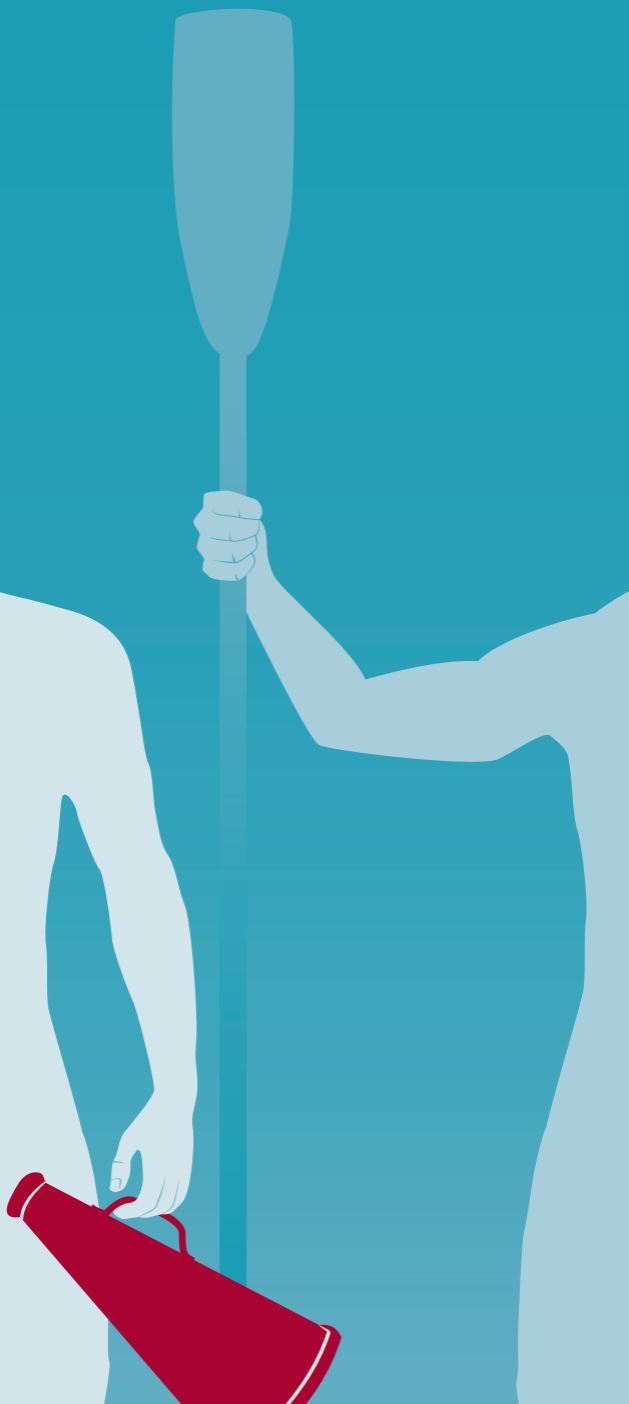




Stern Stewart & Co.

LEAN

SERVICES & ORGANIZATION –
THE CONSISTENT SEPARATION OF
SERVICE AND MANAGEMENT





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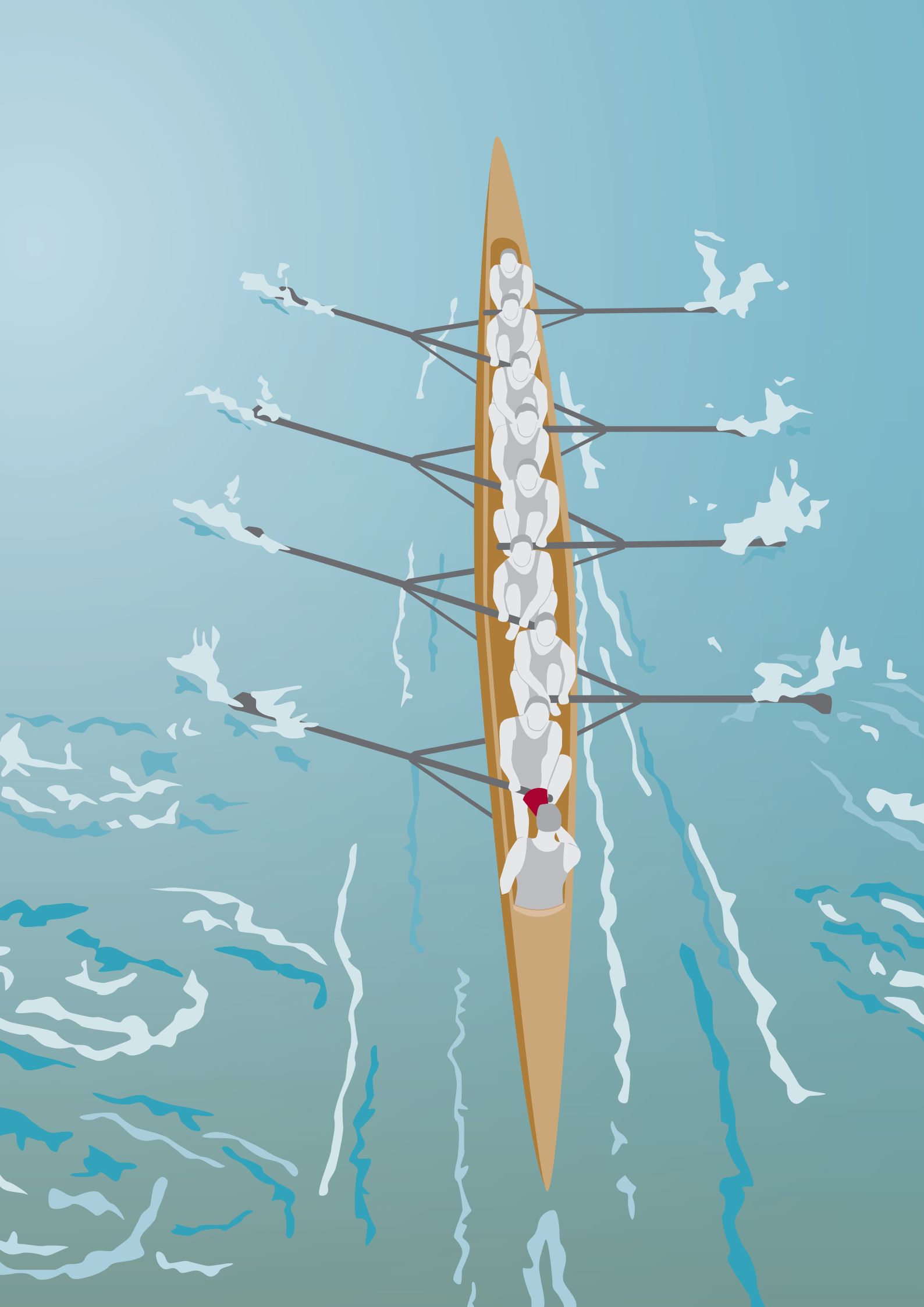
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Gerhard Nennung, Stefan Heppelmann

Management Summary

Originating with Toyota, the term “lean management” has become synonymous with efficiently organized production processes in all industries. With respect to the services of an organization, however, this approach is not widespread. Wrongly so. For while “lean” in the area of manufacturing has increased both productivity and the quality of the output, even in well-established organizations, the service functions are frequently only a third as productive, at best.

The reason is often the incorrect definition of roles and responsibilities inherent in the functions – producing a negative effect on dimensioning and output. Take Accounting and Finance for instance: It is not uncommon today to have most of their functions positioned as a “shared service.” Regardless of how effectively the shared service center actually is (capacity management, process design, quality, etc.); everything that typically remains in the holding company is not adequately scrutinized. Probably only a small share of 10-20% is actually officially handled, while the rest consists of expert services that have no place in a “Corporate Center” with its claim to leadership. On the contrary: this combination ensures that the function neither serves nor manages properly – thus not playing its role effectively. Three rules should be adhered to in order to establish organizations and services that are “lean”, in the best sense of the term, i.e., highly productive:

1. The holding company should focus on supervisory functions – thereby becoming sleeker (and at the same time stronger) 2. Based on this, the relationship between the holding company and the strategic business units should be designed to enable the latter to assume entrepreneurial responsibility with “top down” delegation of supervisory processes. **3. Expertise-driven functions should be bundled across all levels and converted into a critical mass with specialized know-how through the creation of so-called ‘Centers of Excellence’.**

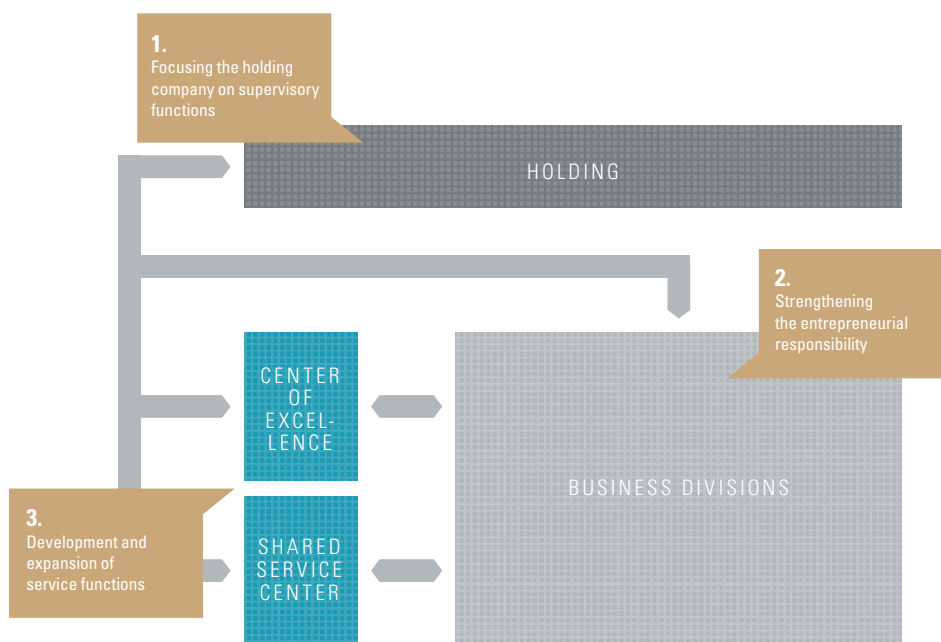


On the Do's and Don'ts of organizational design

First of all: There is no right or wrong organization – even the discussion of whether it is a financial, strategic, management or operational holding company falls short. Instead, the following key questions must be addressed when designing the organization:

- What tasks are to be performed by the holding company? Basically, the following applies: A variety of functions or a large workforce are not synonymous with a productive, efficient holding company. On the contrary: policemen often work as waiters, as a sideline.
- How is the entrepreneurial role of businesses divisions strengthened? Please note: strong business divisions require functioning corporate governance as well as a clearly defined allocation of responsibilities among the holding company and business division.
- How is expertise specifically acquired and a culture of service promoted? Important: It is only when the right management signals are triggered on the demand side and on the service side that waiters become waiters with heart and soul.

In the “lean” organization, enabling a thorough absorption of specialized resources into selected areas ensures not only a powerful holding company, but also the creation of latitude for “entrepreneurial” business divisions and high service quality. Thereby, three design rules apply:



*CONCEPTUAL OBJECTIVE
OF THE “LEAN”
ORGANIZATION*

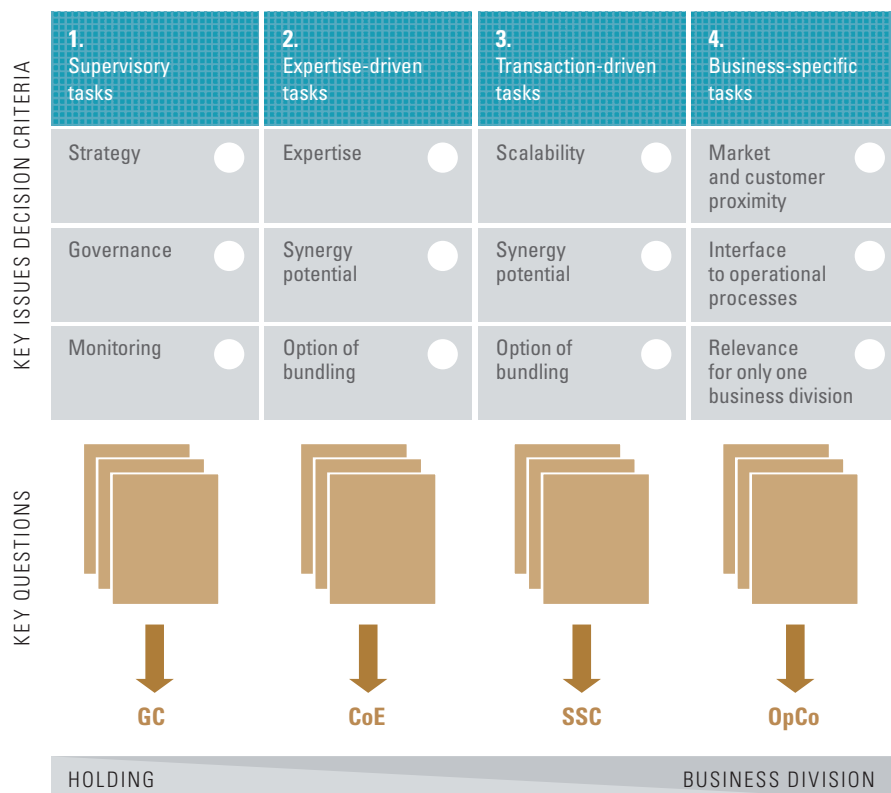
Rule 1: Lean and strong – Reducing the holding company to supervisory functions

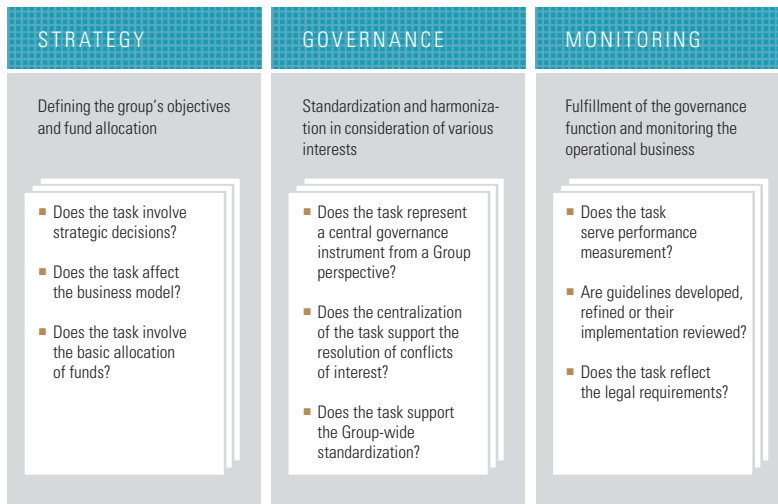
There is no room for service functions in the holding company of a “lean” organization. Therefore, the strict separation of supervisory and service-oriented tasks is the basis for a holding company that is as lean as it is “mean”.

Three criteria characterize supervisory tasks / responsibilities:

1. The task is necessary for the achievement of corporate goals and strategy
2. The task is necessary in order to channel conflicts of interest in terms of corporate governance
3. The task is required from a regulatory perspective, or used for monitoring purposes.

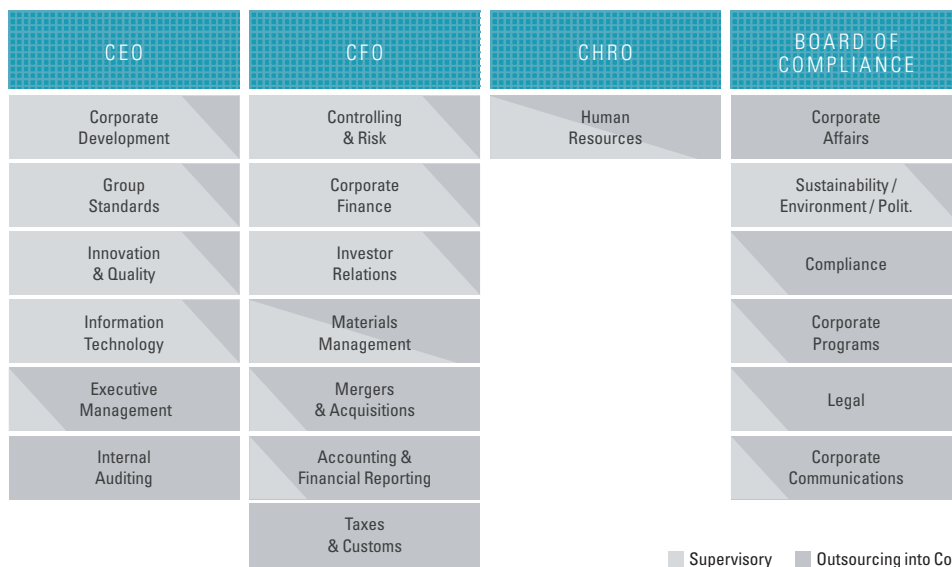
TASK TYPES AND ORGANIZATIONAL INTEGRATION





SUPERVISORY TASKS OF THE HOLDING COMPANY

Typically, the task analysis and the subsequent analysis-based activity split will result, on one hand, in holding company functions that were previously, and to a large extent, will continue to be supervisory (e.g., Corporate Development). On the other hand, it also identifies departments that have no real supervisory function and therefore should not reside in the holding company (e.g., Legal). Furthermore, when considering individual tasks, potential for merging individual departments often becomes apparent.



TYPICAL RESULTS OF THE TASK ANALYSIS

Based on this, the following is important for structuring the future organization: blueprints for de-emotionalizing the decision among various design options. Otherwise, the discussion will become highly perspective-specific, especially in terms of structure, roles, areas of responsibility and function interfaces.

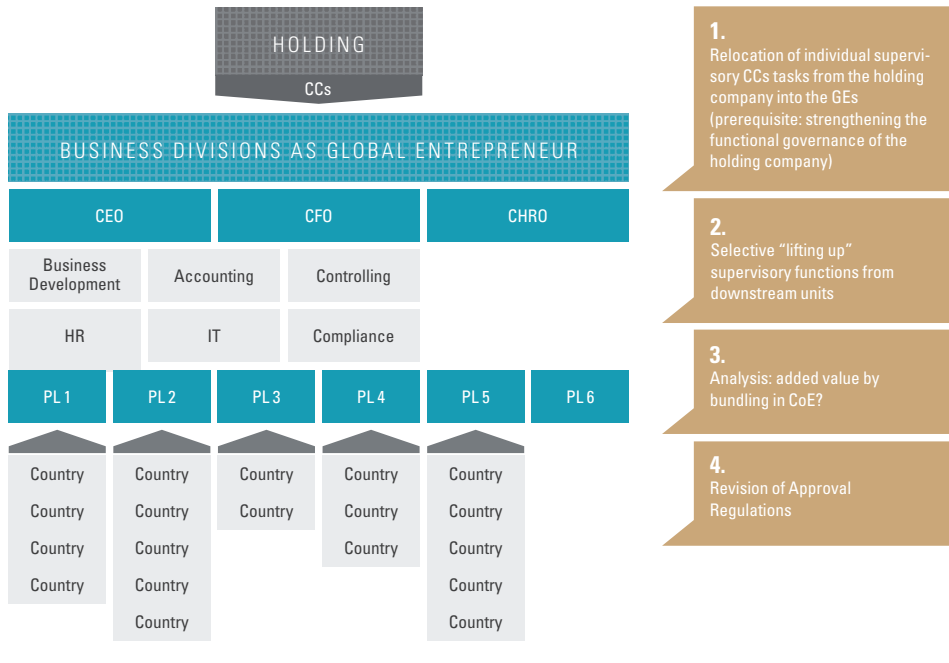
By streamlining the holding company, savings in the mid-double-digit percent range are generally possible. In order to simultaneously increase the impact rate, focusing on value-creating activities is essential. Even well-designed companies currently apply this no more than 40% of the time. A first lever for avoiding waste is to review the performance spectrum. For example, the finance function: What level of granularity and which reports are actually necessary? Other starting points may be found in the processes within departments, e.g., in the form of a reduction of the coordination / monitoring by strengthening the individual's responsibility for quality. Additional potential that can be tapped through regular, institutionalized exchange is typically found in the area of cooperation across departments of the holding company and between the holding company and other units.

In summary, the design of the "lean" group management model represents a new, more powerful layout of the holding company and the optimization of the structural costs. In general, the number of truly supervisory departments can be substantially reduced. The holding unit no longer executes tasks of a service or consultative nature. In short, the holding unit is no longer defined by "requests", but rather by "announcements".

Rule 2: The Rediscovery of Subsidiarity – Empowerment of Business Units to Become "global entrepreneurs"

These are the business units that expand and secure the company's position as a global group. In the "lean" organization, the units play a major role – of course within the framework of the reinforced functional governance of the holding company. Therefore, the business units must be equipped in a manner that allows them to always act flexibly and entrepreneurially as "global groups".

Accordingly, the "lean" organization is designed in terms of the concept of subsidiarity: Tasks, actions, and problem solving should be undertaken independently and autonomously within the business units to the extent possible. Selected supervisory functions should thus be moved out of the holding company; in this process the basic condition applies that there cannot be any substantive duplication or identical tasks on different levels.



LEVER FOR STRENGTHENING THE BUSINESS DIVISIONS

Another approach to the development of the role of business units consists in "lifting up" supervisory functions from downstream units. If there are knowledge-based tasks that cannot add value by their aggregation in the Center of Excellence, then their continued performance within the business units is an option.

Not only the tasks, but also the organizational structure of the business units should be aligned to the entrepreneurial role. In this context, the CEO principle in particular, has proven to be effective. According to this principle, a CFO supports the CEO – in theory complemented by a CHRO. Typically, the overhead of the business division is completed through the Business Development, Controlling, HR, Accounting and IT divisions. However, according to the leitmotif of a lean organization, the majority of the operational resources resides in the Shared Service Center or in the Center of Excellence.

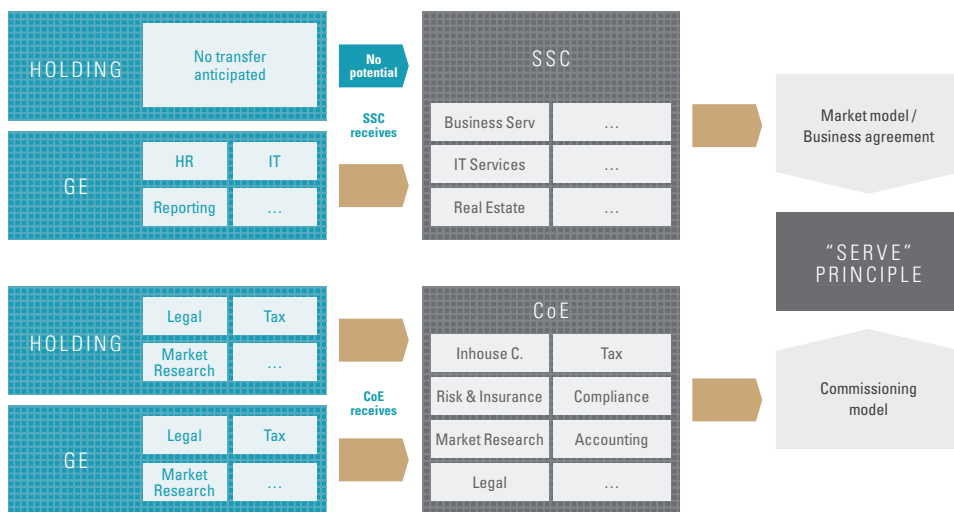
An example of the strengthening of corporate responsibility in the business units is the "financial organization with strong functional and disciplinary guidance and reporting line." Formerly, an investment proposal was first assessed in the business division and subsequently a second time in the holding company. Not only are the redundancies obvious – the practice also promoted mistrust and absolved the controlling of the business of ultimate responsibility. Well-designed companies solve the problem this way: The CFO of the division reports in both discipline-related and business terms directly to the Group CFO. Therefore, the latter has direct control over the investment controlling the business division – and thus requires no separate department for this.

Rule 3: The aggregation of expertise – implementation of “lean” in expert Divisions

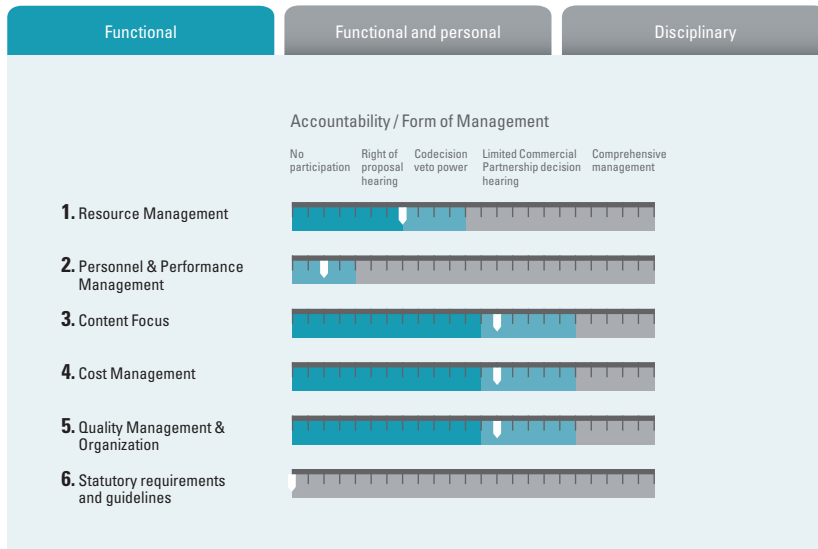
The dominant guidelines for “lean” services are synergies and functional excellence – and thus the counterpart of impact and efficiency, which are paramount at the holding company.

The guidelines are initially implemented with the expansion of shared service centers around the transactional tasks that have been outsourced from the holding company and the business units. In the expertise-driven service functions, however, a change in philosophy occurs: Instead of offering the services from the holding company as previously, the “lean” organization now aggregates the tasks in a Center of Excellence. The aim is the commitment and creation of highly specialized expertise through sharing of resources and expertise. In addition, achieving a critical mass of demand ensures the efficient use of expert knowledge.

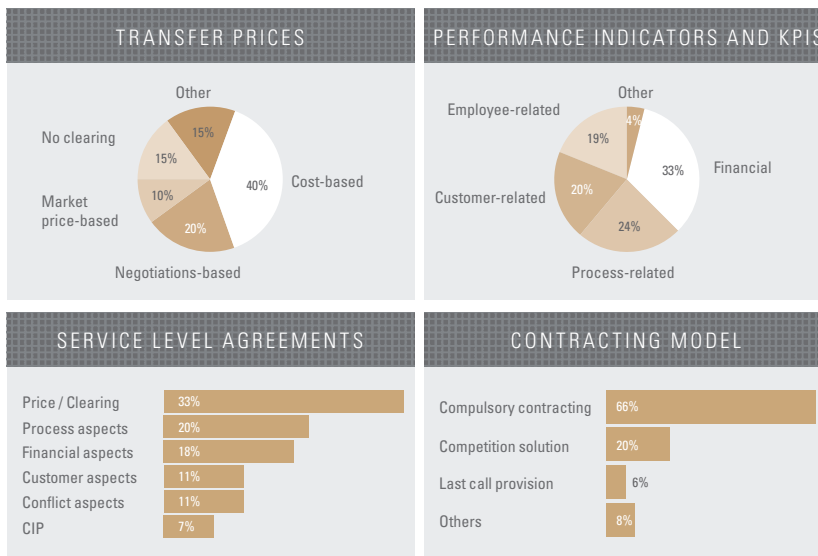
CONTRACT MODEL FOR SERVICE FEATURES



However, it is only the appropriate management and contract models that set the course for an optimal interaction of service providers, holding company and business units. In this regards, the solution latitude of management models is far more sophisticated than [merely] the professional and disciplinary characteristics. That notwithstanding, in the “lean” organization the scope of action is clearly defined: At least in terms of clear functional governance, the manager of the Center of Excellence reports to the holding company via a “solid line”. Moreover, in the management of the Center of Excellence the “cost-efficient quality” within the given budget is paramount – as opposed to the Shared Service Center, whose objectives are maximum process efficiency and low list price.



EXAMPLE: STANDARDIZED MANAGEMENT MODELS AND DESIGN OPTIONS



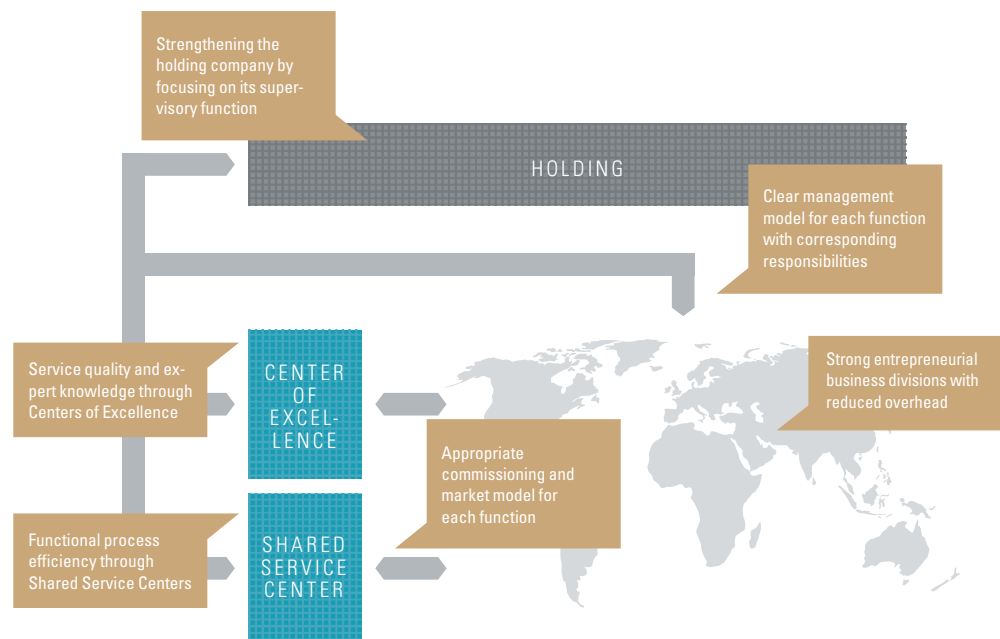
The transition to the Center of Excellence is a key step towards achieving significant cost reductions and quality improvements in overhead functions. These go hand in hand with a mental paradigm shift: The waiters become waiters with their heart and soul and are no longer police officers as a sideline.

Summary

“Lean” Services, “lean” organization – in simple terms: The consistent separation of service and management.

To truly enhance productivity and output quality, the following levers must be applied along the three design principles, when configuring the “lean” organization: First, the holding company must be strengthened by focusing squarely on supervisory tasks. The business units must be clearly distinguished from the holding company; they must be structurally empowered to fill their role as “global entrepreneurs.” In supporting functions, the building of centers of excellence enhances the quality of service and strengthens the consolidation of expert knowledge. At the same time, the extension/roll-out of shared services promotes a rise in process efficiency. Finally, appropriate management and governance systems must be developed to ensure the optimum interaction of holding company, business units and service functions.

MODEL ROLES OF THE “LEAN” ORGANIZATION



Consistently implemented, the following features characterize a “lean” organization:

1. The holding company is no longer defined by “requests” but rather by “announcements”.
2. The business units can act as “global entrepreneurs”.
3. The support functions turn into service providers, dedicated with heart and soul.

Stern Stewart & Co.

Stern Stewart & Co. is an independent strategy consulting boutique. Our consulting focus is on the key management issues. This includes strategy and corporate finance, as well as organization and performance management. We see the company's management as a strategic investor in the business and support them to increase the value of their company.



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