Sharing services, saving money?
Five risks to cost saving when organizations share administrative services

Dr. Thomas Elston,
Postdoctoral Research Fellow

(Drawing on research with Dr. Muiris MacCarthaigh, Queens University Belfast)
Outline

• Shared services in government
• Mixed experience to date
• **Five risks to cost saving** identified by organization theory and political science
  – 1. Escalating start-up costs
  – 2. Increased transaction costs
  – 3. Reduced service quality
  – 4. Functional duplication
  – 5. Opportunity costs
• Lessons – what can be done?
Shared services in government

• The idea is actually quite old
  – In UK government: printing and publishing (19thC), and estates and procurement (20thC)
  – In the US: Recommendations by the Brownlow Committee (1930s)
  – In Australia: three Departments of Administrative Services in the history of the commonwealth government
  – Procurement cooperatives in many countries

• Neither is the ‘shared services’ terminology all that new, arriving in state-level government in the 1990s, and growing in popularity during the 2000s

• But the need to ‘do more with less’ since the global financial crisis has led many local, regional and national governments to look for further cost savings through greater use of shared services.*
Mixed experience to date

• **Some success stories**
  – UK Prison Service – award-winning public sector SSC

• **Some disappointments**
  – USA survey: half of SSC projects did not realize any savings, and a quarter actually reported cost increases (Schwarz 2014)

• **Some disasters**
  – Transport and research funding in the UK – massively over budget
  – Queensland Health Payroll – “in the front rank of failures in public administration in [Australia]”
  – Western Australia – decommissioned in 2011

• **Factors affecting likelihood of success** (NB: research-in-progress!):
  – Simple vs., complex transactions
  – Single-sector vs. multi-sector consolidation
  – Procurement vs. other corporate functions
  – Others?
Risk 1  Escalating start-up costs due to path dependence

• Large – sometimes huge – reform projects
  – Queensland SSC– “the largest organizational reform undertaken within the State Government”

• Reform often costs more than planned
  – UK Transport (105%) and Research Funding (65%)
  – Western Australia SSC – “original 2003 business case was fundamentally flawed”

• The problem of path dependence – organizations tend to continue in the same direction because there are many costs involved in changing course
  – Original investment costs*
  – Connections between different systems/processes*
  – Learning effects*
Risk 2 Increased transaction costs

• Organizations incur production and transaction costs
  – Raw materials, direct labor = potential economies of scale
  – Arranging and monitoring = determining how the back-office currently works, undergoing a tendering process, contract negotiation and monitoring, ongoing communication and coordination to deliver the service, etc., etc.*

• Often, when production costs decrease, transaction costs increase – and vice versa. There is a trade-off.

• The balance depends on:
  – The complexity of the service
  – The ease of performance monitoring
  – The trust between user and provider, etc.

• So, shared services can mean cheaper production costs but higher transaction costs. This explains the disappointing results in the USA (Schwarz, 2014).
Risk 3 Reduced service quality

• Common assumption that service quality should improve because of increased investment and expertise. But SSC clients sometimes report lower satisfaction.

• **Goal displacement** is where the ends become more important than the means. This is common in rule-based organizations.
  – “You start getting Shared Services and Procurement having policies and ideas of their own, and their idea about what your business should be. And they stop acting like the provider, and start acting like the customer.” (Senior UK official)

• **Slower decision-making** can also occur in rule-based organizations and in collaborative arrangements where multiple agreements are needed to effect a change.

• And **innovation can be harder** in organizations dominated by rules and standardization, if these produce inflexibility.*

• All of these can damage cost saving.
Risk 4  Functional duplication

• Duplication occurs when client organisations retain functions in-house. There are many possible reasons for duplication.

• Management **preference for autonomy**
  – Plenty of reports of manager/employee resistance to SSC reforms

• **Cultural expectations / top-down regulation** conflicts with internal efficiency/expediency
  – SSC reforms might be fashionable or mandated top-down, but managers only comply with this superficially because of concern for internal efficiency and effectiveness.

• Duplication as a **fail-safe**
  – Lots of reports of clients double-checking the work of the SSC, or performing additional work not available in their standardized offering.

• **Duplication undermines cost saving.**
Opportunity costs

• In any organization, capacity for reform is limited – in terms of human and financial resource.

• This means that leaders face choices and incur opportunity costs when selecting one reform strategy over another.

• Shared services require major organizational change. How else might that resource be spent, and how would the results compare?

• Are their less resource-intensive alternatives that achieve the same end while freeing up reform capacity?
  – UK National Audit Office recently argued that “many of the benefits generated [so far] could have been achieved by other means or with lower investment.”

• The answer will depend on context, but the point is that **the shared services model must be considered alongside alternatives.**
The five risks to cost saving*
Lessons – what can be done?

• SSC failure is not just the result of poor project management.

• Do not assume that shared services will automatically benefit your organization.
  – **Construct the business case with care**: be critical, skeptical, and evaluate all the options – including improved in-house provision and partial sharing.
  – Have a **large margin of error** for implementation costs, and account for initial and on-going **transaction costs**.

• Confront the trade-offs.
  – Very few public administration reforms are wholly beneficial. Examine the trade-offs **to prevent unintended consequences** and **develop risk-management strategies**.

• Use feedback.
  – Don’t dismiss negative feedback as simply irrational employee resistance. There are many rational reasons for clients to be wary of SSC reforms, and understanding these can **help improve reform outcomes**.
Thank you!

For a **written report** of this presentation, please email me at thomas.elston@bsg.ox.ac.uk

Download a **four-page policy memo** on the dos and don’ts of shared services at http://www.bsg.ox.ac.uk/research/policy-memos/share-not-share

See a **recent blog post** on shared services announced in the US at https://blogs.bsg.ox.ac.uk/2015/10/28/shared-services-too-good-to-be-true/

The Blavatnik School of Government
**A world better led, better served, better governed**