

Maconomy White Paper



Organization of Finance and the Shared Services Thinking in the Marketing Communications Industry

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Introduction

Major changes have taken place in the marketing communications industry during the last 10 years. Clients have become extremely conscious about what they get at what price. Ownership has consolidated into about 10 more or less global holding companies dominating the market. And new performance standards have emerged – for the big groups as well as for small independent companies.

Surprisingly enough, these major changes seem to have had little influence on the fundamental operating structure of the businesses. It is still an industry dominated by a huge number of relatively small and relatively autonomous operating entities with an almost full replication of back-office functions – in particular the finance function

Here is an argument about how and why to arrive at modernized financial set-up and achieve:

- Reduced accounting transaction costs
- Increased margins on client projects

...and an argument about why the change is extremely urgent, and what will happen if it is ignored.

Future financial setup

The financial functions can be split into two categories: i) volume and transaction oriented standardized processes (ledger keeping, reconciliation, payments, reminders, payrolls, reports, etc.) and ii) consulting, ad hoc analysis and management.

These two categories need to be organized distinctly differently in the future:

- The first part (i) is most efficiently organized in Shared Financial Services setups across operating units, brands, countries and for small non-networked companies even across competitors.
- The second part (ii) is most efficiently delegated to the Project Managers in the client service function who make the decisions on the projects.

Consolidating the transaction oriented finance functions (cf. (i) above) in a Shared Services facility is the only way to achieve economies of scale as well as the quality, stability and power necessary to become an excellent financial organization. Costs will decrease, and at the same time it will be easier to attract and retain the right individuals. It will be possible to report faster and more consistently. Moreover, it will be possible to apply the same standards on any issue from performance indicators to reporting format to all operating units. For independent operating units buying services from an external Shared Services supplier, this will of course work somewhat differently. However, the fundamental benefits of having access to efficient processes and best-of-breed, industry standards will remain the same.

With a few exceptions the size of the operating units in the industry is simply too small to achieve this kind of professional excellence on a stand-alone basis.

Distributing the financial management of projects to the client service staff (cf. (ii) above) is the only way to support the delicate decisions made every hour on ongoing client jobs. It is also the only way of ensuring that the right people get all the good lessons to be learned. And, these are not the financial people – but the client service people. Too often valuable information is left with a bookkeeper who is not able to get his/her conclusions across to the decision makers. Particularly in the small operating units, the finance function is staffed either with people who are not capable of interpreting the financial data to information on which decisions can be based – or with people who are not capable of influencing the right decisions makers with their interpretations.

Large units sometimes have a change willing and business oriented senior finance person who focuses on and excels at using numbers - rather than producing them. In that case it is a good idea to retain the person in the management team of the operating unit and make him/her responsible for the interface to the Shared Services facility and for implementing finance management in the client service department.

How it will work

Organizing the Shared Services setup

There are several organizational dimensions that need to be taken into consideration when creating a Shared Services setup.

A geographical dimension (by city, country, region or global) or a business line dimension (by advertising, PR, marketing research) has to be chosen as the main driver when a network establishes its Shared Services setup. For the independent Shared Services suppliers, the market will typically be defined differently – e.g. as all project based business within a certain geographical area.

Furthermore, there is the choice between organizing physically or virtually. A lot of considerations such as legal requirements, language barriers, time zones, tradition, etc. go into making the right decision, and often a stepwise and somewhat customized plan is the ideal conclusion. Again the independent Shared Services suppliers will typically have a broader definition of their setup, allowing several forms of interface with their clients.

Pricing Shared Services

Another important issue for the network Shared Services setups is how to price the services. Should it be a profit center, a zero profit setup or a cost center? By using a profit center model it will be possible to benchmark the efficiency against external suppliers with similar services – which is always a nice feature.



Also the profit center model will be the preferred model in keeping up with the arm's length principle in connection with intercompany trading.

The price tag from a Shared Services setup established as a profit center or a zero profit center will often be a negative surprise to the subscribing operating units. However, this is most likely not because the solution is expensive, but rather because the real costs of the previous finance setup was never really calculated, and what the cost of the financial resources needed would have been in the event the operating units had to recruit themselves.

There is a tendency to compare the total costs of a Shared Services setup with just the compensation element of the previous setup. But the Shared Services setup obviously needs to price its services with due consideration to its full costs - including lease of copy machines, the polishing of windows and the electricity needed for keeping the lights on, etc.

An independent operating unit should expect a total price tag of around 2.5% of its gross income for financial services from a Shared Services setup, whereas an operating unit, which is part of a typical multinational setup, should anticipate around 5%.

Converting to Shared Services

A big-bang conversion to a Shared Services solution is as risky as a big-bang conversion to a new system without live testing or running the old and the new systems in parallel. It is possible and optimal - when it succeeds. And it is a total killer - when it does not succeed.

Therefore, it should be considered to convert stepwise, but it will have to be arranged in a way that allows everyone to get the full end picture up front. Otherwise, the process will kill the project in job content and job security discussions.

The most important thing is to get the process started in a way that allows demonstration of some quick advantages to the sceptical organization. Often it will take a while until the overall reduction in staff costs and increase in financial professionalism are seen. Gains on the audit bill and IT costs will show quicker, but the biggest advantage often arises as soon as the distribution of the financial systems to the client service function has taken place. Responsible business people generally enjoy monitoring the financial interpretation of their action - and soon that interpretation will impact their action.

Client services dealing with finance

Client service is the first function to know when there is a client case (be it new business or client payments) that starts to consume time. They will therefore need to bear the responsibility of ensuring that a project number is instantly made available for the daily online time reporting from all employees.

Client service is also the first function to know when an offer has been accepted by the client. They will therefore need to be in charge of getting that offer converted to a budget for all external costs and internal resources – broken down into calendar days.



Client service will be deeply involved in the day-to-day execution of the client cases. They will be the first to know when there are unforeseen problems, they will be the ones to contact the client about changes in the project scope, and they will be the ones to make decisions about change of direction or the resources assigned. In other words, they will therefore need to be responsible for the continuous online and real-time monitoring of the client project system and for updating the project budget part.

Client service is the function quoting the next offer to clients. As a consequence, they will also be the ones absorbing all the knowledge from current projects - knowledge necessary to be able to price the next projects intelligently.

It is a lot of (new) tasks for client service – it will be tough to be them! But it is about time to realize that client service is the key commercial role in the agency and to align job content and job expectation to that fact.

Resistance to future setup

As the change completely dissolves the current financial function, significantly loosens the concentration of power with the local operating unit CEO and introduces comprehensive new tasks for client service, numerous excuses for not accepting this change will be made.

One objection will be that the client service staff is not interested in taking on a significant load of financial tasks. This is often true. But what is also true is that mental barriers will be lowered and new openings appear when intelligent argumentation and education are introduced.

Ultimately, however, management will have to be prepared for substantial staff changes in client service in the event that conversion of current staff proves unsuccessful.

Furthermore, it will be claimed that the local hand-on treatment of all transactions of a finance clerk, who knows the business and the individuals, is a necessity for the smooth running of the business. This is often true – but only until rules and procedures have been tightened and described sufficiently to allow efficient and professional processing. A task that should be done anyway, as it is bound to improve the profitability and transparency of the company.

Another objection will be that the systems are not ready for it. That is also quite often true. A dramatic organizational change like this will only deliver full impact if supported by systems that match by their very nature. Fortunately such systems exist indeed.

Surrounding trends vs. future and current financial setup

Massive consolidation

Competition is fierce and increasing – including competition from clients for whom insourcing has been made possible due to both the rapid technological development with digitalization of the whole workflow from design to ad insertion and to the increased competence level of their staff.

This very competitive environment has led the communications industry to massive consolidation during the past 15 years – particularly the last five years. A vast majority of the business volume is serviced by units controlled by less than 10 global holding companies. Still, however, these big holding companies consist of operating units as small as before the consolidation – and each of them often with their own full panel of functions, such as a finance department. The most obvious opportunity for these large players to optimize their businesses is not to develop new breathtaking services but rather to make the running of their businesses more efficient. And here the back office is obviously an object. By way of example, there is absolutely no reason to have a cluster of neighbouring units with each their full fletch financial setup. And the question is if there is a reason even when the units are geographically far apart.

The consolidation wave has also had an impact on the independent operating units, as the owners of these will compare their key performance ratios with the big players – and want to do just as well as them or better.

Prompt reporting

To satisfy internal management needs and to service the public with information about financial performance, the big holding companies will need to be able to make fast and accurate globally consolidated monthly closures. This need calls for a high degree of standardization of processes and policies and easy integration of systems across the various operating entities in the group.

Again the trend affects the independent operators too. They will of course want their financial statements as fast as they can see their competition being serviced.

Lost poor performer patience

The huge investments that have been made in acquiring companies include the geographical markets that are not considered core to the acquirer. Nevertheless, for many acquirers these non-core investments have become substantial and therefore they have also become a substantial problem when the non-core markets are poor performers. And they quite often are. The large players have lost their patience with the non-core markets and will demand that they perform up to the same standards as the major markets.

Introduction of Corporate Governance standards

The financial collapses earlier this decade has brought Corporate Governance into the minds of everyone. And not least into the minds of the large holding companies publicly listed in the US – or otherwise dominated by US business standards e.g. by client requirements. Various corporate governance standards – such as Sarbanes Oxley – have become part of the daily lives in the marketing communications industry. An industry previously said to have less rules and procedures than any other industry, which is why a particularly firm grip on these topics is called for.

Full transparency

As the marketing communication companies have consolidated so have their clients. As clients have become bigger so has the likelihood that the engagement is covered by an international agreement requiring full transparency and equal terms and conditions on all markets.

What if the financial setup is not changed

The overall dominating finance structure today in the marketing communications industry is a full financial setup by operating unit. In situations where two or more majority owned operating units are closely located, they may share a CFO and highly specialized finance functions like payroll, treasury and reporting. But even so a unit oriented finance structure is intact with either a de facto or locally perceived reporting line to the operating unit CEO. The finance department will be small as the lowest ranking in the internal departmental hierarchy of the operating unit.

Such structure concentrates a lot of information and power around the unit CEO – a profile who is quite often primarily a client and product oriented person and not the more general business person that one would expect to find in similar positions in other industries.

This constellation tends to have two major impacts on the organization:

- The finance organisations will not be able to do what is needed in the organization. Very often the finance people will be the ones carrying worried attitudes and apprehensions not immediately shared by the often more optimistic and enthusiastic operational management - who will therefore not support the argument when challenged by the line people in the organization. More importantly, operational management will not support the action that the worried attitudes may call for. The “bookkeepers” will be asked to shut up and go back to their desks in the basement – leaving the decision makers in the organization with no financial data at all or data that cannot be interpreted.
- Problems attracting, retaining and paying the best finance people. The best finance candidates will deem the finance organizations too small and too much under the thumb of operational management. They will be looking for positions where they are accepted - not as a necessary evil, but as a valued team player expected to contribute broadly to the company. Also, there are natural and narrow limits as to how much a stand-alone operating unit can afford to spend on their backoffice.

Often these two forces will reinforce mutually and create a downwards moving spin of financial quality in the organization and it therefore has a significant element of self-destruction.

This self destructing spin will increase rapidly in speed due to the inevitable trends within and around the industry. For the same reason it is unlikely that the marketing communication industry will allow the current setup to prevail for very much longer.

