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To share or not to share?

Delivering corporate services in 21st century government

by Thomas Elston

Policy recommendations

Sharing corporate services between different organisations should reduce costs and improve quality. But too much sharing can cause problems with coordination, centralisation and overregulation.

- When comparing reform options, consider the costs of consuming corporate services as well as the costs of producing them.
- Adopt a discriminate approach, sharing data-light services but keeping data-heavy services in-house or in small-scale partnerships.
- Ensure that agencies using shared services can influence their design and delivery.

Introduction

Faced with declining budgets and rising demand for services, many governments are looking to improve efficiency and effectiveness by redesigning organisational structures and processes. Much attention has been on corporate support services, like finance, procurement, legal and HR. These play a vital enabling role in the delivery of public policies, and are often provided close to the frontline. But is this the best strategy?

Is it really necessary for individual agencies to produce their own corporate services? What are the benefits of reducing this duplication and sharing common activities between organisations? And do these benefits outweigh the costs, in terms of less local control and less tailoring to specific needs?

This memo addresses these questions. It argues that there are pros and cons to both in-house and shared corporate services, and that governments should strike a balance between the two.

What are corporate services?

Corporate services are those administrative and professional functions that are found in most organisations, irrespective of sector or mission. They support the organisation in delivering its primary purpose – for example, by recruiting personnel, purchasing goods and services, or providing analysis and advice.

Finance, procurement, human resources, information technology, estates, legal services and internal audit are all examples of corporate services. Often, they overlap with one another and vary in complexity. For instance, financial services include payroll and invoicing, which are standardised, IT-driven tasks, as well as data analysis, forecasting and reporting.

Different corporate services are of greater or lesser consequence in different organisations. For example, where there is a large case processing operation, as in a tax authority or social security agency, information technology will be much more prominent than in an ordinary policy-making office.

Moreover, some corporate services require that providers have intimate knowledge of an organisation and its operating environment in order to deliver high-quality support, while others are more-or-less standardised across organisations. The former are 'data-heavy' services, involving on-going dialogue between service providers and service consumers (e.g. IT specialists and frontline managers). The latter are 'data-light' services, requiring minimal day-to-day engagement.

Why do corporate services matter?

Corporate services influence the efficiency, effectiveness and legitimacy of government.

Efficiency. Corporate services use resources that might otherwise go direct to the frontline. But efficiency is difficult to measure. Unit costs of production and the ratio of administrative to frontline staff are commonly used indicators, but these are problematic if they assume no variation in service quality. Moreover, lower unit costs do not automatically increase efficiency, since the burden of activity might simply have shifted 'off-the-books'. For instance, when employees process their own expense claims electronically, rather than sending them to a dedicated finance team, the unit cost of production will appear lower even if the total resource expended by the organisation on expense processing is constant.

Effectiveness. Corporate services also influence policy outcomes. In any organisation, error or delay in the provision of advice, resources or personnel is detrimental, but so is their mismatch with organisational need (see Box 1). Equipment that is adequate in some parts of government may be unusable in others. Procedures that help one agency might hinder another. Therefore, effective government requires corporate services to be usable and useful across a wide range of policy environments.

Legitimacy. Finally, administrative corruption undermines confidence in government and reduces the legitimacy of its policies. This explains why processes for awarding contracts and appointing personnel are often heavily regulated in the public sector.

In summary, high-performing corporate services are not simply those with the lowest unit costs or the highest technical capability, as important as these criteria are. They must also meet the needs of a diverse range of organisations, and promote the legitimacy of government.

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To share or not to share? In-house vs. shared services

Traditionally, the two methods for delivering corporate services were in-house provision and shared services (sometimes called 'central services' or 'functional organisation'). Over time, government and industry have switched between these two approaches as their various costs and benefits have become apparent.

In-house corporate services

In-house provision involves a single organisation or organisational division producing its own corporate support functions. The main advantage is that a single authority has ultimate control over all the resources required to deliver the organisation's outputs. Services are designed to meet specific requirements, delivered to particular timetables, and resourced flexibly according to changing local priorities. Service providers have an intimate understanding of needs, risks and long-term strategy in the organisation, and liaise closely with frontline managers to develop best-fit solutions. External accountability is also clearer, since executives cannot blame third parties for resourcing problems that adversely affect the organisation's performance.

In-house corporate services became increasingly popular in government agencies after the 1980s, as reformers sought to decentralise resources to local cost centres and hold managers more directly accountable for performance.[1] But this brought challenges as well as benefits. In particular, in-house services are often more expensive to produce, since lower volumes of activity have higher unit costs. Strategic investment in new technologies and expertise is also more difficult when service demand is low, and the burden of meeting public sector regulations is greater. Finally, the additional responsibility of local corporate service delivery can be an unwelcome distraction for managers facing the many pressures of frontline policy delivery.

Shared corporate services

As an alternative to in-house provision, shared services historically involved the production and distribution of resources to a range of organisations or organisational divisions from a central authority, such as a finance ministry or the headquarters of a private sector conglomerate. But today, other options are available. One is to create a joint venture, where groups of agencies pool their resources and operate the service provider collaboratively – a strategy

[1] Peters, B. G. (1996). *The Future of Governing: Four Emerging Models*. University Press of Kansas

that is increasingly popular in local government. Another is to outsource functions to a specialist firm.

Whichever method is chosen, the aim is to address the key challenges of in-house corporate services. Specifically, higher volumes of activity enable scale economies, increased professionalisation and reduced barriers to investment. But alongside these benefits are a series of new problems that weaken the relative advantages of the shared services approach. Three are outlined below:

1. *Coordination problems*. When organisations depend on third parties for necessary resources and advice, coordinating internal activities becomes more difficult. Managers rely on external teams with limited knowledge of, and interest in, the needs of a particular operating environment. Shared service providers have to satisfy multiple user agencies with competing demands. Over time, accumulated delays and compromises can undermine goal attainment within individual organisations, prompting a return to in-house provision, at least for business-critical services.

2. *Centralisation problems*. Organisations that share services must align their internal processes and agree to common service standards. Historically, this involved central authorities determining lowest-common-denominator specifications. Unfortunately, because the information available to any decision-maker is partial and biased, this can prove dysfunctional.[2] Operational issues and interdependencies might be unknown centrally, or underestimated. A compromise that appears tolerable to most stakeholders may damage a minority. As these problems accumulate, the local control afforded by in-house corporate services again becomes attractive.

3. *Overregulation*. Finally, the high level of standardisation required to operate large-scale shared services can prove challenging. When organisations face external conditions of change and uncertainty, standardised management processes impede responsiveness and innovation.[3] Again, this makes the freedom and flexibility of in-house corporate services more attractive.

Three recommendations

Given that there are advantages and disadvantages to both the in-house and shared service models, how can governments optimise their corporate service delivery? Three recommendations are made below:

1. Recognise consumption costs as well as production costs

The first recommendation is to develop more complete business cases before embarking upon corporate service reform. This means accounting for both the costs of producing corporate services and the costs of consuming them.

Shared services can reduce production costs by harnessing economies of scale. But the increased distance between service users and service providers risks inflating consumption costs. Conversely, in-house corporate services generally have lower consumption costs due to user-provider intimacy, but higher production costs because of the lack of scale.

Reform business cases that don't directly confront this trade-off risk over estimating the benefits of shared services. Ultimately, a service that is cheaper to produce but more difficult to use or less fit-for-purpose will not increase organisational efficiency.

Box 1: Corporate service reforms in Minnesota[4]

Centralized corporate services were long used in the Minnesota State Government, with different state agencies drawing on the same central supplier. However, in the 1980s, concern grew that this was impeding the efficiency and effectiveness of government.

Procurement was run centrally in order to secure bulk-buy efficiencies, but this caused delays or compromises to specifications, and sometimes led to the cancelation of frontline programmes. Recruitment processes were slow and inflexible, and central service providers were more concerned with meeting central targets and regulations than with facilitating and enhancing policy delivery at the frontline.

The solution involved a combination of changes to accountability structures and resource decentralization. Some services were retained centrally, with providers being made more directly accountable to users through performance management and pay-by-use techniques. For others, agencies were empowered to choose from a range of providers, including themselves, on the basis of whose services best met local cost and quality requirements.

Both efficiency and user satisfaction improved significantly following these reforms.

[2] Lindblom, C. (1965). *The Intelligence of Democracy*. Free Press.
[3] Burns, T., & Stalker, G. M. (1961). *The Management of Innovation*. Tavistock.
[4] Barzelay, M. (1992). *Breaking Through Bureaucracy*. University of California Press

2. Adopt a discriminate approach, sharing data-light services and keeping data-heavy services in-house or in small-scale partnerships

The second recommendation is to adopt a discriminate approach to corporate service delivery, rather than one based solely on either the shared or in-house models.

Data-light services require little contextual information to deliver effective support to organisations, and thus involve minimal user-provider dialogue. Consumption costs will generally be lower for these services, meaning that they can more readily be shared between large numbers of organisations. For instance, standardised finance functions, like payroll, invoicing and basic procurement, are often provided to numerous agencies.

Conversely, services like financial modelling, complex estate planning and strategic procurement require more extensive user-provider engagement. They are 'data-heavy', and will likely have higher consumption costs. In these cases, in-house provision will sometimes be most appropriate. However, it might also be possible to share such data-heavy activities within a small joint venture or consortium. This can deliver some of the cost and capability benefits of large-scale production, but without creating too much distance between users and providers in such a way that consumption cost inflation exceeds production cost reductions.

3. Empower corporate service users

Finally, from wherever services are provided, it is essential that they are fit-for-purpose and add value to government operations in diverse environments. This means resisting the temptation for central authorities to determine unilaterally what services will be provided to agencies and what their specification will be. Instead, to minimise problems of coordination, centralisation and overregulation, corporate service providers should be accountable to frontline agencies, where operational knowledge is concentrated.

To this end, user agencies might participate in customer insight forums, or select their provider from a marketplace based on competitive tendering. Those agencies party to a shared services joint venture can influence the provider through management meetings. Others might adopt a 'business partnering' approach, where provider staff are co-located in user agencies as an aid to communication and mutual understanding.

Box 1 describes a successful case of corporate service reform in the United States. This combined a discriminate approach to service provision with an emphasis on provider accountability. It came to be nationally recognised as delivering significant benefits to government efficiency and effectiveness.

Conclusion

The basic idea behind the shared services approach is very attractive. Advocates promise more efficient government without adverse consequences for frontline policy delivery. But the message in this policy memo is more cautionary: over-adoption is just as risky as no adoption.

Governments should therefore be discriminating when selecting services to be shared between organisations, and should build reforms that empower rather than constrain corporate service users. Together, this approach might not have the appeal of a 'big bang' reform, but it is likely to manage the risks of poor coordination, centralisation and overregulation that service sharing brings.

About the author

Dr Thomas Elston is a Postdoctoral Research Fellow at the Blavatnik School of Government. He holds a three-year research fellowship from the Leverhulme Trust to examine whether modernisation can assuage the traditional dilemmas of administrative centralization.

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