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Centers of Excellence: Management Within Multinational Corporations


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Centers of Excellence Management within Multinational Corporations

by

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Abstract

As organizations expand geographically, and especially when expanding globally, they often find it necessary, or more effective, to develop Centers of Excellence (CoE). If properly structured these centers can reduce cost, improve efficiency, leverage organizational assets, and often improve levels of organizational innovation. This is the next installment in a series of articles started in the first issues of the JMI exploring these very challenging issues (Coughlan & Bernstein, 2015). In this installment the authors will specifically address issues surrounding leadership, integrated governance model, standardization, continuous improvement, business continuity, and managing through hard target metrics. This article assumes that the CoE is past its initial startup phase and it operating at a full level of scale. In addition, this paper is focused on multi-national corporations (MNCs) where CoEs are internally operated – not outsourced to third parties - and more specifically on knowledge based CoEs..

Keywords: 3 to 5 keywords

Introduction

The building of expert skills, or capabilities, rarely happen in the normal course of business or in traditional business environments. Therefore, it is often necessary to develop environments with a concentration of experts, deep interaction between related disciplines, focused training and research, and the infrastructure to share this knowledge and abilities across the organization. These environments have become known as Centers of Excellence (CoE), and they have been implemented across a variety of disciplines and in a number of different formats, including but not limited to: centers of operational excellence, research and development centers, centers of elite professional services or medical practice, think tanks, and strategy centers (Frost, Birkinshaw, & Ensign, 2002; Mieg, 2014). Since the term is broadly used, and sometimes would seem to have conflicting definitions, in this paper we will use the definition provided by Frost et. al. (2002, p. 997):

[CoE is defined as:] an organizational unit that embodies a set of capabilities that has been explicitly recognized by the firm as an important source of value creation, with the intention that these capabilities be leveraged by and / or disseminated to other parts of the firm.

This paper is the next installment in a series of articles that were begun in the founding issue of the Journal of Management and Innovation (JMI) and will likely continue in subsequent issues. The initial article focused on the startup or launch phase of a CoE. In this article the authors will focus more on issues that may begin to develop post the startup phase; including the following: leadership, integrated

governance model, standardization, continuous improvement, business continuity and managing through hard target metrics.

Leadership model

As we discussed in the initial article in this series, among the critical factors that contribute to the success of a CoE is its ability to be innovative and provide thought leadership in a specific area. To achieve this the center will need to develop a local culture where participants are willing and able to question the status quo, where diversity of thought and perspective are embraced, and one that will likely include individuals from different cultural backgrounds who will be required to successfully interact. In addition, in the development of this local culture significant effort must be made to insure the local culture will integrate with the broader corporate culture. This kind of environment present a number of challenges to managers who attempt to implement a traditional top down leadership style (Hofstede, 2009; Kelley, 2005; Meyer, 2014).

Therefore, in establishing the local culture expatriates play an integral role as cultural bridge or gatekeeper. Expatriate leaders should not just be dictating cultural, or replicating what the culture is in the home country. Their role often is to provide shared context for information, cultural artifacts, and environmental conditions (Marchegiani & Pirolo, 2004). The goal being that ability of the CoE to develop exceptional skills and capabilities not be hampered, and that its local culture has enough cultural proximity to the home country to integrate well within the organization.

In some instances, it may be necessary to import an entire expatriate management until local hires can be developed into managers. This is particularly necessary where the culture of leadership in the CoE host country is materially different than the leadership style of the MNC. In these cases, extensive training of new staff in the management approach of the MNC will need to be developed. While an expensive option, in the long run, it will often lead to a more rapid accretion of productivity expected by the CoE and actually be the most cost efficient approach. This is a result of a more rapid integration of processes, and more rapid reengineering of those processes to yield a faster ramp up of productivity actions.

Of equal importance to where the leadership comes from, is the leadership style. There are of course many effective leadership styles, but to optimally manage a CoE, the blending of two styles of leadership would tend to be optimal, Visionary (transformational) and Affiliative (collaborative)(Murray, 2010). Since one of the key missions of a CoE operation is to adapt processes and a labor model to achieve a more cost efficient, but similar result, the ideal leader should have a strong transformational background and subject matter specific knowledge of the particular CoE operations. In addition, failure or sub optimization of a CoE is commonly caused by a lack of integration between the CoE and the rest of the Corporation (“Centers of Excellence | The Hackett Group,” 2017). This is particularly important for knowledge based CoE’s, as the integration of the processes assigned to the CoE cannot be done in a silo fashion apart from the core operations of the enterprise. The consequences of a lack of integration can be severe. Certainly not

fully achieving cost point objectives is a failure. However, other impacts can have a greater impact to the enterprise. A successful CoE operation should be literally transparent to the MNC clients. Poor integration can lead to material customer facing errors and dissatisfaction. Of even greater impact a lack of integration can lead to lapses in control processes, whereby the unit headquarter operations may be making an assumption of control points being executed by the CoE, when in fact there is a lack of linkage and control points are not being performed by any organization.

MNC's that are deeply engaged in a CoE model have realized that their pipeline for future talent development will need to emanate from the center to unit headquarter organizations. In order to ensure a robust level of talent, the CoE and the unit headquarter organizations must operate in a coordinated fashion since the majority of hiring and attendant future talent will need to be developed and obtained from the centers.

One successful approach for talent development is to develop locally hired employees into successively higher levels of management responsibility and over time replacing the expatriate managers. In addition, some segment of the hired population should have a demonstrated mobility to, over time, staff unit headquarter operations of the MNC. Managing labor costs will be covered later in this article, but it is as critical as the development of talent and should operate in tandem.

Lastly, it should not be lost on the reader, that a crucial role of a CoE leader is communication of the vision and the plans (Harrison, Paul, & Burnard, 2016). Employees need to understand the vision to gain their buy in and develop that transformational mind set as a part of the organizational DNA. Further, they need to understand events that will be unpleasant along with the pleasant ones. Employees will create rumors far worse than any contemplated management actions and leveling with the staff on the good, the bad and the ugly coming their way will engender far greater buy in and loyalty.

Lastly, to ensure the highest level of integration and coordination between CoE's and the broader enterprise leadership, having all centers in a given function report hard line directly to a worldwide single vertical leader at the Corporate Headquarters level is crucial. Absent such a structure, the CoE leadership will have too many competing directions and this will drive inefficiency, a lack of opportunity to standardize processes and inconsistent and potentially competing directions, as well as, a lack of single point process ownership.

Integrated Governance

The integration of governance over a COE operation is closely related to the leadership approach. An integrated governance is critical to the effective management of a MNC's CoE's. Most MNC's have centers that manage many different functions of the enterprise. The traditional approach is to have tightly managed central governance for every function. The belief being that without central control there would be tendency to operate in an uncoordinated fashion

resulting in too many and inefficiencies, a lack of consideration for long term labor costs, skills, political stability and other potential business continuity interruptions (Dyer, Forget, Osmani, & Zahn, 2013).

Following the traditional approach, a relatively small corporate headquarters organization should be in place that will establish location strategies, size limitations, balancing business continuity and labor cost escalation risks, evaluation of geo political risks, coordinated real estate and infrastructure strategies and synergies that can be achieved across functions and implementing and managing location leaders. While having a location leader to oversee the administration of local operations and government relations where multiple CoE's reside is a preferred model, to avoid the issue of a center operations developing a silo relationship to the organizations they support the operational management of each center optimally will report up through their respective organizational chain and have a dotted line relationship to the center leader.

A variation on the traditional approach is an in integrated shared services organization. The advantages are efficiency, the risks are a lack of organizational responsiveness and a lack of accepting the ownership of center results. If an organization chooses the integrated shared services approach, it will require an extremely high level of senior management sponsorship and attention to ensure operating unit acceptance and integrations (Price Waterhouse Coopers 2008). Generally, the shared services approach is best suited to functions that are highly process oriented, such as accounts payable or administrative call centers. However,

it is less attractive for processes that tend to be less defined and require a higher level of intellectual independence such as Financial Planning.

Recent literature would suggest that the issues is more coordination than control, that tight centralized control can lead to efficient organizations that are not effective, or that the centralized control can become a bottleneck . As a center moves from purely mechanical tasks, rout tasks, or clerical activities to ones that requires cognitive skill, analysis, and creativity the success of the team often dependent on higher levels of discretion relative to their work habits and processes. In an organizations that require high level of cognitive creativity often more to more modern structures - such as Team of Teams (McChrystal, Collins, Silverman, & Fussell, 2015), Open Organization (Whitehurst & Hamel, 2015), or Holacracy (Robertson, 2015) – lead to dramatically increases both effectiveness and creativity.

However, these structures usually only work in organizations that have extremely high levels of transparency, and high level of communications across the team, its partners, and its internal customers – as well as a culture that is tolerant of new ideas and approaches to solving problems. Organization that are highly regulated, or have cultures that require strict adherence to cultural norms, might find such structures unsuccessful. Regardless of the of the environmental variables moving to more open organizational structure requires high levels of personal professionalism on the part of team members, training to create a sense of gravity, and well established expectations on the part of the team and its leadership (Coughlan, 2016).

Standardization and Continuous Improvement and managing labor costs

Traditionally, CoE's have been set up as either a lift and shift operation or a reengineered operation. More contemporary approaches take a more integrated step of integrating both lift and shift along with reengineered steps (Postma, 2011). Regardless of the approach taken, the mission of the CoE should be to take processes in any state of reengineering and drive continuous improvement. Often among the first steps to driving continuous improvement is to focus on standardizing processes across all the various business units supported. Standardization can be a series of moderate steps to communize processes or it can be done by radical transformation. Depending on the requirements at hand, both approaches have merit. However radical transformation requires a much higher level of cross functional senior management support, higher levels of skills, risk takers and leadership that has the capability to engage persuasively across an organization (Harrison et al., 2016).

In fact, a truly transformed state is when although an enterprise may choose to operate from multiple locations for reasons of time zones, language factors, risk mitigation and scale limitations, but could do the work from any location as it is fully standardized. This is an extremely ambitious objective for any large MNC to achieve, but it is the ideal objective.

There are many ways to drive standardization. Certainly traditional reengineering approaches are an important vehicle. Having employees co-located and working together in integrated teams is a natural way to standardize. A

powerful tool to standardize processes is to deploy lean six sigma techniques. Lean six sigma as a process has great reengineering value not only because it takes processes and devolves them into the smallest of activities to root out unnecessary steps, but it can be used in both small and large projects equally effectively. This scalability of Lean Six Sigma techniques, allows for the skills to be developed organically within an organization and continually grow in attacking successively more complex topics. Additionally, because it is a professionally recognized skills designation, employees tend to migrate toward it not only to improve the enterprise but to improve their own credentials at the same time. Lean Six Sigma when implemented in conjunction with contemporary technology applications such as analytic techniques can yield extraordinary levels of work elimination and productivity (Dyer et al., 2013).

Ultimately standardization of processes is seldom a rapid or onetime event, but rather a slow continuous process that literally becomes the DNA of the organization. To succeed, it must be continually reinforced, sponsored and measured by leadership. The labor cost arbitrage of moving work into lower cost locations as CoE's, is normally a onetime event. Accordingly, CoE's typically are measured to continually improving productivity and cost reduction targets, which can only be achieved by this continual focus on process standardization and improvement. Additionally, as noted below in managing labor costs, highly effective CoE leadership can continually drive new labor cost arbitrage by developing skills that can successively move up the value chain.

Two critical theories consider when looking at standardization are Baldwin and Clark concept of modularity, and the Coase theorem of transactional cost. Under the Baldwin Clark concept complex projects (e.g.: software development, automotive design, . . .) are broken down into discrete modules which are intended to be part of a larger whole. The intent is that each discrete module can be modified or upgraded without affecting the other modules. This can be done with both products and services. There are of course limits to this concept but it is what has allowed industries such as PCs and software to grow as quickly as they have (Sviokla, 2016) .

Coase theorem of transactional costs posits that aside from transactional costs the most efficient outcome will prevail in the market. The critical element of the theory is transactional cost. According to this theorem “the only companies with growth potential are those that keep their internal transactional costs (their own expenses) lower than their external transactional costs (the expense of doing business with others” (Sviokla, 2016). If the organization cannot accomplish this at some level there is no reason for the corporation to exist.

A great challenge for CoE management is managing labor costs. The initial cost arbitrage as noted is a onetime benefit and the CoE risks offsetting process productivity with rising labor cost as employees develop higher levels of skills and or simply time based salary increments. Additionally, MNC's tend to agglomerate operations in locations where skills exist. This tends to begin a continual cycle of escalating labor costs.

There are two primary ways to mitigate the cost pressures on labor. The work force needs to be bifurcated into a limited set of highly skilled people who can advance into continually more complex roles. Shifting those roles from the traditional operating units into the center effectively increases the value provided by this limited subset of staff and justifies the higher labor costs as it regenerates a new cycle of arbitrage as the more complex roles are moved into the CoE.

However, not all staff have the ability or desire to rapidly move up this complexity chain of work tasks. In order to keep labor costs from escalating for this segment of the population, the CoE needs to be able to implement and manage a high level of attrition, whether it be naturally occurring or forced by management. This requires a large investment in training, utilizing the benefit of scale by having large teams working together in one location and the use of a thin layer of deep subject matter experts to continually train new employees on processes. However, making this investment, allows the CoE to constantly evergreen their work force, with higher paid employees exiting and being replaced by new less expensive employees. Adding to the complexity of executing this strategy is to have a strong understanding and adherence to local labor laws and regulations. However, in the absence of this continual ever-greening cycle of managing labor the MNC risks losing the unending ability to yield on productivity improvements due to labor cost offsets.

Business Continuity

To this point in this article on managing a CoE, the focus has been on the ability to yield the benefits of centralizing work in lower cost labor markets that are typically in less stable locations in the world that perhaps one would experience in the US or European Union. Business continuity is an offsetting risk to these benefits that must be managed or management is going to put the viability of key business processes at risk.

While there are many alternatives to identify the type of business continuity interruption a common definition is a three tiered approach. Level one, a minor incident, Level 2 an emergency level that is disruptive to operations, and level 3 a serious disaster that would significantly impair if not stop operations (Loomis, 2010).

Because MNC's are becoming more and more dependent on CoE operations, leadership must be prepared to address all levels of business continuity interruption. The risk is further compounded by the fact that CoE's as noted are often located in less stable areas of the world and that skills are highly concentrated, often fully co-located into single buildings to yield the highest levels of synergies.

The simplest mitigation would be to create virtual CoE's that do not co-locate people, however, given current levels of technology, this largely defeats the expected synergies of large teams co-locating and working together. Given that reality, leadership needs to take actions to mitigate risks to operations. These risks range from minor such as a short term power outage to extreme such as a natural disaster or political unrest rendering staff of being unable to get to the work place or

a total loss of communications access (“Business Continuity Planning Suite | Ready.gov,” n.d.).

First and foremost a center should have a well-documented and tested disaster recovery plan that includes contact information for both managers and staff that should be kept outside the work place so that communication channels can be optimized. Documentation without detailed testing is a very risky recovery plan as management, is only guessing its efficacy (“Business Continuity Planning Suite | Ready.gov,” n.d.).

Further a small disaster could turn into a catastrophic event for a CoE. For example, a small fire and building evacuation that may last only a short time, can completely defeat a center's ability to operate if the sprinkler system destroys desk or laptop computers and rendering the center with limited to no communication ability.

There are however means that leadership can put in place to mitigate the varying levels of business continuity interruption. For a level 1 situation, having alternative work locations available or deploying laptops to employees who have the capability to work from home is a relatively simple solution. There are security concerns that must be addressed if employees are utilizing unsecure internet connections for sensitive information and the cost of laptops is higher than desktops, but a relatively inexpensive means of mitigation. Leadership should also have well documented work tasks by employee so that in the case where a subset of

employees are not available, key work tasks can be redeployed to staff that perform comparable tasks.

Level 2 business continuity issues add a significant level of complexity for management. First management must assume that the work place is not available for a significant period of time or that a material number of employees are not available.

Layering on top of the mitigating actions in a level 1 disaster, highly detailed and documented desk procedures are a first order requirement and they need to be stored on a server that is materially separated from the CoE location or ideally cloud assessable. Additionally, access to the server must be broad enough that it is highly likely management and staff can access the materials. In other words, the worst scenario would be to have a CoE's desk procedures dependent on one or a limited number of administrators that became unavailable rendering the plan useless. Additionally, cloud based back up of all key files used by the staff is a desirable state. As important as the data is, people and access are still the most important component of operations. As such, cross training and having a firm understanding of required VS discretionary tasks is critical, as work will be distributed among available personnel. In situations where a CoE has a sister location, to the extent that the level of transformation has evolved to the point of work standardization, the "hot" transfer of key tasks across locations should be enabled and tested.

In the worst scenario of a Level 3 continuity interruption where by a center for any number of natural or manmade reasons is rendered in operable for an

extended period of time, a catastrophic recovery plan is needed. In this situation, an enterprise would shift its focus solely to genuinely vital business requirements which are typically, the ability to support clients, the ability to access and move cash, the ability to pay employees and suppliers and lastly the ability to meet statutory requirements. There are many other elements of business operations that may be seemly important, but in fact in the short term, will not prevent the vital activities from being delivered upon. For example, a Financial Plan is highly important as are monthly internal measurements, but in the short run they are not vital.

The key is to have a disaster recovery plan that will allow the vital activities to continue. This can best be accomplished when there are sister CoE locations whereby all location focus only on vital activities and the ability to *hot* transfer tasks has been well documented and tested. This luxury may not be afforded every enterprise and therefore alternative approaches are appropriate. These include the ability to transfer tasks from the CoE back to the respective unit headquarter operations of a company. Or alternatively, if a location is physically lost, but the staff are mobile, there should be plans to temporarily relocate them to other company facilities. The peak work periods in a monthly or quarterly cycle will also to a degree establish the impact level of the interruption.

This article does not address disaster recovery of IT operations as that is an entirely different scenario and most well run MNC's have hardened and well established IT back up plans and needed redundancy or outsourced contracts for IT

disaster recovery. There are however other mitigating actions that can be taken, as most operational interruptions fall short of a level 3 disaster. For example, in the scenario where personal computer equipment may be lost, a plan to rapidly deploy replacement equipment is an advisable action. However, many MNC's will discover that import controls will greatly slow down the delivery of new equipment.

Alternatively, a company may keep an emergency stock of personal computers in a secured location. Certainly they will never be able to afford the economics of complete replacement back up, but using technology that allows for a desktop image to be stored on a memory stick, will allow employees to deploy into a three shift operation and share equipment, while at the same time eliminating the requirements for less important tasks and manage to keep key operations running. In other cases, MNC's are able to operate at a scale where a CoE can be operated as one organization, but physically be in two separate locations, greatly facilitating the short term movement of staff and work task.

Of all the management obligations in running a CoE, disaster recovery is the one that management hopes they never have to implement, but it is perhaps the most important activity and investment to protect the operations of the enterprise and while easy to ignore, it must be constantly front of mind and regularly tested.

Managing a COE through hard metrics

Einstein said "not everything that counts can be counted and not everything that can be counted counts". Although Deming is often misquoted as saying that you cannot manage what you can't measure, when it comes to managing a CoE

operation, there is a lot of truth in that statement. Simply the term, Center of Excellence, implies that businesses are going to hold these operations to a high standard on many metrics and the fact is that the business will get what they measure. In managing a center there are an unlimited number of key metrics, but in this paper, we are going to focus on eight of the most critical. As critical as having the proper key metrics in place to measure, is to have a regular cadence weekly, monthly, etc. to measure CoE leadership on their performance and in turn related incentives. This is a key role of the world wide vertical CoE leader to drive the cadence on measuring all metrics, not just those mentioned in the paper.

Labor Cost

As noted above managing to an established labor cost is a key metric that requires at a minimum monthly attention so that any needed corrective actions can be taken. While it is the mission of the CoE to deliver high quality and standardized services, achievement cost and budgetary targets is also paramount. There are two schools of thought on distribution of a CoE cost. Where the operating units have little control over spending levels, such as in an internal audit function, the budgets are most effectively charged to a corporate allocation pool. On the hand, where the operating units play a strong role in the number of resources required, a direct charge back mechanism can be a very effective control point.

Productivity

Since it is a primary role of a CoE to perpetually drive productivity, a regular cadence of actions that deliver a comparable service at a lower cost is a primary

measurement. This can be through measuring the impact of technology or process improvements and standardization, lean six sigma results, elimination of unnecessary work tasks, shifting work through the benefits of scale and teamwork to a lower salary band of employee, or re-shifting work from one CoE to another that operates at a lower cost, but may not be suitable for all types of tasks. To maintain the shared governance model, it is paramount that changes in process that have a change in the end results, or any control point, need to be jointly approved with the leadership in the MNC unit organization. If there is a process change, but the end results have no change, the CoE should feel empowered to simply execute on those independently.

Attrition and Staff Development

The CoE model is inherently built to manage a higher level of attrition than traditional MNC business models. This is driven by the more competitive emerging markets that they are typically located in, the younger employee demographics and as noted above the desire for some level of attrition as part of managing labor costs. However, for any given CoE, there is a sweet spot for targeted attrition, as well as, tracking what would often be called *regrettable attrition* when a high talent employee is lost. Managing attrition through a monthly process is an ideal interval as trends can be spotted and corrective action taken on a timely basis.

In order to manage a less experienced, high turnover model an effective CoE must have an extremely robust training and education program. The focus should be both job specific and simply skills development enrichment. Resources should be

dedicated to coordinating training, utilizing all of the various subject matter experts in the CoE and as needed supplementing with *outside skills*. To ensure a rich and effective program, metrics on education and training should be reviewed quarterly.

Internal client satisfaction

The mission of the CoE to drive cost and process improvements cannot be executed in a vacuum. Measuring the level of satisfaction of the internal client is also a key mission. This should be done formally through periodic surveys, as well as random leadership discussions directly with clients. There is a balance point in the measurement of client satisfaction. Perfect satisfaction would typically not be an ideal or achievable goal. Given the initiative to drive change, there is a high probability that at any point in time a client is experiencing the difficulty and potentially reacting negatively in the short run to change, which is a normal human nature response (University of Michigan, 2000). Accordingly, the key to measuring client satisfaction is less about the absolute result and more about driving a continually positive trend. This is a measurement metric that should be thoroughly reviewed at least semi-annually.

Top talent development

As previously noted two key missions of a CoE are to ultimately become self-sufficient in developing locally hired leadership to eliminate the need for costly expatriate managers. The second, is to provide a pipeline of talent to the enterprise, such that a small segment of the CoE population can move into leadership roles across the enterprise outside of the CoE and to also develop inside the CoE, allowing

the center to evolve its way up the value chain in terms of job roles performed. Measuring and tracking the careers of high talent employees should absolutely be the role of the worldwide vertical leader. Ensuring programs are in place, such as promotions and retention awards to minimize attrition and to also ensure these individuals and properly developing into more complex and leadership roles. As MNC's become more and more dependent on CoE talent as a continually larger portion of the enterprise population is CoE based, this is a metric that deserves at least a thorough review on a quarterly basis.

Control Processes

As MNC's become increasingly dependent on their centers, more and more control activities will be delegated to the CoE. The best way to mitigate a lack of experience and higher than traditional attrition in the area of controls is to have extremely robust measurements to ensure processes are being properly executed. Ideally controls should be evaluated monthly and include both peer and external reviews.

IT integration

Ultimately productivity cannot be optimized unless processes and IT process and analytics tools are tightly integrated. Standardization of processes is a gate to optimizing IT resources and support. But a weekly read out on IT projects and attendant metrics is an ideal mechanism to ensure the process is working as effectively and money is being efficiently spent to gain the greatest process productivity and improvement yield

Business Continuity

As previously addressed, business continuity is a critical element to running a successful CoE. The greatest risk with business continuity plans is that they are thoughtfully build and tested, but age and without constant updating will rapidly become down level in their effectiveness, perhaps even making them inoperable. This is an area that should be continually updated, tested and reviewed on at least a quarterly basis by the worldwide vertical process owner.

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