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This year is a leap year, and like February 29 - which comes around every four years - it seems that restructuring efforts unfortunately come into vogue in a big way only every few years in response to some economic issue or malaise. You need to just read through any number of recent company earnings announcements to see that many organizations are taking restructuring charges and lowering their earnings as a result. Restructuring is generally a euphemism for "heads are rolling" and despite the significant impacts to the organization and its people, restructuring efforts are often undertaken in quite a haphazard and arbitrary way. Organizations often find that while restructuring may cause everything to change, nothing is actually different once completed.

Traditional restructuring efforts, whether in the finance organization or across the company, tend to suffer from three primary problems:

- They do not discriminate. Restructuring efforts generally treat all expenses the same. Edicts to "cut expenses by 5 percent across the board" or "reduce head count by 10 percent" are not uncommon and fail to consider that all expenses are not created equal nor should every business unit, product group, etc., be subject to the same restructuring requirements.
- They don't solve the fundamental issues. Restructuring efforts are similar to putting a Band Aid on an infected wound. You're not really solving the problem, but you're making yourself feel better because you are at least doing something. *The fundamental problems reside in inefficient and poorly constructed processes which ultimately result in cost and resource inefficiencies that hurt the organization. Traditional restructuring only goes after the visible signs of substandard performance - it doesn't get at the underlying causes.*
- They are generally reactive. Restructuring typically happens in the face of economic challenges that are hurting the organization, so such efforts are often "imposed" on the organization because of exogenous issues or factors. Instead, a well-structured discipline to optimize processes and costs by rooting out inefficiencies and unproductive complexity that crops up within the organization should be practiced on an ongoing basis.

Organizations should always be "restructuring" and optimizing how they do things. This ongoing optimization can be likened to the well-known philosophy of Toyota, which seeks continuous improvement. To solve for the aforementioned challenges and weaknesses apparent in most restructuring efforts, a well-defined Process and Cost Optimization (PaCO) methodology should be used.

If organizations adopt and commit to the PaCO discipline and its mantra of continuous organizational improvement, we submit that it will allow them to weather economic turmoil better than their competitive peers and also position them to emerge more nimble out of any such strife. When times are good, their leaner and more well-constructed structure equips them with greater capacity to invest in and capitalize upon opportunities that may be before them to grow their businesses.

There are three steps that an organization should adopt as it embraces PaCO:

### **Step 1: Reflect**

When we talk about reflecting, we are not talking about a "New Age-y" or existential reflection about your expense base. The reality is that all expenses are not created equal, so before thinking of restructuring, organizations should reflect on the nature of their expenses to determine which are strategic and which are nonstrategic.

Strategic expenses are those that are highly critical to the organization's short-, medium-, and long-term growth, innovation, and flexibility as an organization and are those that directly impact customers and/or the company's products and services. A central tenet of the PaCO methodology is that it advocates a departure from managing all expenses as items that need to be minimized and instead pushes for different but interrelated disciplines to manage expenses based on the criticality of those expenses to the organization.

Expenses that directly and actively contribute to the future health of the business through contributions to growth, innovation, and/or flexibility should be considered as investments in the business - not expenses. The Corporate Portfolio Management Association estimates that 25 to 40 percent of operating expenses fall within this strategic expense or investment category. Because of their direct impact on the future health of the company, these investments should fall outside the scope of any restructuring effort and should be managed via a corporate portfolio management discipline.

These investments should be optimized in a way that determines where the best opportunities for investment are. The goal with these strategic investments is not to minimize cost but to maximize value. These strategic investments may span expenses such as marketing, advertising, sales, innovation, R&D, and some types of growth-oriented IT and operations investments. In general, these strategic expenses - or rather, strategic investments - tend to be in those areas that are more customer- or product-facing.

The remaining expenses that are not discretionary and that should be managed using PaCO are the remaining 60 to 75 percent of the operating expense base. In a sense, these are the expenses of the company that are required to keep the lights on but do not directly drive the growth of the organization.

To differentiate from the previously mentioned strategic expenses, this category of expense will be deemed nonstrategic expenses.

Examples of such expenses include areas like payables, receivables, IT infrastructure, operations infrastructure, real estate, finance, human resources, legal, public affairs, etc. This doesn't imply that these are unimportant expenses, but given their distance from the end customer or the organization's products and services, it does make sense to consider them in a different light from strategic expenses such as marketing, R&D, etc.

### Expense Table [1]

At the conclusion of Step 1, you have reflected on and distinguished between two types of expenses: strategic, which are better characterized as investments, and nonstrategic. With this bifurcation of expenses in hand, you are now equipped to move to Step 2 of the PaCO methodology.

### **Step 2: Repair**

The PaCO methodology doesn't simply push for across-the-board cuts of nonstrategic expenses or promote knee-jerk initiatives to move activities offshore. Instead, before taking any action, it is important to understand why these expenses are being incurred and what these expenses should be achieving.

Quick-strike restructurings are often arbitrary, and while they provide quick returns, they tend to be more disruptive. Moreover, if they are not followed by process changes, the reductions and savings they enable often are not sustainable, with the expenses just creeping back over time and organizations experiencing "déjà vu all over again."

The repair phase of the PaCO methodology focuses on optimizing the underlying processes of these nonstrategic expenses. Before you can take action, you need to understand what is good, bad, and ugly about a specific process. In essence, you must diagnose the problem before you prescribe a solution.

At the start of this diagnosis exercise, a comprehensive inventory of processes needs to be developed, supplemented by information related to key skills required and the number of FTEs supporting each of these processes. This is more often a dynamic list that will change as corporations go through the ongoing circular loop of reflect, repair, and reap. Also, at the start, this inventory will usually tend to be at a "30,000-foot" level, providing a high-level overview of the task conducted, skills, and FTEs. While this level is good for an inventory, to conduct true repair work, you have to "look under the hood" and drill deeper into these processes.

Process Maps are a proven tool to do this very thing. In a hierarchical manner, they display how a transaction is processed, identifying a stream of activities that transforms a defined set of inputs into predefined output(s). How does this understanding of activities, inputs, and outputs translate to repair? The "devil" as they say, is again in the "details." A process map at the "30,000-foot" level will usually not yield an area to repair. But start digging deeper and you will uncover numerous opportunities.

In the following section, we will use some simple examples to talk a little bit about taking the

high-level process inventory and information on skills and FTEs to uncover some very tangible opportunities.

### Organizational Level 1 Process: Nonstrategic Expenses



The organizational level 1 process shown here represents the entire size of the "prize" that the PaCO program will focus on. A view such as this provides a high-level overview of the size of the respective organization (cost/FTEs, etc.) and provides prioritization logic on how to focus the repair phase. Process mapping, skills inventory etc. should be conducted going from the largest organization/cost base to the smallest one.

### Finance Level 1 Process (not exhaustive)



Let's examine the finance organization in more detail, and put it through this "30,000-foot" reflection of core finance processes. Identification of key skills and FTEs at this level will provide some understanding of the organization and underlying costs but will not be enough to bubble up any repair opportunities. Here again, unless otherwise evident through some anecdotal evidence, priority should be given to the process with the largest cost base. Now, let's take the "Payroll" process and drill down further.

### Finance Level 2 Process: Payroll (illustrative)

#### Payroll Graph [2]

At this next level, under the finance core Level 1 processes, you will start unearthing more details related to different process steps, key skills required, and number of FTEs required for each of the process steps. Very rarely - in processes that are extremely broken - opportunities may surface at this level, but more likely you will have to dig deeper for any sizable impact. Within the Payroll process you may now choose to drill down further into a "Level 3" process map. Here is an illustrative example of a level 3 process map of the subprocess "Print and mail paychecks to employees."

### Finance Level 3 Process: Payroll: Print and Mail Paychecks to Employees (illustrative)

#### Print and Mail Paychecks to Employees Graph [3]

This is the level of detail at which the first real signs of opportunity emerge. At this level, you will start seeing:

- A clear pattern of how a faulty input impacts the predefined output.
- A cause-and-effect relationship within a work flow and an ability to start mapping information related to input, output, FTEs, skills, and cost to each step of the process.
- An ability to benchmark cost and efficiency, etc., internally and externally.

Some examples of repair opportunities that may emerge are:

- Too many defects due to manual processing or faulty, out-of-date capabilities supporting the process.
- Too many FTEs for each input level due to lack of technology or lack of scale efficiencies.
- Rework driven by lack of clearly defined hand-offs at each step of the process.
- Higher-than-benchmark costs - due to a higher number of FTEs, higher overhead, geographic cost differences, etc.

To ensure a standardized way to look at the repair opportunity, it is advisable to adopt one process improvement protocol across the corporation. This will ensure a standard way of identifying opportunity and measuring success. Six Sigma is one such common and popular protocol used within a number of corporations today.

From this analysis of the process, you've created the foundation for ongoing business transformation, a systematic program to optimize processes and capabilities so that the right set of people with the appropriate skills at the optimal locations are conducting the process(s) with the most efficient and optimal use of capabilities.

This is not easy, however, because it does require long-term organizational buy-in, a strong will, and effective program management. But with this repair mantra ingrained within the organization, you'll be in a position to constantly evaluate the company's processes and improve them on an ongoing basis.

With this understanding of what requires repair, you're now ready to take action and move to Step 3 of the PaCO methodology.

### **Step 3: Reap**

#### Reap Graph [4]

During the reflect phase, you've done the hard work to understand your expenses in greater detail and have broken them down into the strategic and the nonstrategic. Then you evaluated the nonstrategic expenses and their underlying processes as part of the repair phase and have determined how these processes should be carried out correctly. With that information in hand, you are ready to take action, reap the rewards of your efforts, and actually optimize your cost base.

How do you go about doing this? For the most part, you will leverage a lot of the work done in the reflect and repair phases, but from here on you will need a framework for assimilating all of the information above and developing a set of specific recommendations that will deliver savings that you can literally take to the bank.

The following section details a solution/recommendation framework that will enable you to take the inventory of processes, skills, and FTEs gathered during the repair phase and develop a set of recommendations that you can use to reap real process efficiencies and cost savings.

### **Reap Solution/Recommendation Framework**

From the framework above, it is important to understand the relative complexity and ease of implementation of these recommendations. This will ensure that the organization is appropriately focused on getting the quick wins while managing expectations around recommendations that are more complex and difficult to implement. Using this framework, the recommendations can be categorized as follows:

- **Quick wins/low-hanging fruit:** Global, standard, reliable, and repeatable processes that can be migrated offshore right away to leverage the low-cost advantage that these offshore locations provide.
- **Medium-term opportunities:** Recommendations related to process improvements to make them standard, reliable, and repeatable; consolidation of like skills or regional processes into shared services capabilities.
- **Long-term transformations:** Processes that are outliers to the above framework and will need significant improvement or potential redesign.

You will want to take a portfolio approach to your PaCO portfolio as well. You can utilize quick wins to deliver hard-dollar cost savings and also to create momentum and excitement around your efforts. Think of these real savings and this organizational momentum as the currency you can use to invest in and enable the medium- and long-term opportunities before you.

As you tackle the short-, medium-, and long-term opportunities, your investment in and embrace of the PaCO methodology can yield eye-popping results. We've seen organizations achieve a 15 to 20 times return on such efforts, and with the ongoing nature of a PaCO model, these returns continue to be enhanced over time.

As mentioned earlier, senior management endorsement and a will to commit the organization to this change process over the long haul is critical to the success of the PaCO program. Also critical is a very strong operational framework to manage the program. A few key organizational considerations:

- **A central Program Management Office (PMO).** Reporting directly to the CEO or the CFO, the PMO should have a mandate to work across the various functions and businesses within the corporation to set up and run the PaCO program. The PMO should be composed of experienced project managers, process engineers, and Six Sigma black belts and master black belts. They will work with the various business leaders, finance leaders, and other subject matter experts to run each stage of the PaCO

program and set optimization targets for each of the functional areas within the nonstrategic expense base.

- A central capability/repository to track and report saves. While initially this may seem like overkill, an investment in the capability to track and report saves at an individual project level more than pays for itself over a short period of time. Not only does it provide an approval work flow and credibility to the individual efforts of the various project teams, but also it will enable you to uncover linkages and opportunities to share information and even resources among various PaCO initiatives.

Restructuring does not need to be a "four-letter word" within the organization if a more thoughtful, proactive, and disciplined approach to optimizing costs and processes on an ongoing basis is adopted.

Use of the Process and Cost Optimization (PaCO) model allows you to be relentless in your efforts to carve out inefficient processes and costs on an ongoing basis. It also lets everyone know that inefficiency will not be tolerated at any time.

Ultimately, executives and managers will be best served by establishing an organizational discipline that focuses their energies on creating ongoing cost and process efficiencies that provide a real advantage - and away from those that are reactionary and knee-jerk and just provide short-term, illusory benefits.

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