional area, including finance. These

innovations have enabled large multi-divisional organisations to centralise their finance function, possibly from operating units around the world, into a shared service centre (SSC). Such a centre operates to a set of rules that ensure consistency in the methods applied across the organisation, resulting in a constant standard of output.



The advantages of SSCs are summarised in a CIMA technical briefing, "Contracting out the finance function" (August 2001), which argues that centralisation offers both financial and non-financial benefits. These include:

- Economies of scale that enable the organisation to cut posts and so reduce its employment costs.
- The potential to locate an SSC in an area where labour costs are low.
- Savings on the cost of premises and associated outgoings on insurance, security and legal fees.
- The ability to achieve tax savings by moving more profits to a low-tax regime.
- The consolidation of the various disparate systems used by different business units.
- The ability to cater for the company's growth in a cost-effective way, because any acquisition, new product or service can be handled by the SSC with only a marginal increase in resources.
- Quality improvements arising from a dedicated SSC pursuing a more professional supplier-client relationship.
- The ability to measure SSC processes and standardise them via internal benchmarking.

The number of SSCs continues to grow: half of all respondents to CIMA's ongoing survey last year claimed to work in an organisation that used such a centre.

Recent studies have assessed the impact of SSCs on efficiency and effectiveness. Research by the Hackett Group in 2006, for example, found a steady reduction in companies' finance and accounts costs as a percentage of turnover since the early Nineties. The top-performing respondents cut their costs by 60 per cent. They achieved such efficiency gains through process improvement (simplification, standardisation and automation), greater use of technology (ERP and business intelligence systems) and economies of scale, whether their SSCs were in-house or outsourced.

American Express provides a useful example of an SSC implementation. The company rationalised its financial activities from 46 locations around the world into three SSCs with the objective of achieving cost savings, economies of scale and improvements in quality. Two years later it was able to close one of these centres because the other two had become so efficient.

Although SSCs have proved their value, setting one up can entail considerable effort and expense. This is particularly true where the centre is to be located abroad, because different legislation, tax rules and financial reporting requirements – not to mention the cultural, linguistic and currency management issues – must be taken into account.

An alternative to the SSC approach is the arrangement known as contracting out or business process outsourcing. Both terms refer to the act of procuring a product or service from a third party in accordance with terms that are legally enforceable. This involves a considered decision to entrust internal functions to an external supplier. The reasons for entering an outsourcing arrangement overlap with those for setting up a SSC, but they do differ in some key respects.

One of the main reasons for using outsourcing and SSCs is to save costs. In the case of outsourcing, the saving on direct labour costs can be substantial, especially if the service is located in another country ("offshored") where employment costs are significantly lower. Where the outsourcing supplier has many customers and a large operation, the client could benefit from the reduced costs associated with the supplier's economies of scale. It may also be able to obtain a service of a higher quality than could be achieved in-house because the supplier has the ability to attract specialist expertise.

The second main reason for outsourcing is that it allows the organisation – particularly the finance function – to focus on its core activities. For finance, much of the routine work involved in transaction processing can be outsourced, but the analysis and interpretation of data for decision-making is seen as central to the organisation, requiring a deep knowledge of the business.

As with any function, the outsourcing of finance has drawbacks as well as advantages. The main ones include:

- A loss of control arising from the reliance on a third party to provide the service.
- A loss of expertise arising from the lack of an in-house finance function.
- A threat to confidentiality.
- A risk that the service provided will be of unsatisfactory quality.

All of these issues need to be addressed whenever a service is outsourced, so it's particularly important to draw up a watertight service-level agreement.

The challenge that such developments pose to the finance profession is that a substantial proportion of what was traditionally the work of accountants is now being done in large "factory processing units" employing hundreds of people. While there is no question that they are qualified to do the work, there's a risk that a division of labour will open up between the accountants who are involved in routine processing and those who take the chance to assume the role of "business partner".

Leaders in the finance field see the transformation in the profession wrought by technological innovation and globalisation as an opportunity for finance and accounting professionals to move up from the routine tasks of transaction processing to assume a business partnering role in which they will use their finance and accounting expertise to help managers at both strategic and operational level make and implement decisions. But the changes represent threats as well as opportunities. It has been argued that, unless finance professionals actively promote the business partnership role, they are unlikely to fulfil their potential and their organisations may suffer as a result.

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The role of business partner has always existed. Many FDs have assumed it partly because they have developed a good understanding of their organisation and are able to contribute to strategic decision-making. But structural changes in many organisations have meant that the typical finance professional is no longer a member of a relatively small team providing and interpreting data for the company in which they are embedded. They are increasingly employed in an SSC or an outsourced processing centre that may employ hundreds of people. When financial professionals are physically and socially remote from their non-financial colleagues, the mutual learning that once occurred between accountants and their colleagues in marketing, sales, HR etc is far less likely to take place.

Organisations and professional bodies have responded to these new structural arrangements by formalising the development of the previously informal role of business partner. CIMA, for example, is committed to ensuring that its members understand the managerial aspects of business, while several leading organisations – eg, Unilever and Kimberly-Clark – have set procedures in place to develop their financial professionals into future business partners.

To date there is no clear "best practice" model for the finance business partner, but a meeting of the CIMA Improving Decision-Making in Business Forum last year made the following observations:

- SSCs, including outsourced centres, can offer reporting and analysis services that would otherwise have been provided by a business partner.
- Most business partners are embedded in the business and provide tactical financial support – for example with budgets, planning and analysis – to line managers. Some of this support can now be provided by SSCs.
- Some business partners are more definitely expert members of the finance function, reporting directly to the finance director. These may provide business partnering in specialist areas such as risk management or mergers and acquisitions, or they may be strategic business partners who support the group FD.
- Only a select few finance people who are embedded in the organisation can combine the business understanding and working relationships gained through their proximity to non-financial colleagues with strategic thinking to provide leadership. The forum regards these as true business partners. They can challenge line managers as sparring partners.

Despite the debate about the business partner role, the early findings of independent research commissioned by CIMA suggest that most organisations have yet to develop a more strategic role for finance. Although there is evidence to show that some accountants are assuming a more business-orientated role, many are occupied mainly by transactional accounting and financial reporting.

"Having introduced SSCs, we still have about 800 finance managers, but only 100 of these could be considered strategic business partners," reported one member of the forum. "Many of the rest may not have the aptitude to develop the broader soft and business skills to complement their core financial skills. Even those that do have these qualities may find that their core financial skills will not suffice for the form of quantitative analysis often required to support decision-making."

If this example is typical, it suggests that all those organisations involved in training and developing accountants must make a concerted effort if these professionals are to realise their full potential.

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E2 further reading

A Norton and J Hughes, *The Official CIMA Learning System – Enterprise Management*, CIMA Publishing, 2009.

The CIMA Improving Decision-Making in Business Forum, "Improving decision-making in organisations: the opportunity to reinvent finance business partners", CIMA, July 2009.

Exam practice

Try the following question to test your understanding. The solution will appear in CIMA's student e-magazine, *Velocity* (www.cimaglobal.com/velocity).

CB, a western European company that had established global leadership in electronic transmission technologies in the late Nineties, began a rapid expansion programme that targeted markets in the US, Latin America and Asia. Having pursued joint ventures and acquisitions involving 18 different companies, CB found itself with multiple finance reporting units and finance directors in each of the 43 countries in which it operated. Faced with IT duplication and complexity, the senior management team realised that CB's finance and accounting department was not aiding profitable growth and needed to be standardised.

In 2009 CB addressed the question of how best to restructure the finance function across the organisation. One option was to outsource routine finance activities to a third-party supplier and the other was to establish a centralised shared service centre, which, although it would be expensive and time-consuming to set up, would allow the company to retain greater control of its own operations. Whichever alternative was chosen, the implications for the members of CB's finance department would be significant.

You are required to:

(a) Discuss the merits and drawbacks of outsourcing CB's finance function to a third party compared with those of setting up and centralising the function in a dedicated shared service centre (*15 marks*).

(b) Explain the implications for the employees working in CB's finance department if (i) the function were to be outsourced and (ii) the function were to be restructured so that its tasks were performed centrally in a shared service centre (*ten marks*).