

DERIVING BUSINESS VALUE

from cost allocation and portfolio management

Procurement and Finance management



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Introduction

How to improve cost effectiveness and cost awareness through portfolio management and cost allocation

The idea in brief

The problem

Cost allocation drives procurement behaviour. Hence, lack of cost allocation may lead to suboptimal demand.

The argument

Effective control and execution of the cost allocation process pave the way for efficient demand management. Impact on a business level as well as on a behavioural level requires improvement of cost effectiveness and cost awareness through application portfolio and business process management as well as cost allocation practice.

The solution

It is critical to have the right governance and organisation in place to ensure cost-effective applications in a robust application portfolio that satisfies business needs. It is important to have an agile governance of the portfolio of application and process enhancement initiatives underway in the organisation to facilitate effective and fair chargeback (or showback) mechanisms.

In this Viewpoint, we invite you to follow our approach to create value in the areas of the business where sourcing, procurement, IT and financial management take place. The value creation is centred around cost allocation and hereby relating consumers, requisitioners and functional purchasers of products and services to the actual cost base that is imposed by the purchase.

When introducing a cost allocation initiative in an organisation, the purpose of this initiative should be stated clearly and be related to the value drivers creating the anticipated impact.

The initiative aims at improving IT cost effectiveness and facilitating the organisation's capability and practices in relation to IT cost awareness.

This Viewpoint will examine how organisations can improve cost effectiveness, leading to a series of business and behavioural benefits (impacts).

Business impact includes:

1. Better control of IT costs and IT spend
2. Better use of IT resources

3. Proactive management and utilisation of the portfolio of IT applications

Behavioural impact includes:

1. A more comprehensive, fact-based and nuanced dialogue in the organisation on IT costs
2. A thorough understanding of the IT cost practice
3. A common IT cost awareness and understanding of what drives IT costs

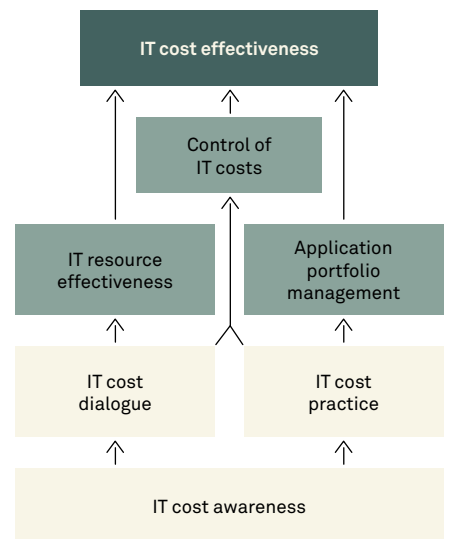


Figure 1 Impact case structure

In the following section we will address the question:



HOW DO I INTRODUCE IT COST AND BUSINESS VALUE AWARENESS IN THE ORGANISATION?

In order to emphasise the importance of change, we have elaborated the business and behavioural impact drivers.

Desired business impact:

- Control of IT costs to stabilise/reduce cost development
- IT resource effectiveness based on transparent and efficient KPI-driven IT cost allocation process through showback/chargeback of IT costs to top management and line of business
- Overview of the IT landscape and maturing of the IT landscape through application portfolio management, including application-specific development directions and prioritisation

Desired behavioural impact:

- Establish a culture of IT cost awareness due to understood and accepted cost allocation. The cost allocation will be based on a fair and transparent model, including change of business unit and affiliate behaviour with regard to ordering, maintaining and shut-down of applications/services due to cost focus

- Enhance IT cost dialogue based on business unit IT cost templates and adopt solid “explain or defend” rhetoric in reporting supporting a fact-based IT cost dialogue in the organisation
- Develop ongoing IT cost practice with regard to data management, allocation, analysis, decision-making and management

The value drivers of the cost allocation can be related to exact key performance indicators (KPIs), which may govern the cost allocation initiative.

Co-creation – our preferred customer interaction form

For more than a decade, we in Implement Consulting Group has gradually developed our customer engagement and project approach, moving from expert advice towards a higher degree of customer involvement, and now has an elaborated and widespread co-creation practice as the DNA of the consulting practice. Hence, the customer has become an active and knowledgeable participant in a common process leading the engagement of the surrounding business network.

Co-creation was originally coined by the scholars Prahalad and Ramaswamy in their 2000 Harvard Business Review article “Co-Opting Customer Competence”. This idea has been developed further in their 2004 book *The Future of Competition*. Several other authors have contributed in this area.

Co-creation is an approach to customer interaction which emphasises the generation and ongoing realisation of mutual consulting firm-customer knowledge and value creation. An approach where the consulting firm’s and the customer’s resources and

capabilities are combined and renewed to create value through new forms of interaction, service and learning processes. In essence, co-created value arises from personalised unique experiences with and for the customer.

In a cost allocation project, co-creation is introduced as having the customer involved in all activities from business need definition, process mapping and requirements development to design of application portfolio, data requirements, financial and application data retrieval, allocation mechanisms and mock-ups, in addition to change management preparation, development, testing and implementation, change management and further roll-out, impacting the execution speed, quality and value.

Structure of the Viewpoint

We see a clear interrelation between cost allocation and cost awareness and the possibility to utilise the cost insight in strategic decisions on application portfolio management and application life cycle – including applications’ coverage of selected business processes – and the overall governance of the organisation.

Each subject matter will be covered in the following sections.

Cost allocation will provide the organisation with the needed cost awareness and transparency to identify the true cost profile of all applications within the organisation.

This will lead to a more comprehensive analysis of each application’s value vs. costs in the organisation that – together with an assessment of business value and IT-strategic fit – will enable the organisation to develop their unique **application portfolio** roadmap

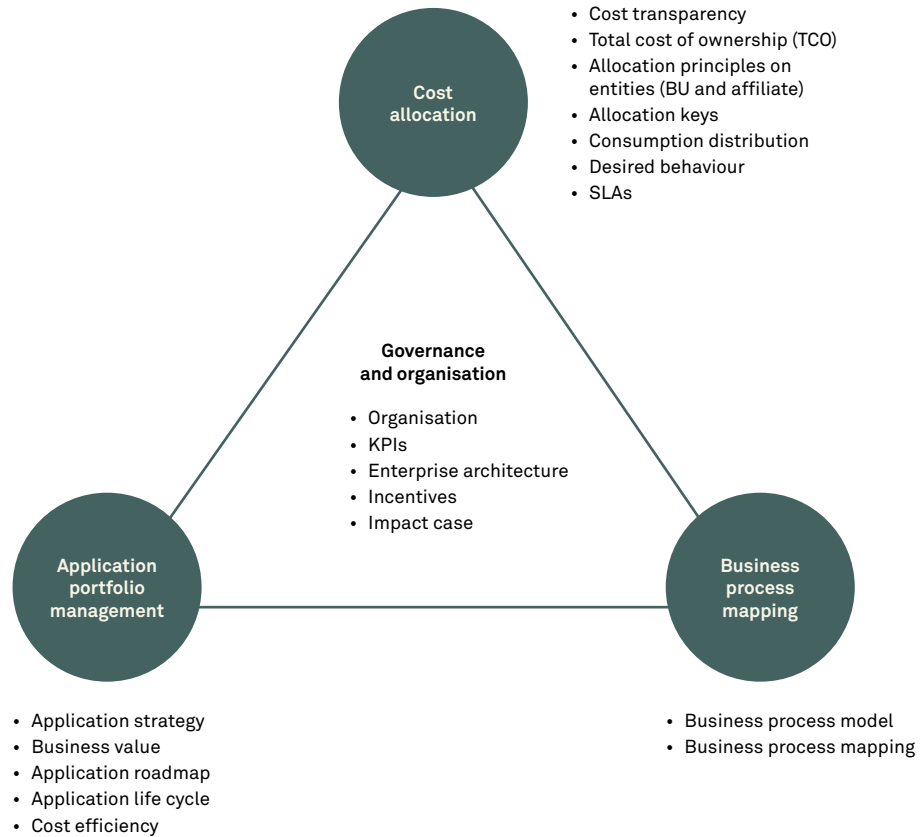


Figure 2 The cost allocation model

according to **business process** coverage and other factors. Finally, we will discuss key **governance** principles concerning business process and application design and development.

In the following section we will address the question:

?
HOW DO I CONTROL IT COSTS?

This Viewpoint focusses on IT projects and costs, while the interrelation between cost allocation, application portfolio management, business process mapping and governance is applicable to all types of business projects and the related expenditure.

Three cases are described in this Viewpoint, detailing situation and complications, cost allocation focus areas, methodology and process, business and behavioural impact and specific learning points from concrete projects.

Cost allocation

IT organisations are increasingly required to communicate the value of IT and how to reduce costs while maintaining quality and agility. As a result, IT organisations need more visibility with regard to the full costs of IT services to understand the cost burden placed on IT by specific business units.

The IT organisation must be positioned as a valued supplier of solutions and services and motivate (internal) customers (such as business units and affiliates) to actively participate in improvement projects and initiatives.

By better understanding how IT is used by various functions and business units (BUs), IT solutions and services can be more precisely deployed to meet changing business needs.

Implementing a system to track IT resource usage can generate significant benefits to IT and the organisation in general.

Benefits include:

- Better prioritisation of IT resources
- Closer budgetary control for early recognition of problem areas

- Stronger business cases allowing for more informed decisions when introducing new solutions and services
- More effective IT business partnership if the business understands how resources are spent
- Increased perceived value of IT, since IT will be seen as a strategic component of the business instead of a (simple) cost centre

The potential pitfalls include IT cost allocation imprecision due to complex models and implementation as well as irrelevance of IT cost allocation data if the pricing metrics of the cost allocation model cannot be mapped to current cost issues.

In the following section we will address the question:



HOW DO I STRUCTURE AN EFFECTIVE IT COST PRACTICE?

Cost allocation process

The process of analysis, development and implementation of cost allocation is described in this section.

The process contains eleven steps: Nine steps for analysis and development, and two steps for preparation of change approach and roll-out as well as implementation.

The process is not dependent on whether a chargeback, showback or a combined model is chosen.

In the following section the differences between chargeback and showback will be highlighted and cost categories and pricing models will be described.

Chargeback or showback

When embarking on a journey to define an IT cost chargeback model in an organisation, we need to clarify if a **showback** model or a **chargeback** model is required.

A **showback** model provides IT management, business units and group management with an analysis of the IT costs in each department without actually cross-charging the IT costs.

With a **chargeback** model, the IT department hands over a formal bill to their organisation's functions and business units to recover IT costs.



Figure 3 Components of the cost allocation

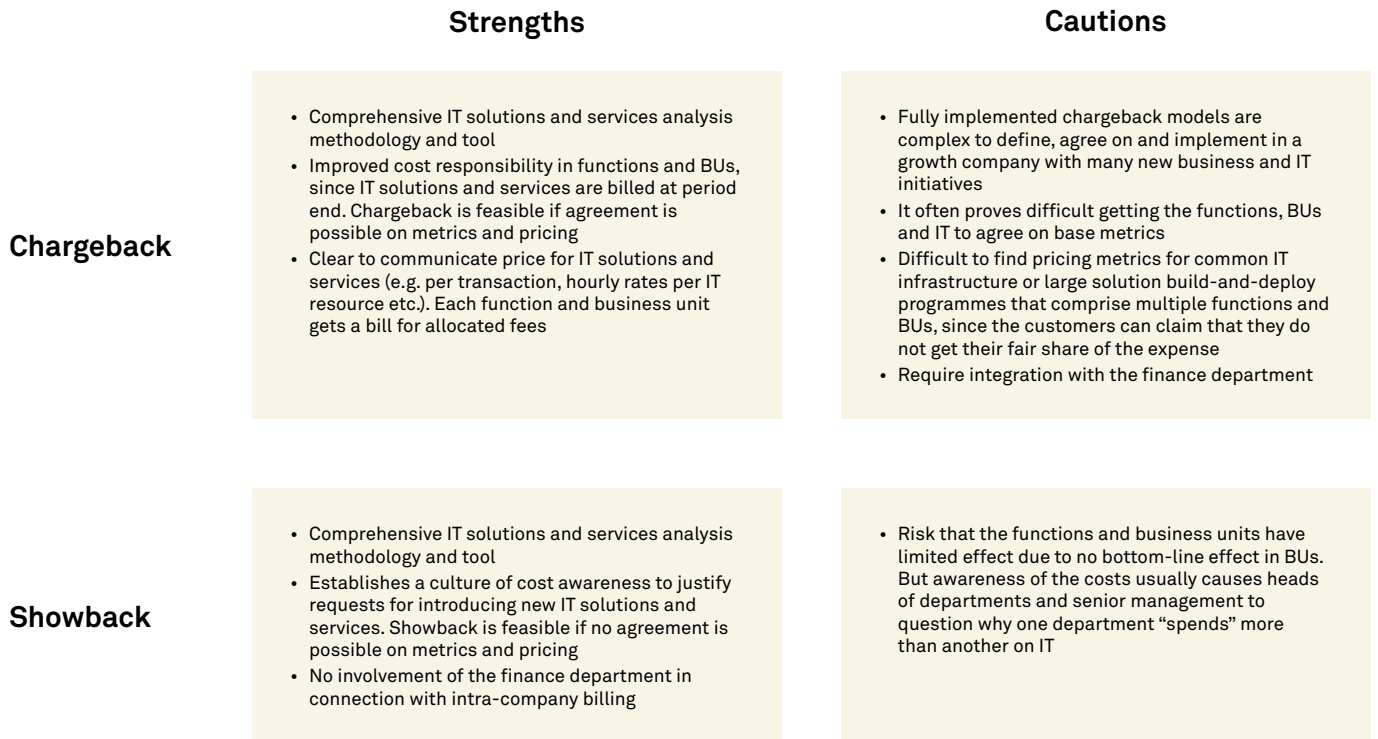


Figure 4 Chargeback vs. showback models

Sonia Lelii, 2012: "Showback vs chargeback: Showback new resource analysis tool of choice", SearchCloudStorage TechTarget



The strengths and weaknesses of the chargeback and showback models are described in figure 4.

In practice, a combined approach often may be relevant. For example during roll-out of a chargeback, it might be beneficial to start with a showback in order to mature the measurements and ease the implementation and likely resistance towards the change for a period of time before adopting the actual chargeback in the business units. Another possibility is that under-performing entities or business units immediately could have chargeback imposed in order to correct behaviour.

Other rationales might also drive the decision to pursue a combined approach, for example cost allocation based on chargeback in operations and cost allocation based on showback in project development and implementation areas of the business.

In the following section we will focus on IT cost allocation.

Cost allocation categories

Different cost categories for allocating IT costs may be allocated differently. Hence, it is important to identify the relevant groups of costs with the same characteristics.

Direct attribution. Application-specific IT costs and applications used in one BU and affiliate. These application-specific costs will be directly attributed to the one BU and affiliate using the application. Business unit and affiliate-specific application costs will be directly attributed to the business unit and affiliate in question

Allocation model. Application-specific IT costs and applications in scope for cost allocation used by multiple business units and affiliates.

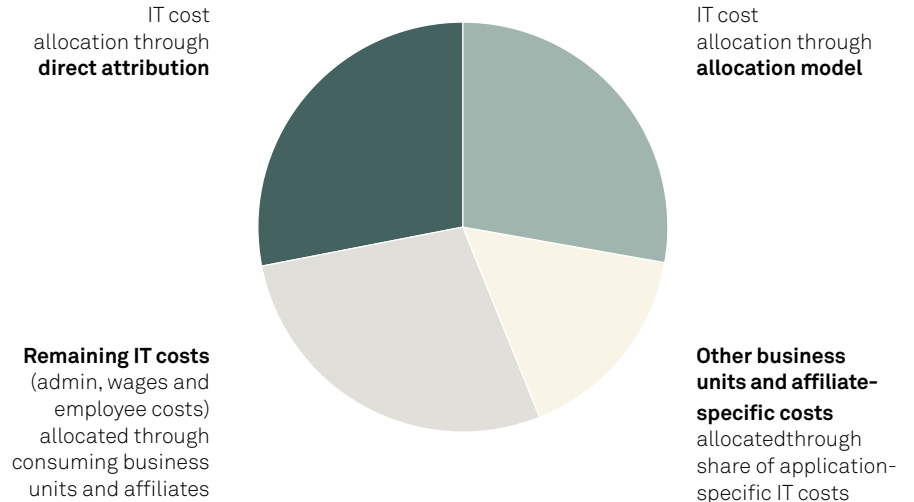


Figure 5 Cost allocation categories

Cost allocation keys can be defined and assigned to specific applications according to:

- Cost trigger
- Characteristic of application usage
- Geographical coverage
- Application strategy

Other business units and affiliate-specific costs. These application-specific costs will be directly attributed to the business units and affiliates using the application.

Remaining IT costs can be allocated based on the share of application-specific IT costs.

Designing chargeback models
As long as IT has a solid understanding of its operating costs, it can use pricing as a strategic tool for improving

alignment with the business by giving executives a better understanding and control of IT resources. Different models with different levels of service can be used for driving more cost-efficient consumption of IT and more effectively match services with business needs.

A number of different frameworks are publicly available to describe various pricing models. The standard base models for pricing IT value could be:

- Subscription pricing
- Peak-level pricing
- User-based pricing
- Ticket-based pricing

For more details on these four base models for pricing IT value, see appendix 1.

Application portfolio management

Application portfolio management is the process of rationalising and evolving the organisation's business application portfolio according to the organisation's strategic destination. Application portfolio management involves applying structured processes to evaluate business applications, determine issues or variations for defined standards and implement appropriate actions to resolve these issues. The objective of application portfolio management is to maintain awareness of the portfolio and to optimise life-cycle costs, quality, risks and value creation across all applications and integration assets.

Application portfolio management is driven by:

- IT strategy and architecture
- Business value and capabilities
- Cost efficiency

In the following section we will address the question:

HOW TO MANAGE THE PORTFOLIO OF PROJECTS AND BUSINESS APPLICATIONS?

The objective for organisations initiating application portfolio management work includes integration of all available application information, development and implementation:

1. Transparency through standard application portfolio (by business function)
2. Governance and maintenance process of standard applications and clear decision rules
3. Approval process of non-standard development requests

in order to

1. Reduce total cost of ownership (TCO) and optimise IT cost per user through application portfolio management
2. Provide flexibility, allowing the business to seize new opportunities

Current challenges in many organisations

Beginning with the end in mind is a critical success factor in the execution of application portfolio management. Thus, clear objectives need to be set in order to deliver an executable roadmap. By keeping the application portfolio management objectives in mind during the analysis, focus can be aimed at the details needed to achieve these objectives.

To many organisations, the situation today is:

- Multiple locations with own IT organisation and application landscape
- No integrated overview of the applications at every location

- Limited overview of coverage of business processes by application portfolio
- IT strategy towards implementing group-wide solutions

There are several reasons for focussing on application portfolio management. Getting a clear **understanding of the functionality of all applications** in each business unit and affiliate compared to the group-wide processes is important in **designing a roadmap for each business unit and affiliate** to plan the transition from the current situation to future IT application landscape. This **involves identifying "gaps"** if current applications do not provide sufficient support, and intermediate solutions are required to close urgent business issues. Usually, this also involves **providing solutions proactively** to close the gaps. In order to be able to monitor this process, it is important to **set up processes and KPIs**.

The benefits of developing a clear application portfolio management strategy and roadmap include:

1. Better alignment of IT with the organisation's business needs. It is critical for an organisation to have the "right technology at the right place at the right time".
2. Improved maintenance and operations planning. A key focus for organisations is to increase the return on investments (ROI) in IT solutions and technologies. Furthermore, better planning will also provide a better transition from legacy applications and technologies, which can lead to a reduced technical environment complexity.

Deriving business value from cost allocation and portfolio management

3. Enhanced enterprise application efforts. A clear application portfolio strategy and roadmap will provide a clear strategic view on all applications within the organisation and a clear understanding of current applications used in each business unit and affiliate in relation to group-wide functionality.

A coherent view of the application portfolio will ease the development of management, analysis and reporting capabilities, since the underlying data model and master data structures will be better mapped. Less duplication of work efforts will be a good side effect.

4. Establishment of data standards. The data standards defined across the organisation will lead to a reduction in costs for integration efforts in the long run and improved access to and sharing of data across applications.

Business value					IT strategy
Process coverage	Competitive advantage	Support for decision-making	Operational risks of failure*	Create value**	IT strategic position
1 = Supports parts of a single process	1 = Commodity or no competitive advantage Back-office systems – i.e. accounts receivable, billing etc.	1 = Not relevant to decision-making	1 = Limited effect on operations. Workaround available	1 = Supports outdated processes, very rarely used by a small number of users, other application (Excel) can do the job	1 = Architecture is out of support, programme often fails, uses old technology
3 = Fully supports one process or more than one subprocess across different processes	3 = Fast follower. Systems which provide competitive advantage by improving service, cutting costs and increasing the effectiveness of decision-making or the efficiency of operations	3 = Supports long-term decision-making or other sources available	3 = Business will stop within 2 to 5 days. Workaround available but cannot be sustained for a longer period of time	3 = Supports critical processes, delivers moderate cost savings/improvement of productivity	3 = Provides reliable and stable solution but not standard
5 = Supports two or more operational processes	5 = First mover advantage. Systems which deliver competitive advantages by creating new and unique products or services or by generating a significant cost or performance advantage	5 = Provides key input/support for strategic/tactical/operational decision-making process	5 = Business will stop within 1 day or will cause reputational damage	5 = Business immediately stops if the application is not available or provides competitive advantage/new revenue for the organisation or critical legal requirement	5 = New standard to be used for 5–10 years, flexible and reliable
15%	15%	25%	20%	25%	100%

Figure 6 Application classification parameters and criteria

* If periodic procedure (monthly/quarterly/yearly), consider worst-case scenario, i.e. failure at period end

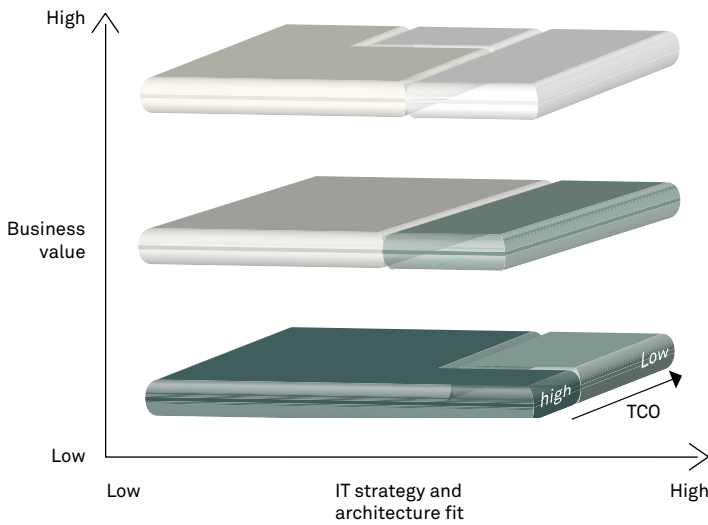
** Evaluated by CXO and key users

5. Increased visibility of IT spending. The application portfolio management effort will lead to a detailed analysis of the IT spend. A detailed cost view will lead to improved investment management decision-making, and an application consolidation as defined in a

roadmap can lead to an overall significant reduction in IT costs.

6. An IT governance and demand management model for managing all IT resources in the organisation needs to be developed.

7. Improved engagement with business units and affiliates in addressing all business requirements, irrespective of current installed base.



Portfolio evaluation dimensions

IT strategy and architecture fit:

- IT strategy alignment
- IT architecture alignment
- Technical efficiency (scalability, modularity, stability)
- IT security

Business value:

- Value related to business objectives
- Ability to execute
- Business urgency
- Risks

Total cost of ownership (TCO):

- Application life-cycle costs

Portfolio actions:

- Exploit
 Integrate
 Tolerate
 Migrate
 Eliminate

Application strategy	The application is classified within the following strategic categories
Exploit	Leverage fully on the application. Candidate for group standard
Integrate	Integrate/interface application with a group standard
Tolerate	Keep application in portfolio – only minor changes allowed
Migrate	Migrate application to a group standard
Eliminate	Application to be discontinued

Figure 7 Application portfolio management and evaluation – balancing the choices

Deriving business value from cost allocation and portfolio management

In order to be able to prepare a proper application portfolio analysis and roadmap, preparation of an inventory of all applications in use in the organisation is required (including key attributes per application). It is important that all applications are evaluated in order to determine:

1. The application's business value
2. How the application fits the organisation's IT-strategic position
3. The application's total cost of ownership (TCO)

The application's business value could be evaluated from a group perspective (see figure 6, page 10) based on: 1) process coverage, 2) competitive advantage, 3) decision-making support, 4) operational risks of failure, and 5) the application's business value evaluated from a business unit or affiliate perspective.

Furthermore, the application's fit to the organisation's IT strategic position is used for evaluating the technical platform, solution stability as well as the local and central support skills available.

Based on the application's business value, IT strategic position and the application's running costs (internal and external), it is possible to assess the application's development in the application portfolio.

These analysis activities lead to a shortterm/midterm classification related to the application life cycle: exploit, integrate, tolerate, migrate, eliminate.

Phase 1
1 – 3 months

- Inventory of applications in use and their key attributes
- Assessment of applications from business and technology perspectives
- Shortterm/midterm classification related to application life cycle: exploit, integrate, tolerate, migrate, eliminate, leading to a focus on group-wide processes
- Roadmap that outlines application portfolio rationalisation as a result of group-wide programme
- Establishment of governance model for managing IT resources in the organisation
- Improve engagement with BUs and affiliates in addressing all business requirements

Phase 2
6 – 9 months

- Implement an application portfolio management tool
- Update application portfolio roadmap reflecting new group-wide programme schedule
- Complete the assessment of the standard application portfolio from the business, technology and financial perspectives
- Support the implementation of controls
- Make the standard portfolio information available to BUs and affiliates for managing demands and identifying improvement opportunities
- Identify application gaps, overlaps and improvement opportunities outside the group-wide scope
- Recommended actions for each application (or application group) to realise improvement opportunities, leading to strategic focus areas

Phase 3
18 – 24 months

- A future-state application portfolio, application architecture and portfolio metrics against which to manage over time
- Roadmap that outlines and prioritises application improvement programmes (a multi-year schedule of initiatives to rationalise, reduce costs and increase overall value)
- Ongoing assessment of financial, staffing and process implications of completed projects

Figure 8 Deliverables from application portfolio management

Project costs (illustrative)

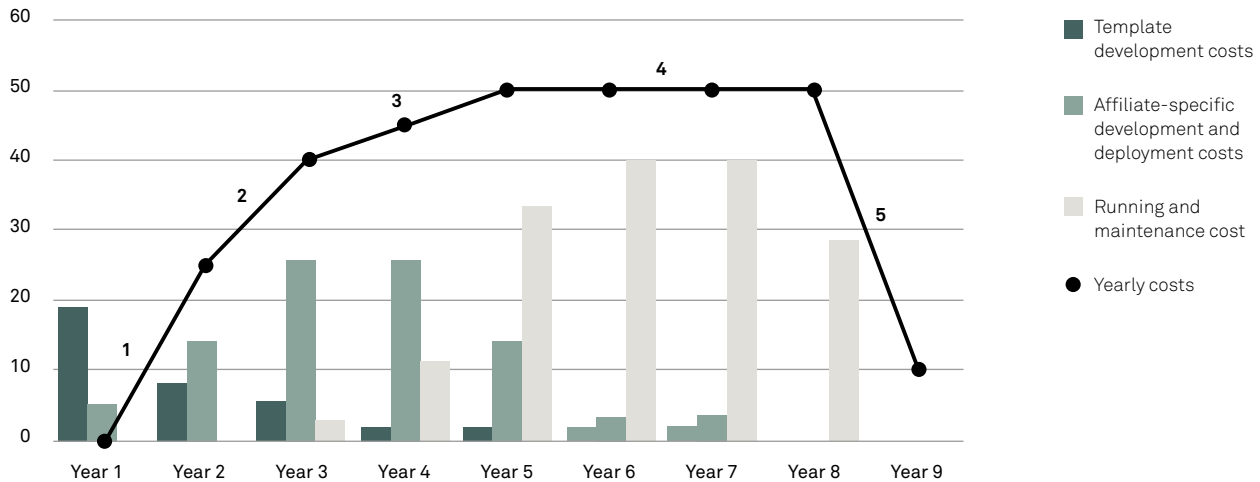


Figure 9 Project and application life cycle

Exploit. Applications with high business value, high IT strategic position and medium to low TCO could be leveraged in the organisation and be exploited as the group standard candidate for covering the business processes in question.

Integrate. Applications with high business value and low to medium IT strategic position could be considered for integration or interfacing with a group standard application. If the business value is lower, the applications could be considered for migration to a group standard application and the application could be eliminated.

Tolerate. Applications with medium business value that provides a high IT strategic position (reliable and stable solution that can be used several years into the future) could be tolerated, and the application could be kept in the application portfolio (with only minor changes allowed).

Migrate. Applications with medium business value and low strategic IT strategic fit could be considered for migration to a group standard application.

Eliminate. Applications with low business value, low IT strategic position and medium to high TCO could be considered for elimination. A plan for discontinuing the application should be prepared.

The implications are significant in case of e.g. acquiring a new business, since the IT merger activities to some extent will be dictated by the application roadmap of the acquiring organisation. The buying organisation will have a clear view of what solutions to offer newly acquired organisations.

When all applications have been classified according to the application life cycle, it is possible to start an evaluation of the rationalisation opportunities for the applications. A detailed

roadmap can be prepared, outlining the plan for application portfolio rationalisation (see example in figure 18).

What are the deliverables from a well-managed application portfolio management programme? As illustrated in figure 8, a series of outcomes are possible within the first 1 – 3 months, especially in relation to establishing a governance model for managing IT resources in the organisation, improving the engagement with business units/affiliates in addressing all business requirements and establishing application standards.

In the medium-to-long term (6 – 24 months), the application portfolio management programme can provide better alignment of IT with the organisation's business needs, increased visibility of IT spending and improved maintenance and operations planning due to the identification and exploitation of group-wide standard applications.

Project and application life cycle – and business unit/affiliate-desired motivation

A comprehensive understanding of the applications’ costs also provides valuable insight into the life-cycle costs and the effect on business unit and affiliate motivation for transitioning to/ from applications.

Figure 9 describes a typical cost profile for an application: starting out as a project with template development costs followed by business unit and affiliate-specific development and deployment costs and with yearly running and maintenance costs.

In order to ensure that the business units/affiliate have the right motivation to adhere to the group-wide application standards and follow their respective application portfolio roadmaps over time, an IT cost allocation methodology can be developed that motivates the desired behaviour of decision-makers.

Project phases and associated IT cost allocation methodology

Depending on the stage of the life cycle of the project and application, the following actions are likely to be taken:

1. All business units and affiliates should be actively involved in building a comprehensive group-wide template solution with integrated processes, master data standards and documentation
2. The pilot business unit and affiliate should adhere to the developed template functionality and limit the requests for affiliate-specific requirements (except country legal requirements)
3. Deployment business units and affiliates should adhere to the developed template functionality and limit the requests for affiliate-specific requirements (except country legal requirements)

4. All business units and affiliates should focus on the efficient performance of the standard solution and limit the requests for affiliate-specific requirements (except country legal requirements)
5. Ensure that business units, affiliates and IT are focused on a fast transition to the new solution

For further details on project phases and associated IT cost allocation methodology, see appendix 2.

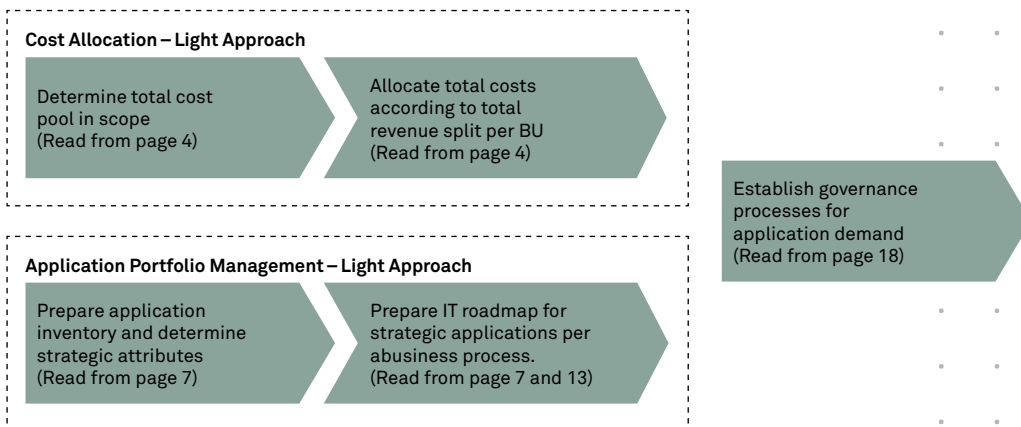
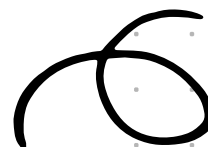


Figure 10 Light development approach



Business process mapping

In order to ensure a systematic analysis of business applications and their business process coverage, we propose performing a comprehensive mapping of all business applications for the business process/processes they currently support.

In the following section we will address the question:



HOW DO I ASSURE IT RESOURCE EFFECTIVENESS THROUGH EFFICIENT BUSINESS PROCESSES?

Business process mapping refers to activities involved in defining what a business unit or affiliate does, who is responsible, to what standard a business process could be completed and how the success of a business process can be determined.

The main purpose behind business process mapping is to assist organisations in becoming more efficient. A clear and detailed business process map allows the organisation to easier identify improvement opportunities for the current processes.

To ensure a **full view of the entire organisation's business process scope** as well as all involved business applications, it is recommended to proceed systematically:

- Prepare the organisation's application portfolio inventory (list of current applications)
- Map existing applications for all group-wide business processes. The applications' business process coverage could reach across all organisational dimensions, incl. business units, group functions, affiliates and countries
- Identify internal (business unit and affiliate) or external best practices to set a goal for future high-performing organisations
- Assign business process owner (from within the organisation) to all business processes
- Evaluate (and confirm) the group standard applications and the developed application roadmaps per business process
- Empower the demand management role (in the yearly budget process and ad hoc requests during the year) to guide requesters from group functions, affiliates and countries to request process and IT solutions from the portfolio of applications. This is to avoid "mushrooming" of non-standard applications. Follow a strict approval and governance process to ensure a well-founded business case
- **Plan deployment of group standard application in business unit and affiliate.**
If a business unit and affiliate currently do not have a business application supporting the execution of a business process, a deployment (exploit) of the group standard business application could be performed to ensure a broadened use of the application (to become truly group-wide for the business application) (see letter A in figure 12).
- **Plan implementation of new group-wide solution.**
If a group standard application is currently not in use in the organisation (see letter B in figure 12) – or if the business process currently is not supported by a business application (only supported by Microsoft Office tools) (see letter C in figure 12) – the organisation could plan for a new group-wide solution to be developed.
- **Plan continuous exploitation.**
When a group standard application is being used group-wide in the organisation to execute the designated business processes, a clear plan for process and performance enhancements must be formulated and executed (see letter D in figure 12). A drive towards world-class business processes and business applications is never-ending.

A complete and clear mapping of all business applications for the business process model will provide the organisation with insight into the following

Deriving business value from cost allocation and portfolio management

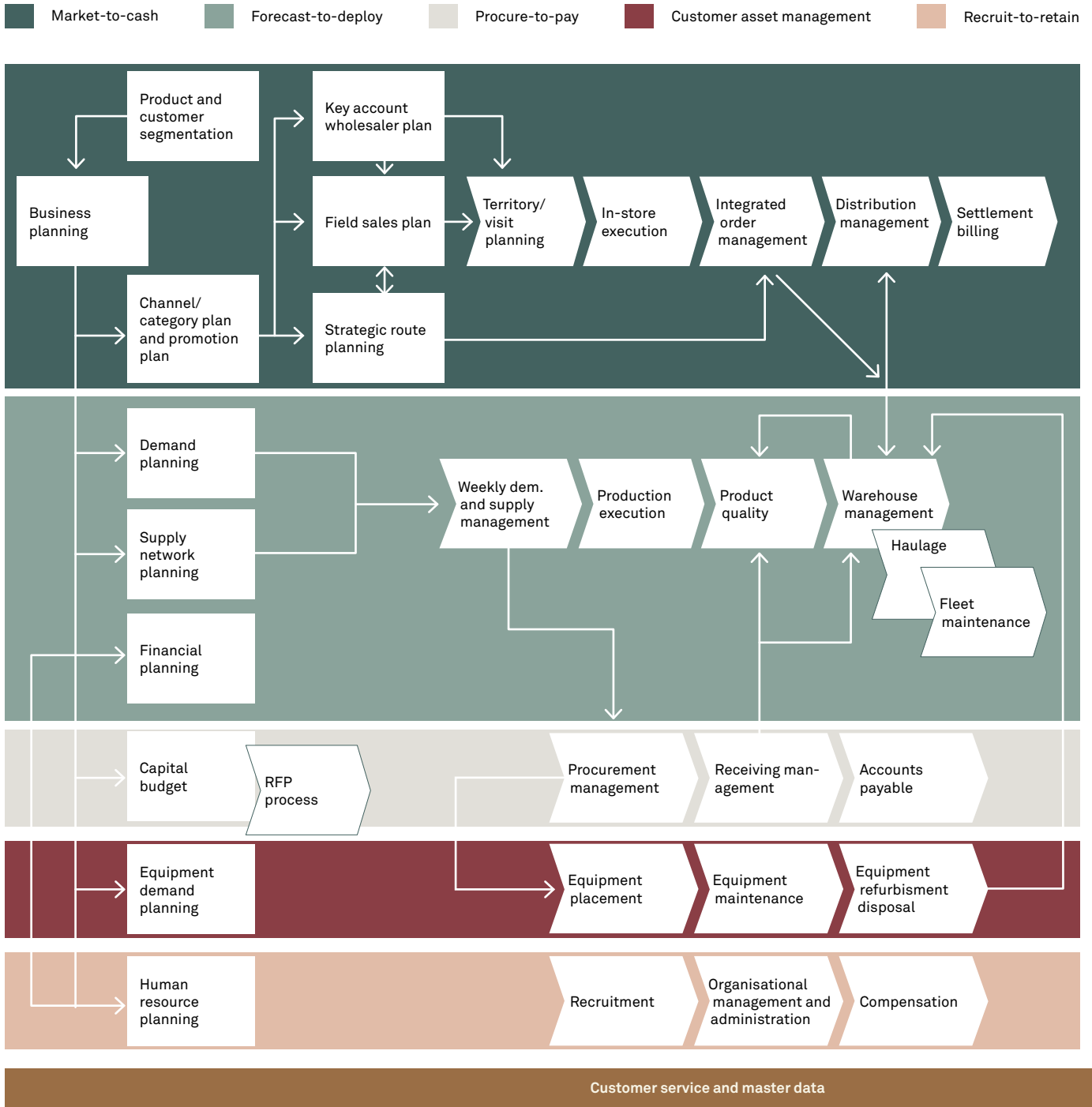
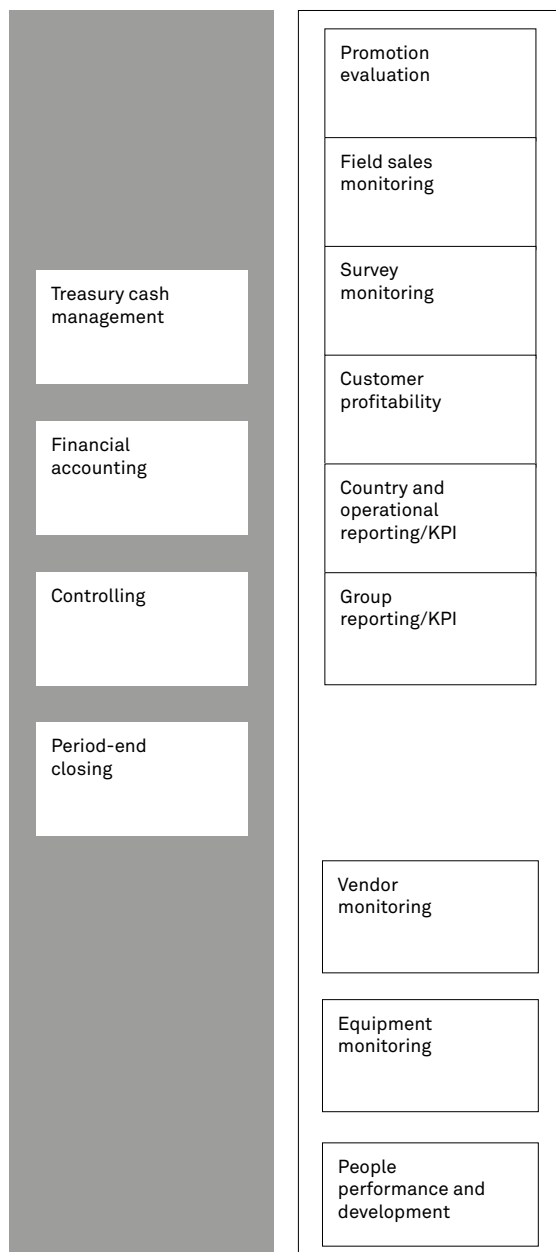


Figure 11 Business process model (BPM)

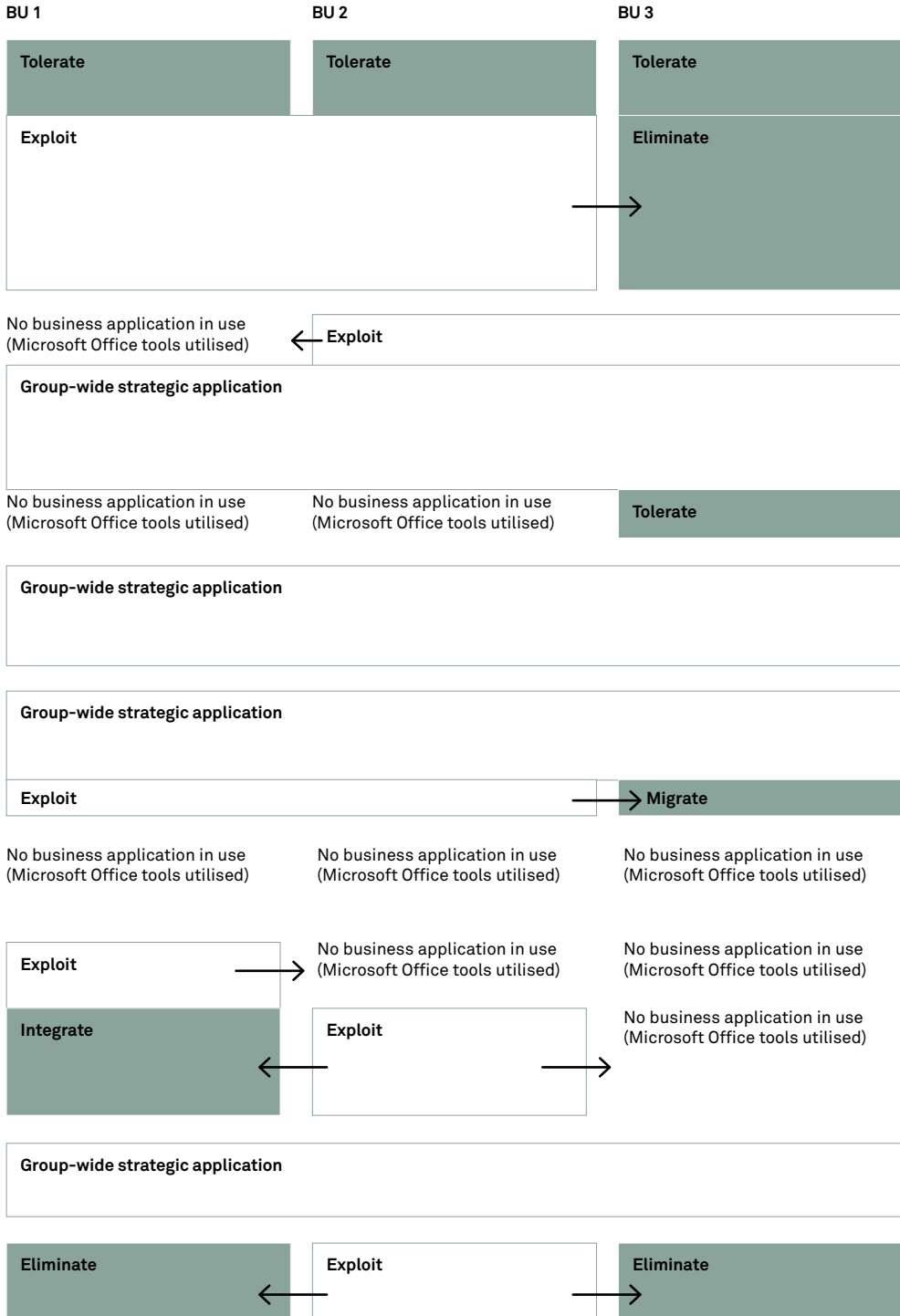
Finance management



MTC	Market-to-cash	BU1	BU2	BU3
MTC-010	Channel and category planning	✓		✓
MTC-020	Key account management			
MTC-030	Promotion management	✓	✓	✓
MTC-040	Strategic sales and distribution route planning			
MTC-050	Field sales management	✓	✓	✓
MTC-060	Integrated order management		✓	✓
MTC-070	Distribution management	✓		✓
MTC-080	Pricing management	✓		✓
MTC-090	Settlement and billing		✓	✓
MTC-100	Customer asset management	✓		✓
FTD	Forecast-to-deploy			
FTD-010	Business planning (3-year BP, ABP)	✓	✓	✓
FTD-020	Monthly planning – rolling estimate			
FTD-030	Integrated weekly demand & supply management	✓		✓
FTD-040	Production execution	✓		✓
FTD-050	Plant maintenance		✓	✓
FTD-060	Ensure product quality		✓	✓
FTD-070	Warehouse management	✓		✓
FTD-080	Haulage	✓	✓	✓
FTD-090	Fleet maintenance			
PTP	Procure-to-pay			
PTP-010	Vendor management	✓	✓	✓
PTP-020	Procurement management			
PTP-030	Receiving management	✓	✓	✓
PTP-040	Accounts payable	✓	✓	✓
FM	Finance management			
FM-010	Financial accounting	✓	✓	✓
FM-020	Controlling	✓	✓	✓
FM-030	Treasury	✓	✓	✓
FM-040	Period end closing	✓	✓	✓
FM-050	Corporate and management reporting	✓	✓	✓
HRM	Human resource management			
HRM-010	Organisational management			
HRM-020	eRecruitment		✓	✓
HRM-030	Personnel administration	✓		✓
HRM-040	Training and events management			
HRM-050	Compensation management	✓	✓	✓
HRM-060	Objectives setting and performance management	✓		✓
HRM-070	Personnel cost planning	✓		✓
HRM-080	Time management		✓	✓
HRM-090	Payroll			
HRM-100	Manager self-service	✓	✓	✓
HRM-110	Leadership pipeline (for example TOP 300)		✓	✓
MDM	Master data and data standards management			
MDM-010	Data standards management			
MDM-020	Master data maintenance	✓	✓	✓
MDM-030	Data distribution management	✓	✓	✓
MRK	Management reporting and KPI			
MRK-010	Corporate management	✓	✓	✓
MRK-020	Country management	✓	✓	✓
MRK-030	Operational	✓	✓	✓

MTC	Market-to-cash
MTC-010	Channel and category planning
MTC-020	Key account management
MTC-030	Promotion management
MTC-040	Strategic sales and distribution route planning
MTC-050	Field sales management
MTC-060	Integrated order management
MTC-070	Distribution management
MTC-080	Pricing management
MTC-090	Settlement and billing
MTC-100	Customer asset management
FTD	Forecast-to-deploy
FTD-010	Business planning (3-year BP, ABP)
FTD-020	Monthly planning – rolling estimate
FTD-030	Integrated weekly demand & supply management
FTD-040	Production execution
FTD-050	Plant maintenance
FTD-060	Ensure product quality
FTD-070	Warehouse management
FTD-080	Haulage
FTD-090	Fleet maintenance
PTP	Procure-to-pay
PTP-010	Vendor management
PTP-020	Procurement management
PTP-030	Receiving management
PTP-040	Accounts payable
FM	Finance management
FM-010	Financial accounting
FM-020	Controlling
FM-030	Treasury
FM-040	Period end closing
FM-050	Corporate and management reporting
HRM	Human resource management
HRM-010	Organisational management
HRM-020	eRecruitment
HRM-030	Personnel administration
HRM-040	Training and events management
HRM-050	Compensation management
HRM-060	Objectives setting and performance management
HRM-070	Personnel cost planning
HRM-080	Time management
HRM-090	Payroll
HRM-100	Manager self-service
HRM-110	Leadership pipeline (for example TOP 300)
MDM	Master data and data standards management
MDM-010	Data standards management
MDM-020	Master data maintenance
MDM-030	Data distribution management
MRK	Management reporting and KPI
MRK-010	Corporate management
MRK-020	Country management
MRK-030	Operational

Figure 12 Business process mapping




Application strategy

B. Tolerate & plan
A. Exploit
A. Exploit
D. Exploit & enhance
B. Tolerate & plan
D. Exploit & enhance
D. Exploit & enhance
A. Exploit
C. Tolerate & plan
A. Exploit
A. Exploit
D. Exploit & enhance
A. Exploit

Governance

As investments grow and become a larger share of an organisation's capital expenditure, IT management is required by senior management to demonstrate the business value and alignment of their investments as well as the reliability, availability, security, continuity and integrity of the information and supporting services.

In the following section we will address the question:



HOW DO I ENSURE A COMPANY-WIDE IT COST DIALOGUE?

Governing cost allocation is often set in the context of the organisation's general performance management and management control system.

Principles for achieving performance management and management control may include:

- Identification of critical success factors for the business and IT and identification of the KPIs linked to these factors
- Building KPIs into the organisation's performance evaluation system, starting at the top and permeating to all positions that can influence those KPIs
- Making KPIs relevant, simple, comparable, easy to report and focused on goals and objectives

- Defining and issuing a management control policy and related procedures which identify all of the areas requiring management controls
- Monitoring, auditing and ensuring that IT operations are in accordance with the approved controls
- Developing a risk management and mitigation plan, policy and process
- Developing a business/IT continuity and disaster recovery plan and policy
- Developing a clear performance review, escalation and issues resolution policy and process with clear accountability and responsibilities

Several management control systems are available.

The Balanced Scorecard system, developed by Kaplan and Norton, is a management system that provides a clear prescription as to what companies should measure to clarify their vision and strategy and subsequently translate them into action with respect to four areas: financial, customers, internal business processes and learning and growth. The scorecard objectives, measures, targets and initiatives could be cascaded down to business units, departments, processes and employees.

Control Objectives for Information and related Technology (COBIT) is a model designed to control and help audit the IT function. The framework has four domains, i.e. plan and organise, acquire and implement, deliver and support and monitor and evaluate, and the IT processes and controls are part of each domain.

The COSO model (Committee Of Sponsoring Organizations of the Treadway Commission) may be considered an enterprise risk management process with the purpose of being ready for the unknown. It is effected by an organisation's board of directors, management and other personnel, applied in strategy setting and across the enterprise, designed to identify potential events that may affect the entity and manage risk to be within its risk appetite, to provide reasonable assurance regarding the achievement of the objectives of the entity.

In order to govern new business activities, an effective definition and delivery cycles on a project portfolio, programme and project level have to be established. Such a setup will ensure establishment of a structure for selecting the right programmes and projects for the organisation, ensuring ongoing alignment of programmes and projects with strategic objectives, assessing whether new requirements can be accommodated within the existing organisational capability, capacity and maturity, relate cost allocation to sourcing process for CAPEX and allocate the right resources to the right programmes and projects to ensure ongoing delivery.

The governance of a cost allocation project is very similar to a traditional project with regard to project owner, steering committee, reference group etc.

However, in setting up the organisation for the project and the operational team, certain roles and tasks ought to be considered.

In figure 13, the governance roles that are relevant to the organisation are listed.

What/role	How/task	When/frequency
Allocation model owner	Determine year plan. Coordinate with stakeholders. Determine KPIs.	Ongoing
Maintenance responsibility	Update costs from budget/actual cost splits and market dialogue. Update allocation keys. Future enhancement of the IT cost allocation model.	Quarterly (or more frequently, if necessary)
Responsible for application portfolio management	Update application portfolio and details relative to IT landscape and operations. Set application portfolio actions and roll-out scope.	Ongoing
Demand manager	Facilitate the annual/ad hoc requests for new applications and solutions.	Annual/ad hoc
Responsible for business process	Engage in dialogue with requesting functional department for identification of ideal application/solution to address business needs.	Ongoing
Responsible for business system	Partner with business process responsible and Group IT to ensure the identification and implementation of the ideal application/solution to address business needs.	Ongoing
System enthusiast	Apply allocation model. Update/create graphical presentations.	Quarterly (or more frequently, if necessary)
Challenger	Analysis of allocation results and pose questions to challenge the status quo.	Quarterly (or more frequently, if necessary)
Responsible for relationship	Demand management dialogue with internal stakeholders.	Ongoing

Figure 13 Governance roles

What is next?

5 actions for your organisation

There is a clear relationship between cost allocation and cost awareness, application portfolio management and business process mapping. Furthermore, it is critical to have the right governance and organisation in place to ensure cost-effective applications in a robust and future-safe application portfolio that satisfies business needs as well as an agile governance of the portfolio of application and process enhancement initiatives underway in the organisation.

In order to ensure an effective cost allocation, definition of an optimal application portfolio roadmap for your business applications and establishment of a proper governance structure and procedures in your organisation, you need to consider the following five actions:

1. See cost allocation, application portfolio management, business process mapping and governance as an integral part of good management principles and make sure that all initiatives are coordinated and interrelations are properly planned (see figure 15).
2. Review the organisation's current cost allocation practices and evaluate if the required cost transparency is in place and all group functions and affiliates have the desired level of information to guide their desired behaviour.
3. Create inventory of all business applications to conduct a complete review of the application portfolio and stay true to the application roadmap in all budget cycles and all demands from the business for new processes and IT solutions.

4. Establish a demand management role to govern all future demands for new processes and IT solutions to ensure that all requests are in line with the application roadmap and with a solid business value.
5. Decide on showback or chargeback cost allocation model. Plan and initiate project.

Summing up, the overall structure and logic of this Viewpoint has been incorporated into figure 14:

- Effective control and execution of the cost allocation process provide cost transparency for a comprehensive application portfolio management and definition of a clear application strategy and roadmap for all business applications.
- The application roadmap and strategy will lead to improved business process execution and a continuous focus on process improvements, application consolidation and a reduction in total cost of ownership.
- Efficient demand management is instrumental in realising the improvement of cost effectiveness and cost awareness.

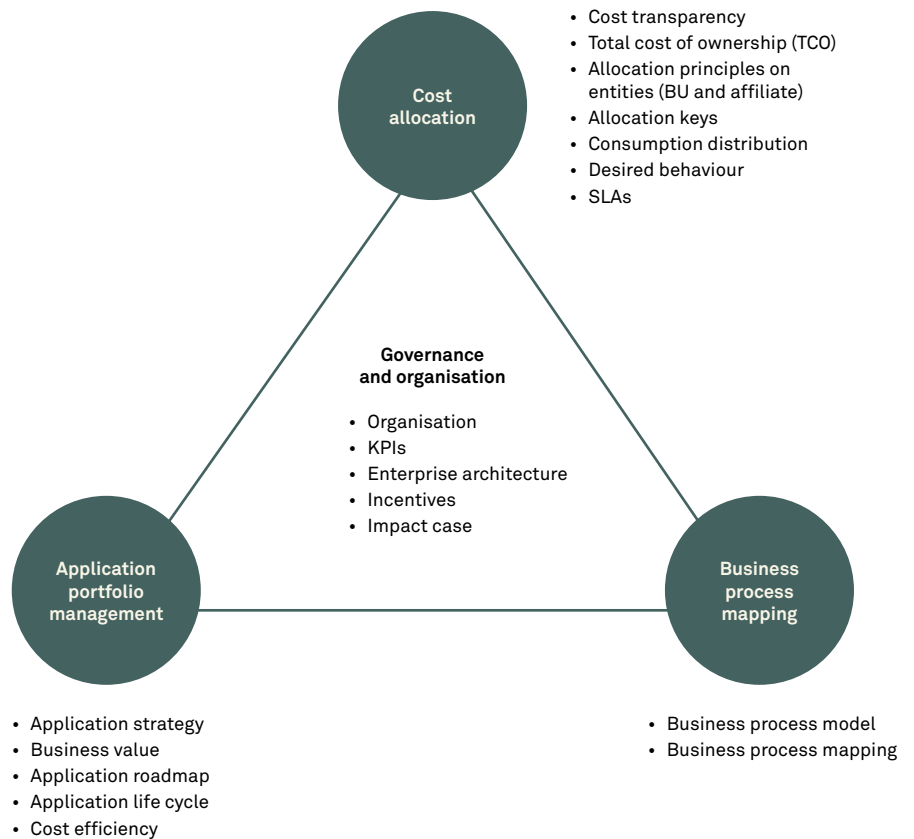


Figure 14 The cost allocation model

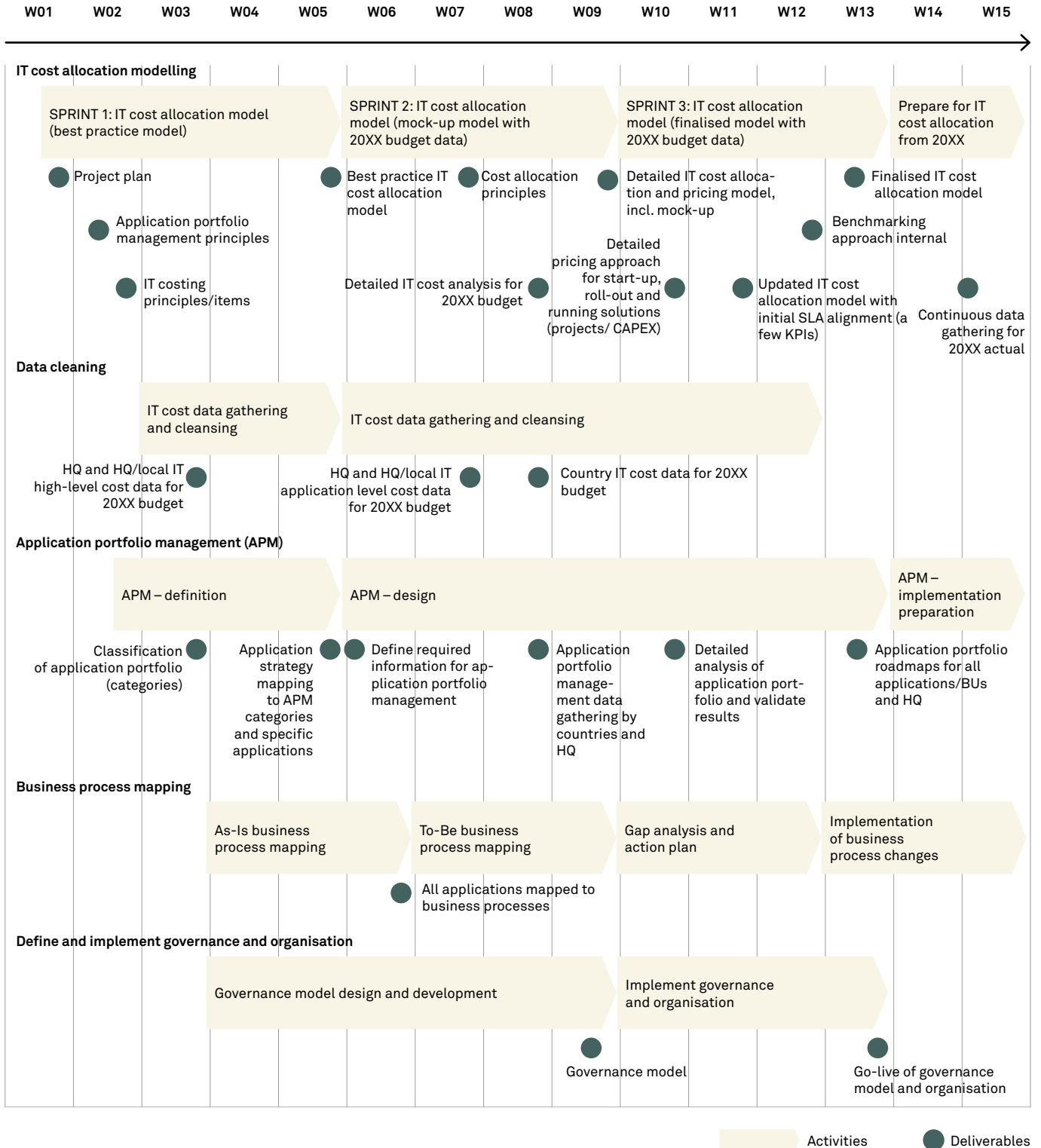


Figure 15 Detailed phase planning

Case: A growth organisation

Situation and complications

The organisation is a fast-growing organisation which successfully has expanded its presence in key markets such as the US and the UK. In spite of several years of strong growth, the organisation has recently experienced a slowdown in growth. Hence, the organisation is realigning global strategies to counter this.

In the process of changing focus from top line to bottom line, the IT department, Group IT, is consolidating the IT landscape and optimising the cost structure.

Traditionally, a large proportion of the IT spend was requisitioned locally and paid for centrally. It was assumed that this asymmetric cost structure between the centralised IT function and the local business units could be optimised.

Cost allocation focus area

The cost allocation focus area was on verifying and visualising the business impact of cost allocation efforts.

The project aimed at improving IT cost effectiveness and facilitating the organisation's capability and practices on IT cost awareness.

Methodology and process

To a large extent, the project followed the process illustrated in figure 15.

As part of an IT business unit cost allocation project, Implement identified a series of KPIs to provide insight into the analysis of current IT costs for Group IT and affiliates. These KPIs were calculated based on provided data.

Business and behavioural impact

The project identified business as well as behavioural impact elements as proposed by the impact case concept (see figure 16).

For future continuous analyses of IT costs, additional KPIs can be added to provide insight into the desired behavioural aspects of the IT cost awareness and reporting.

Furthermore, there are significant advantages in building easy-to-use reporting for further automated data mining.

The gross list of KPIs, which was later limited to a handful of KPIs, is illustrated in figure 16.

Moreover, follow-up and update frequency was determined as quarterly.

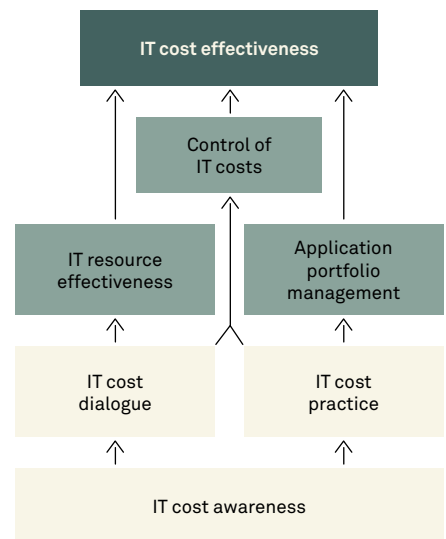
Learning points

This case provides several clear learning points:

- By actually introducing a cost allocation model in the cost control and reporting structure, Implement ensured that the topic was debated in the organisation
- KPIs have to be balanced and chosen carefully. The visual impact board figure highlights some of the considerations that need to be discussed before selecting specific KPIs

Objectives

Impact map



Ce

Figure 16 Visual impact board

- The costs of a new IT user, when considering the full allocation, might be significantly higher than the internal pricing of a new IT user
- Business units related to market support and production functions are not necessarily directly comparable to the revenue-generating business units
- Headquarter costs (IT costs per IT user) are likely higher than average due to 1) centralisation of activities and 2) a high number of ERP users.

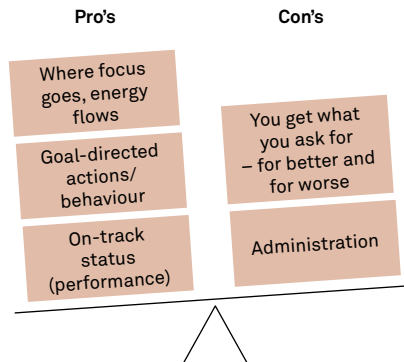


Figure 17 KPI considerations

Impact measurement

Impact objectives	KPI/measure	Baseline	Target	Q1 – Q4 20XX
Business impacts:				
IT cost effectiveness	• Total IT costs as percentage of total revenue	-	-	-
Control of IT costs	• Total IT costs per IT user	-	-	-
IT resource effectiveness	• IT wages and employee costs as percentage of total IT costs • IT costs as percentage of total administrative costs	-	-	-
Application portfolio management	• Number of applications per portfolio action • Number of applications in use from APM list	-	-	-
Behavioural impacts:				
IT cost awareness	• Application and country-specific IT costs as a percentage of total IT costs	-	-	-
IT cost practice	• Percentage of applications with full TCO details	-	-	-
IT cost dialogue	• Percentage of IT costs in affiliate budget vs. Group IT ("showback percentage") • Percentage of country IT costs compared to share of total revenue	-	-	-

Case: A large global organisation

Situation and complications

The organisation had a very complex IT landscape with multiple ERP systems, other business applications (> 1,000 applications) and a geographically dispersed application portfolio (> 25 countries). The organisation decided to implement a full ERP (SAP) solution to cover nearly all business processes and all geographical locations.

Furthermore, in an effort to consolidate the application coverage of all business processes, the organisation decided to undertake an application portfolio management effort to drive down application costs.

Cost allocation focus area

The analysis of total costs was performed during the evaluation of each application's business value estimation and IT-strategic fit. The cost analysis included both:

- Development
- Maintenance and running costs

A full application portfolio management review and implementation in concrete initiatives were performed in the organisation, and a strict governance process (through demand manager, business process and business systems leadership) was implemented.

Methodology and process

The organisation defined a clear approach involving Group IT's strategy department, affiliate IT representatives and Group Finance to ensure inventory, evaluation and strategic decision-making for all business applications in group and/or affiliate use.

Specific evaluation criteria to determine business value and IT-strategic fit were agreed, and comprehensive strategies per group function and affiliate were developed in the form of application roadmaps (see figure 18).

All future application demands will be handled by Group IT's strategy department's demand manager and will be treated in accordance with the application portfolio management methodology, application life cycle and based on a detailed business case.

The organisation established specific roles for business process and business system leaders that had clear ownership of the process and system aspects and could provide the guidance to the business for the right solution to be implemented to satisfy specific demands.

Business and behavioural impact

The focus on business process coverage, strategic IT fit and total costs of applications had a positive effect on the organisation's performance on the KPI "Total IT costs as percentage of total revenue", indicating that IT costs diminished relative to total revenue over the years in question. The organisation also performed well on this parameter compared to the industry (benchmarking).

Furthermore, the clear approach to endorsing group-wide solutions with high business fit and best strategic IT fit has resulted in more requests for applications among the accepted group-wide applications and less demand for non-standard solutions.

This enforces the IT strategy of the organisation to limit the total number of applications and avoid "mushrooming" of non-standard applications.

The application portfolio management approach also had the considerable benefit that all group functions and countries had easy access to information on all group and affiliate applications and had a clear recipe for requesting new solutions in accordance with the organisation standard.

The organisation focused on cost effectiveness and application portfolio optimisation for several years prior to this initiative, but the organisation needed time for the integrated concept to mature and settle. What made the step change in the organisation – and what proved that the methodology was effective:

- Organisation was in place – business process and business system leaders, demand manager etc.
- Strict cost control
- Business case mentality for all application acquisitions and enhancements
- Senior management focus

Learning points

Several clear learning points can be drawn from this case:

- Development of detailed application portfolio review and the setup of application roadmaps for all group functions and affiliates

- Central review of all application costs (TCO perspective) and tracking over time of all cost variations
- Overall application life-cycle management responsibility within Group IT's strategic services function
- Establishment of demand manager, business process and business system ownership to provide optimal guidance and leadership on all business process and system application solutions in the demand management process (in the yearly budget process and ad-hoc during the year)
- The initiative was not a quick implementation with quick short-term wins. It is a process that will lead to other changes in the organisation.

		Year 1	Year 2	Year 3	Year 4	Year 5
Total applications	Active	338	54	44	47	47
	Being replaced	0	282	72	3	2
	Dismissed	0	2	222	288	289
	Tbd	4	4	4	4	4
	Total	342	342	342	342	342

Application	Area	Year 1	Year 2	Year 3	Year 4	Year 5
Application	Commercial	Exploit	Exploit	Exploit	Exploit	Exploit
Application	Commercial	Exploit	Replace	Historical transaction	Eliminate	Discontinued
Application	Commercial	Exploit	Replace	Eliminate	Discontinued	Discontinued
Application	General	Exploit	Exploit	Exploit	Exploit	Exploit
Application	General	Tolerate	Replace	Historical transaction	Eliminate	Discontinued
Application	Info	Exploit	Replace	Historical transaction	Eliminate	Discontinued
Application	Supply chain	Tolerate	Replace	Eliminate	Discontinued	Discontinued
Application	Commercial	Tolerate	Replace	Eliminate	Discontinued	Discontinued
Application	Commercial	Tolerate	Migrate	Eliminate	Discontinued	Discontinued
Application	Commercial	Tolerate	Migrate	Eliminate	Discontinued	Discontinued

Application	Year 1	Year 2	Year 3	Year N	
Application	12.000	12.000							Benefits: <ul style="list-style-type: none"> • Value for money – more/better for less • Centralisation and consolidation of the BUs and affiliates' IT • Standardisation of IT services • Consolidation of application types • Transparency of IT costs
Application	20.000	20.000	20.000	20.000					
Application	15.000	15.000	15.000	15.000	15.000	15.000			
Application	10.000	10.000	10.000	10.000	10.000	10.000	10.000	10.000	
Application	30.000	30.000	30.000	30.000	30.000	30.000	30.000	30.000	
Application	25.000	25.000	25.000	25.000	25.000				
Application	18.000	18.000	18.000	18.000	18.000				
...						
Application	22.000	22.000	22.000						

Figure 18 Application portfolio roadmap (example)

Case: A Nordic multi-affiliate organisation

Situation and complications

The requirements of the organisation were to:

1. Define and implement a comprehensive cost allocation model for collecting and allocating all IT related costs
2. Prepare detailed invoicing to all group functions and affiliates utilising the Group IT services
3. Provide full cost insight into all application costs for IT cost optimisation purposes
4. Document all processes for internal audit and ensure cost transparency through the entire model (from initial registration through cost pooling to system owner in group functions or affiliate)

Cost allocation focus area

The development and implementation of a full cost allocation model had the primary focus to provide the invoicing base and justification of allocating all the organisation's IT costs to the system owners.

The overall owners of the IT cost allocation model is Group Finance, while users of the cost allocation model includes Group Finance, Group IT – and for reporting purposes also the group functions and affiliates.

Methodology and process

Before initiating any build activities, a detailed analysis of all registrations, required information flow, potential allocation keys as well as the desired end result and invoicing details were developed in flow charts in collaboration with Group Finance, Group IT, stakeholders and the project team.

Based on the detailed information flow (see figure 19) required for the complete and correct allocation of IT costs, a detailed, integrated process flow was developed to provide insight into the roles and responsibilities and interconnected processes between Group Finance, Group IT and the group functions and affiliates.

A key element in the cost allocation modelling was to exclude actual measurable consumption levels from the allocation logic. An example was server usage by specific solutions. Instead of allocating a large total cost of servers across all server-using applications, it was decided – in collaboration with the organisation's hosting partner (third party) – to provide detailed server usage information. In this way only solutions using the specific individual servers should cover the costs of the specific servers.

A governance structure was implemented to ensure the correct processing and approval of the allocated IT costs and to ensure adherence to internal audit requirements.

Business and behavioural impact

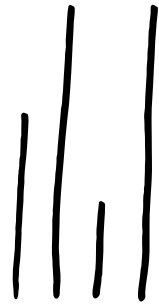
The IT cost allocation model has a series of significant business and behavioural inputs in the organisation:

- One common costing model to be used by multiple business units and stakeholders providing “a single version of the truth”
- Total transparency in cost allocation basis, allocation logic and invoicing value towards internal audit
- Total cost view of all business applications for better decision-making
- Better day-to-day collaboration between Group Finance and Group IT
- Higher degree of acceptance from the group functions and affiliates regarding the invoicing details and amount provided by Group Finance
- A clear separation of cost allocation and customer-specific consumption of IT services and solutions

Learning points

The learning points from the organisation are the following:

- Design with the end in mind – and build only when all information flows, user interfaces, data sources and reporting/invoicing details are known and cleared with all stakeholders and approved by the governing body. Cost allocation models can be very flexible to develop – but very difficult to alter if new requirements are identified during the development phase



- Work collaboratively with all key stakeholders. Co-creation ensures a more comprehensive and detailed analysis of cost allocation needs and a more complete fit with the requirements
- Ensure a close cooperation and dialogue with internal audit to ensure that the cost allocation model follows all rules and regulations, incl. rules covering transfer pricing and transparency

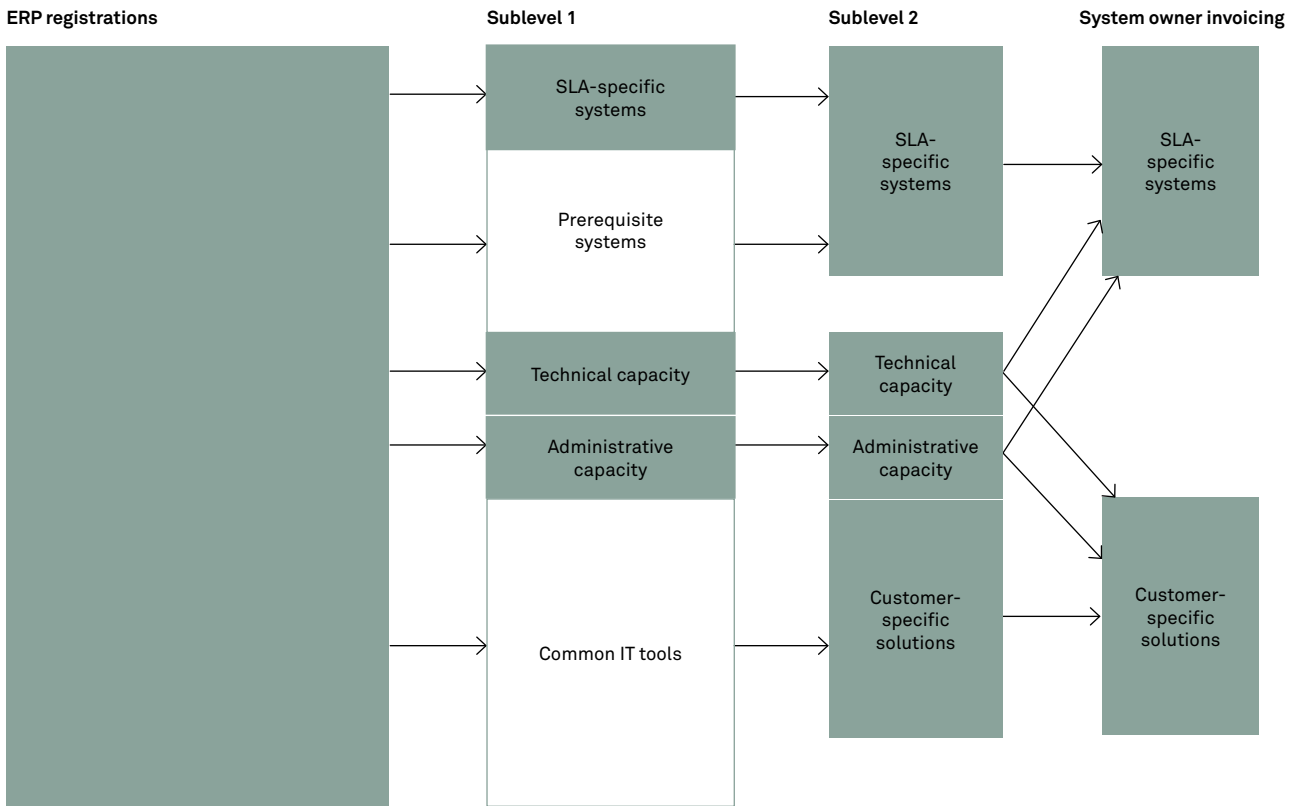


Figure 19 Cost allocation information flow

Appendix 1: Pricing models

Pricing models

Model	Description	Advantages	Disadvantages
Subscription pricing	<p>Subscription pricing is a pay-per-use model in which pricing is per unit of time, which is much easier to monitor and measure than consumption-based pricing.</p> <p>The operational cost of the IT facilities is calculated and amortised across a subscription period (e.g. one year) and then divided between all the users of the service.</p> <p>Depending on the operating profitability goals applied to the IT organisation by the business as a whole, an element of gross margin may be added – perhaps to create a pool to fund future projects.</p>	<p>Simple: If e.g. 5 BUs were subscribing to a service that costs 600,000 per month to provide, the subscription charge (assuming a break-even business model) would be $600,000/5 = 120,000$ per business unit per month.</p>	<p>No usage monitoring or penalties: It assumes that all parts of the business will use the service at the same level on a constant basis with no penalties for excessive consumption or peak-time usage.</p> <p>No cost justification: There are not any metrics by which the actual level of consumption can be measured, calculated and justified to sceptical consumers.</p>
Peak-level pricing	<p>The peak-level approach takes the subscription model and adds a mechanism to monitor and record peak consumption. Consumers are billed according to their peak use, not according to their average use.</p>	<p>Simple to meter: Only peak-level usage needs to be monitored and recorded.</p> <p>Clear cost justification: Easy to show when consumers are using more than the base level resources.</p>	<p>Penalises variability: If there are just a few peaks of usage during a given period of time, the scheme can seem unfair. But shortening the analysis period (e.g. from six months to one year) and the measurement intervals (e.g. from weekly to daily basis) can solve the problem.</p>

Figure 20 Pricing models examples

Source: Mark J. Denne, 2007: "Chargeback demonstrates IT value in the enterprise", CIO.COM

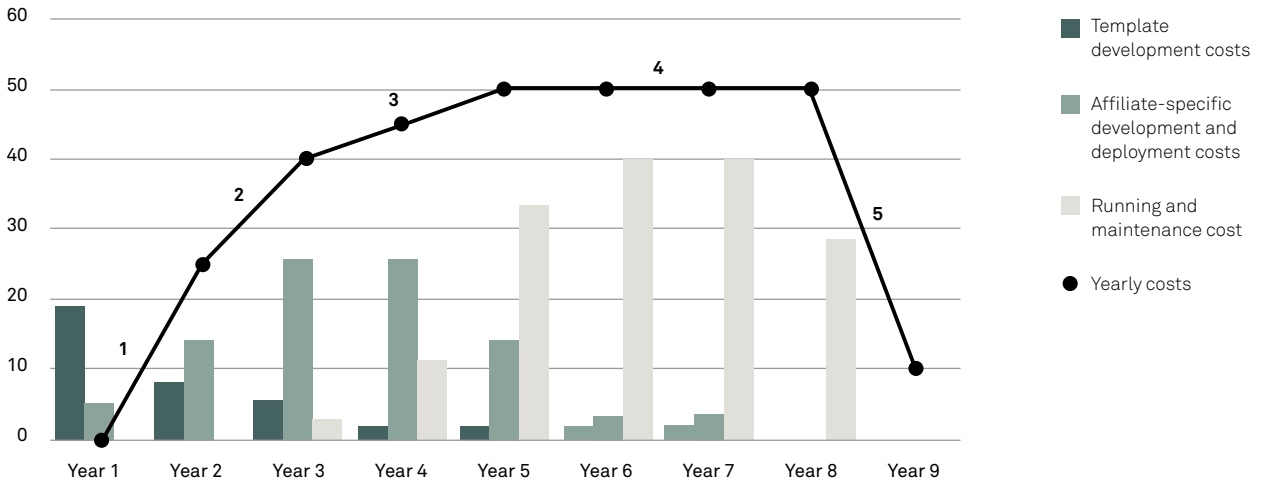


Pricing models

Model	Description	Advantages	Disadvantages
User-based pricing	If user management is a bigger cost issue for IT than hardware usage, it makes more sense to meter IT by the person rather than the device. If users are connected to their computers for fairly similar periods of time and have relatively well-understood transactional profiles (e.g. bank customer service representatives who work on web portals), this can be a fair and easy way to charge for usage.	<p>Easy to implement: Tracking the authentication of individual users to IT services is relatively simple, especially if a single sign-on system is in place.</p> <p>Clear cost justification: The authentication records provide the basis for cost justification.</p>	Ignores system load: If users make heavy demands on systems when they log on, this model short-changes IT.
Ticket-based pricing	In IT environments where quality of service is critical, IT can meter and control usage very tightly using electronic "tickets" that use a short validity period (e.g. 4 hours).	<p>Consumption regulation: Ticket-based pricing lets IT control system load to a fine degree, helping to eliminate usage peaks and ensure business continuity.</p> <p>Simple: All that is required to monitor ticket pricing is a ticket portal.</p> <p>Strongest cost justification: Of all the models, ticket-based pricing is the most powerful in terms of cost justification.</p> <p>Pinpoint monitoring: Tickets can be very specific, allowing both sides to monitor exact usage down to the specific application level.</p>	Ticket hoarding: For the ticket-based model to operate effectively, it is often necessary to implement "use-by" dates on tickets to avoid stockpiling.

Appendix 2: Project life cycle

Project costs (illustrative)



**1. Definition and design phase
– template development
(not affiliate-specific)**

- A detailed business case should be developed, estimating total analysis, definition and design effort for the solution template according to solution scope
- All intended affiliates should participate in the business case template solution development
- Cost allocation:
 - Template development: Cost allocation based on number of estimated application users per BU and affiliate in full operations state

2. Pilot affiliate deployment

- The pilot deployment will lead to affiliate-specific legal/local requirements development as well as improvements to the solution template
- Cost allocation:
 - Affiliate-specific developments: Increased cost allocation fully attributed to requesting affiliate
 - Template enhancements: Cost allocation based on number of estimated application users per BU and affiliate in full operations phase.

3. Full deployment to all intended affiliates

- The full deployment will lead to affiliate-specific legal/local requirements development as well as improvements to the solution template
- Cost allocation:
 - Affiliate-specific development: Increased cost allocation fully attributed to requesting affiliate
 - Template enhancements: Cost allocation based on number of application users per affiliate in full operations state

4. Operations (run) phase for all intended affiliates

- The solution is fully deployed and maintenance releases are implemented with regular releases
- Cost allocation:
 - Run elements: Cost allocation according to application's cost trigger (i.e. number of IT users, user licences, transactions etc.)
 - Enhancements: 1) enhancements to the template solution (with functionality that benefits all affiliates), all IT costs should be included in the total cost pool for allocation according to cost trigger, 2) affiliate-specific enhancements to be fully attributed to requesting affiliate.

5. Retirement

- When a new strategic solution – that will replace the retiring solution – has been developed and stabilised, it is vital that all affiliates plan a fast transition. The result of slow-moving behaviour from the affiliates side is that the remaining affiliates will bear a higher portion of IT costs. In case of slow-moving action from IT, it is fair to assume that Group IT will cover the IT costs not specific to the remaining affiliates (i.e. the remaining affiliates keep paying as in phase 4 “operations (run) phase”
- Cost allocation:
 - If indecision by affiliate, run elements: Cost allocation according to application's cost trigger (i.e. number of IT users, user licences, transactions, etc.)
 - If indecision by IT, run elements: Cost allocation towards BU's and affiliate equal to fee in phase 4 “operations (run) phase”
 - Enhancements: Affiliate-specific enhancements to be fully attributed to requesting affiliate.

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