THE CIO AS ENTREPRENEUR

Efficient customised usage concepts
for agile business models

Efficient Technology Management®

Perspective

When we talk about digital transformation today, we mean groundbreaking strategies, radically new business models and disruptive use cases. However one fact is often lost in the wake of this upheaval, namely that digital transformation also requires a digital infrastructure within companies. The number of PC workstations, mobile devices, storage media and applications continues to grow. Their technology lifecycles are becoming ever shorter and more opaque. As a result, agility and the minimisation of risk when providing this infrastructure are key success factors – for both CIOs and CFOs.

The procurement, management and administration of assets, as well as the accounting treatment of IT investments, need to keep pace with processes in a company's core business. At the same time, cost control and cost reduction remain the dominant issues if business models and use cases are not to be thwarted by excessive expenses.

This white paper explains why common delivery models for IT infrastructure fail to provide the agility that companies require. It shows how greater transparency, flexibility and cost control become possible when IT assets and services are unbundled, while business interruption risk and accounting risk are eliminated. And it explains how the role of the technology manager, which manages financial services and contracting independence of providers, is the way to achieve this objective.

"CIOs and CFOs have strong common interests in the delivery of IT services: more transparency, fewer costs and less risk."

End-to-end outsourcing integrates services and finance with a single provider

Today, IT departments, and in some cases individual departments within a company, are purchasing an ever-growing proportion of IT services in the form of managed services. In this model, full responsibility for the provision of some or all IT services is outsourced to one provider. Depending on the size of the customer, the IT assets that are procured and deployed for customers as part of such service agreements can reach considerable proportions. As a result, large providers then draw on financing models, particularly leasing, in order to preserve their liquidity. This is because funding is deferred. Although most of the fixed capital and startup costs are incurred in the startup phase, it is not usually possible to invoice the customer for operating expenses until the transition and transformation phases.

In order to protect themselves against the **risk of the provider defaulting**, companies want to ensure that they can continue to use the assets that have been supplied in the event that the provider defaults operationally or financially. The aim is to maintain business continuity at all times.
The smaller and more specialised the provider, the greater this risk. If the provider's credit standing deteriorates, it is possible to minimise this risk by contractual means, usually by the provider, the customer and the company financing the project entering into a tripartite agreement. Despite the substantial expense relating to the contract and the accounting treatment, this method of risk minimisation is often chosen.

However, the drawbacks of comprehensive managed-services models include yet more financial and operational factors. Firstly, providers naturally pass on their funding risks to customers – in the form of credit spreads that can add up to a significant amount. Saving on these surcharges alone is sufficient motivation for considering other funding models.

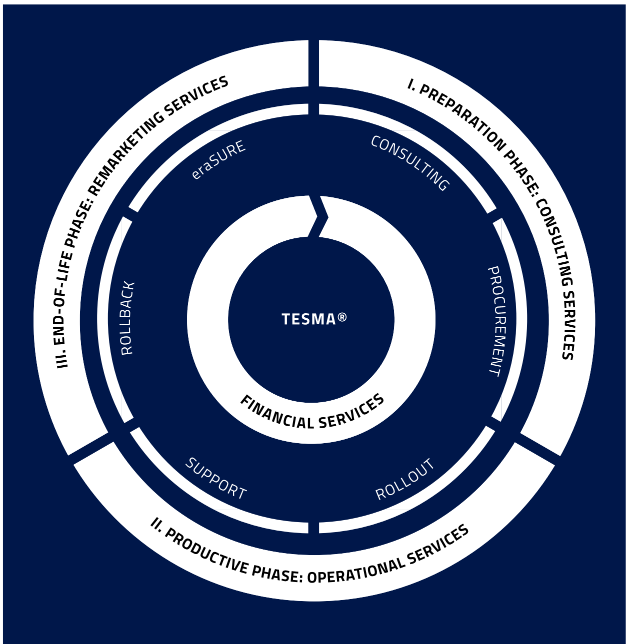
Secondly, the provider's services within the contract are not very flexible because they are tied to external means of procurement. Only a non-captive, higher-level service provider is able to change the number of assets or meet requirements for devices and technologies during the term of a lease at no extra cost.

MANAGED SERVICES CREATE NEW RISKS

For customers, the following two main risks emerge:
The risk of non-compliance with accounting standards is usually covered contractually. Although customers would otherwise run the risk of having to report IT assets on their own balance sheet, in this case they have no obligation to repurchase the assets or assume liability for them. A particularly inconvenient aspect of this risk is that another independent party – namely the customer's own auditor – may question compliance during the term of the lease.

> "Even very large providers expose themselves to financial risk on behalf of their customers, a risk that they mitigate by using leasing structures – consequently creating new risks for customers."

Managed services: What really interests customers



> "Companies use managed services to reduce their workload. Additional expense for financial and IT management erode any benefit gained."

1. MINIMISED WORKLOAD

The two main objectives for buying in managed services are usually the procurement of capacity and expertise, neither of which are available in-house or are able to be provided at the desired price.
What customers definitely do not want are extra expenses for managing the provider. So it is crucial for the following factors to be in place:

- Single point of contact – one service provider really does deal with everything
- Support during all stages of the technology lifecycle – strategic and operational
- Combination of technical expertise and commercial intelligence
- Increased process efficiency across the board
- Full support for the expansion, modification, and adaptation of technology investments

2. REDUCED COSTS AND RISKS

Too often, when managed services are viewed as a whole, the expected cost savings fail to materialise because the benefits of savings on individual running costs are canceled out by management and finance costs elsewhere. This can be avoided by:

- better purchasing terms thanks to market knowledge and volume discounts;
- portfolio harmonisation and streamlining;
- process automation and the elimination of media breaks;
- complete tracking across the entire technology lifecycle: technical details, commercial details, locations, and lease terms.

3. MAXIMUM TRANSPARENCY

Reporting and transparency are by no means interchangeable terms. During the process of digital transformation, companies must be capable of making rapid strategic decisions at all times, including decisions about the efficiency of managed services. Intelligent planning and reporting of the technical and financial situation are essential, such as:

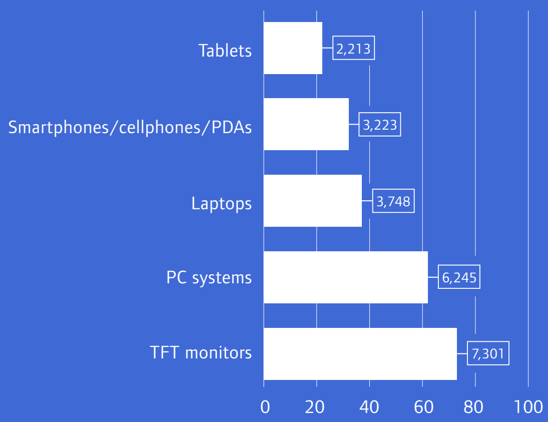
- accurate analysis of existing equipment to ensure well-balanced, optimised technology landscapes;
- simplified management of cash flows and assets;
- straightforward cost allocation;
- highly granular reporting and budgeting of expenses;
- costs identified and allocated to individual cost centers – enabling immediate evaluation of consumption peaks and cost drivers;
- straightforward capacity and consumption planning.

MONITORING

Total rent (per year)	Total rent (per month)
2018: $458,658.39	2/2018: $41,654.02
2019: $465,879.45	3/2019: $32,998.56
▲ +1.57 % + $221.06	▼ –20.78 % – $8,655.46
Total orders (per year)	**No. of assets (per year)**
2018: $986,325.61	2018: 28,985
2019: $357,569.58	2019: 30,258
▼ –63.75 % – $628,756.03	▲ +4.39 % + 1,273

REPORTING

Contract management broken down by asset class



4. FULL OPERATIONAL CONTROL AND GREAT FLEXIBILITY

Instead of managed services, companies can achieve points 1 and 2 today, by using ready bundled cloud services, which are often actually supplied by the same provider. In which case, they have less to do with the assets, or even have nothing more to do with them, so the risks are no longer applicable either. This comes at the price of only being able to buy commodity services and only influencing the scope of the services by scaling them up or down. As a result, customers continue to consciously opt for managed services because it is possible to customise them. It is the customer, not the (cloud) service provider who specifies the package, resulting in a significantly better fit. And even though cloud services promise comprehensive reporting, they do not guarantee the degree of transparency the customer has in mind. It is only possible to make minor adjustments.

The role played by providers

Providers remain specialist suppliers of service technology. It is they who actually make managed services possible. Their expertise forms the cornerstone of outsourced infrastructures and services.

However, providers often feel that they are asked for services that are not really part of their core business – such as procuring and funding hardware and other assets for customers. Because they themselves are just customers in this situation, and are also (by necessity) acting in their own commercial interests, the solutions are ultimately not always the best for the customer.

A second challenge arises when providers themselves employ subcontractors to provide services. This makes it difficult for the IT provider to manage complete asset inventories properly on behalf of the customer.

As a result, optimum provision of services is usually a team effort between the customer, the service provider, the finance provider and the consultant – albeit under the leadership of the customer who specifies the members of the team – ideally without having to worry about technical or administrative details. In turn, consultants and finance providers contribute their experience to the selection of suitable partners and assist with negotiations and the drafting of agreements.

Separation of assets and services in the hybrid approach

How can the risks we have mentioned be avoided or mitigated and how can customers' interests be satisfied without jeopardising the undisputed benefits of managed services? How can the specific interests of CIOs and CFOs be met?

One thing is clear: customers themselves no longer want to be involved in the procurement and administration of IT assets, and no longer have the necessary expertise. They want to delegate the design of funding models that are optimised in terms of tax and finance to specialists. Complying with and monitoring off-balance-sheet parameters pushes the expertise and processes of IT organisations – of both customers and providers – to their limits.

Specialist IT lessors can make an invaluable contribution in this area. They possess funding models as well as the processes needed to ensure that customers comply with accounting standards.

Technically, in a hybrid managed service, customers purchase the IT assets required for the IT service from a technology manager rather than the provider. This manager is also a financial engineer and not only represents the interests of the CIO (maximum performance, minimum cost) but also those of the CFO.

HYBRID MANAGED SERVICE: A SUITE OF SERVICES FROM A TECHNOLOGY MANAGER

The role of technology manager, which falls to the lessor, is essential for the efficiency of this delivery model. It means that the customer does not have to deal with the procurement or administration of IT assets. This responsibility is delegated to the IT provider who procures the IT assets from the lessor and manages them on behalf of the customer. As well as providing financial services, a technology manager must be capable of dealing intelligently with contracts for technical services. A wide range of technical and commercial skills are required, and they must be part of a shared management platform. Consequently, a technology manager who can create commercial transparency and intelligence by means of efficient processes and systems has a crucial advantage.

> "When it comes to managed services, customers do not want to be in the role of overall coordinator. What they need is a central technology manager, particularly where there are complex IT configurations. Providers cannot always perform this role, but new, hybrid models can resolve this stalemate."

NEW CONTRACTUAL STRUCTURES

The hybrid approach requires the customer to enter into two contractual relationships. The contractual arrangements focus separately on the provision of services and the provision of financial services. This undoubtedly means additional expense – but an experienced sourcing consultant can easily incorporate it into a competitive process.

BENEFITS:

By separating assets and services, this process clearly reduces provider default risk and the risk of non-compliance with accounting standards. The minimally higher establishment costs in the competitive phase are offset by the following significant advantages:

- When required, changing provider is easier to handle and does not require a rollout. For IT services in which the deployment of assets is very decentralised or for mobile-device-based services, this represents a significant increase in flexibility and strategic scope.
- Lower total costs result from the absence of provider surcharges for passing on payments to the lessor and it is possible to vary the quantity of assets with a lengthy useful life if they are leased from an experienced lessor.
- The uncertainty about whether IT assets are required to be reported on the balance sheet (operating vs. finance leases) ceases to apply for both the customer and the provider – this greater level of certainty over the entire term of the lease is a factor that should not be underestimated.