

# Shared business services and the evolution of the multi-divisional corporation

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## Abstract

The concept of consolidating common service activities into a discrete Shared Service Centre (SSC), where expertise and technology can be brought to bear on work processes and information flows, is an emerging development in the continuing evolution of the multi-divisional form (MDF). Proponents for the SSC claim that significant efficiency savings can be achieved through process re-engineering, the elimination of shadow systems and location cost arbitrage. Whilst, similar claims are made for third party outsourcing, the SSC enables a quasi-market feel to relationships with its 'customers' in the business units, and crucially allows management to retain hierarchical control over service activities.

There is however little literature on the practical forms of governance arrangements that might enable an individual SSC to play a role in supporting the combination of styles of market and hierarchy within an organisation. Two particular issues are the form and operation of a Service Level Agreement and the freedom of divisions to choose from a range of service sources. Through the use of case study data this article explores the potential of the shared service model to contribute to the continued hybridisation of the MDF, as organisation designers seek to align structure and process with ever changing strategic imperatives.

Key words: shared services centres, multi-divisional form, organisation design, governance.

## 1. Introduction

The development of the multi-divisional form (MDF) has been an iterative process as organisational designers make governance choices to align strategy, structure and process across changing environmental contexts (Chandler, 1962). The chief dilemma of *structure* is weighing the autonomy of divisions to make tactical decisions at the market interface against a concern for both the central co-ordination of the overall organisation and the avoidance of suboptimal and dysfunctional behaviour in individual divisions. The chief dilemma for *process* concerns weighing the extent to which units are seen as individual silos and controlled through direct intervention by top management, against the extent to which units are integrated through information flows across the organisation to shared knowledge and foster co-operative decision making.

Whilst the agenda of cost and headcount reduction tends to dominate the practitioner literature (Bangeman, 2005; Janssen and Joha, 2006), the concept of sharing common support activities can provide further opportunities to create flexibility in directing, co-ordinating and controlling large organizations. Evidence from an ongoing case study is used to demonstrate how relationships between a SSC and divisions can be formulated and governed within an overall range of sourcing options. Building on the evolving theory of the MDF, the paper proposes that the Shared Service Centre (SSC) model might complement other models of organisation structure and process.

The paper proceeds as follows. First, the main variations of the MDF models are outlined in order to conceptualises how organisations have sought over time to manage strategy, structure and process through changing external environments and developments in Information and Communication Technology. Next, the SSC model is introduced and set within a continuum of sourcing possibilities. Third, some case study evidence is presented from a global organisation that has developed a mixed model of service channels. Fourth, there is a discussion of the findings, followed by some tentative conclusions.

## 2. The development of the MDF - Markets versus Hierarchies

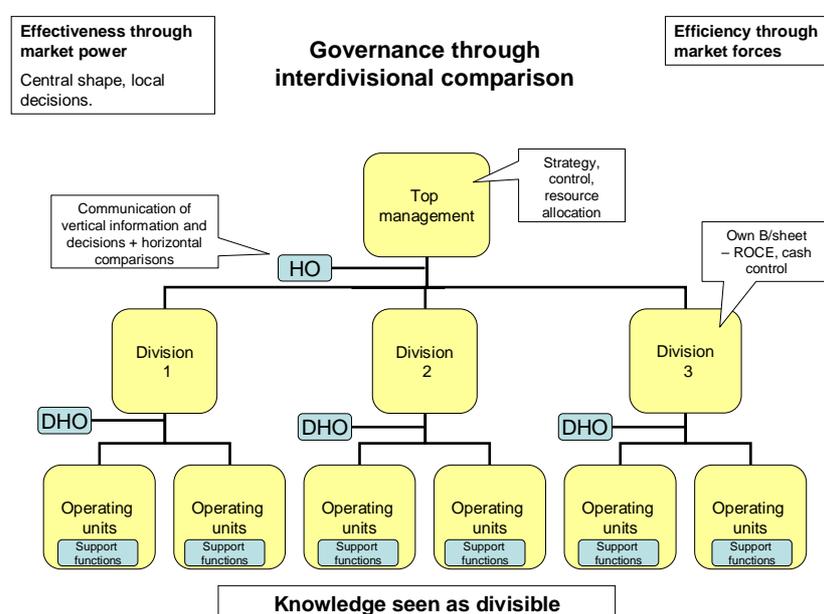
### 2.1 Central control vs. divisional autonomy

The simplest form of organisation is for a single manager to directly control each individual worker or group of workers, what is referred to herein as the **S-form**. Management direction and control is centralised, units have little discretion on *what* to do or *how* to do it, and communication is mainly vertical with little interchange between individual groups. Whilst uncomplicated, in any given situation, there is usually a limit on the size of organisation that can be controlled in such a direct manner.

The MDF evolved in the early part of the 20<sup>th</sup> Century to divide growing corporations into smaller, more manageable elements, by creating *divisional* units that enjoy a degree of operating autonomy, thus creating a *structure* in which central strategy is separated from local tactics. In terms of management control *processes*, the performance of individual divisions is evaluated by comparison with other divisions, with relatively little direct intervention by top management. The chief roles of top management are to allocate resources between divisions and monitor divisional performance. The basic **B-form** depicted in Figure 1. leans towards

economic theory by seeing the firm as a collection of separate activities. It is assumed that each division will become more efficient through the dynamics of market forces in its respective sector, although there may be duplication of systems between Head Office (HO), Divisional Head Offices (DHO) and Unit Support Functions. Galbraith and Nathanson (1978, p. 14) distinguished between functional and product based divisions. Chandler's (1962) thesis of corporate strategy, structure and process is credited with having had a significant influence in management education in US business schools, and hence in the adoption of the MDF (Palmer, Jennings and Zhou, 1993).

**Figure 1. The Basic B-form**



Williamson (1975) hypothesised that the MDF, with its combination of hierarchical control and market discipline, should outperform alternative arrangements. However, Hoskinsson, Hill and Kim (1993: 270) noted that 'empirical studies offer only qualified support for the MDF hypothesis' and claimed that the MDF was an organisational fossil.

## 2.2 Variations of the basic M-form

The interdependent, **I-form**, seeks to internalise sequentially dependent processes. For example, an oil company with drilling, refining and distribution activities can minimise the transaction costs that would otherwise result from open-market relationships between those activities (Williamson, 1975 and 1985). This view casts

the firm as an *internal market* with interdependences and inter-relationships between divisions that need to be managed through central co-ordination and transfer pricing policies. Thus, a central head office will be required to provide top management with information to ensure that the potential economies of scale and scope are realised by designing appropriate policies to guide intra-firm co-operation, and where necessary resolve disputes between units. See Perrow (1986, pp. 183-189) for a case study on the vertical integration of the entertainment industry.

By contrast, in the Holdings or **H-form** a portfolio of dissimilar business activities is combined under a single corporate umbrella. The main rationale leans towards financial engineering rather than to products or markets. It is argued that the H-form can produce synergistic benefits across dissimilar businesses by diversifying business (unsystematic) risks, balancing asymmetric cash flows and optimising taxation arbitrage opportunities. A further argument is that it allows for a highly interactive top management style but on a management-by-exception basis. For example, in the contemporary private equity model, underperforming companies are acquired, given 'turn around' attention, and then held until a suitable opportunity for sale arises. However, Williamson (1975) criticised the H-form's lack of coherence.

### *2.3 Build-up and breakup*

The extent to which a head office actually seeks to direct and co-ordinate tactical decision making in divisions will dictate the size and scope of the centralised apparatus necessary to set overarching corporate policies and manage the information flows between head office and the divisions. The Unitary, or **U-form**, tends back towards the centralised control of the S-form, but increasing size and complexity are managed by the creation of substantive staff functions to support top management planning, decision making and control. A key enabler of this form was the emergence of mainframe computers in the 1970s which vastly expanded the range of data that could be captured and processed. In the early days however, mainframes were expensive and difficult to operate and thus tended to be a central rather than a divisional facility. Williamson (1975) labelled the expansion of the head office role as the 'corrupted' M-form, noting that it can result in both a bureaucratic disposition and a creep in the size and influence of the centre's influence. Since the 1980s there have been a number of attempts to address the problems that arise through the U-form tendency to become bloated, bureaucratic and unresponsive in an increasingly dynamic global marketplace. Indeed the value of some conglomerates sank below what the market judged was the value of the parts and,

through shareholder pressure, they were unbundled. For example, ICI plc split into separate chemical and drug companies (Zeneca) in 1993. Sometimes whole industries under public control (in the UK) were similarly restructured and divisions floated as a number of separate companies, for example, the electricity generation industry in 1990 (see Herbert, 2009) and British Railways in 1996 (see Dent, 1991).

#### *2.4 Co-operative integration*

Alternatively, other MDFs sought to retain the scale benefits of corporate aggregation but adopt new structures and processes to promote the integration of knowledge and operational co-operation across divisions. The advent of the Personal Computer allowed distributed data capture and analysis to be applied at a local rather than a central level enabling situated decision making and self-monitoring by workers. In the 'Horizontal Organisation' **HO-form**, divisional autonomy is preserved but inter-unit communication is facilitated through lateral linkages to share knowledge and solve problems (Ostroff, 1999). In adopting a 'value chain' approach, Ostroff's model has a resonance with the I-form, although the HO-form appears more applicable within, rather than across complete products, for example, within the refining division of a vertically integrated petroleum company.

The 'joined-up' company, **J-form**, signals a more purposive attempt to reconsolidate otherwise disparate divisional units through formal and informal linking roles, backed by a stronger mandate of participation. Whilst structure may remain essentially decentralised, a common feature of such initiatives is the standardisation of processes (operating routines and behaviours, communication protocols and formats, etc.) governing the customer interface. For example, a corporate web site might provide a single portal for customer access to local divisions.

#### *2.5 Executive integration*

Divisions might be integrated more formally through matrix management by combining decision making across, say, product and geographic market foci. Bartlett and Ghoshal (1993) describe how the matrix approach, labelled here as the **MX-form**, was developed by the European conglomerate ABB. Whilst the MX-form remains moderately structured in terms of co-ordinating roles and responsibilities, the actual processes of management are looser and intended to be more dynamic. Co-operation is facilitated by creating a sense of common ownership of resources and results across products and markets at a top level and between functions at lower levels.

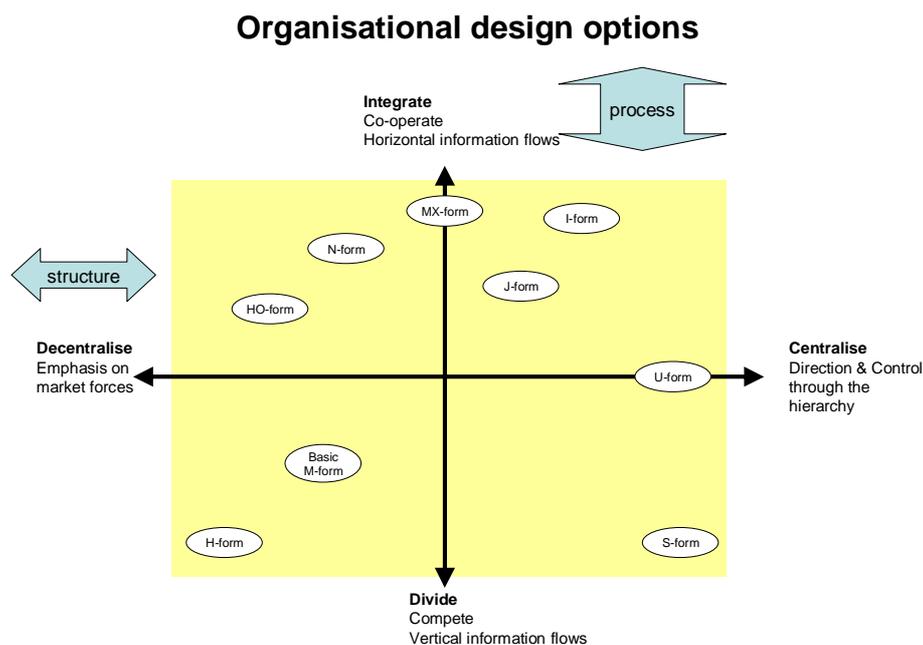
In a more radical extension of the matrix principle, Hedlund (1994) proposed the New (or novelty) **N-form** in which an organisation is seen as comprising an aggregation of individuals, with ad hoc clusters of individuals forming and reforming around emerging market opportunities or problems. The N-form is essentially decentralised and loose in its structure with the intention that people will be motivated to share knowledge through strong common aims. (See also the 'Spaghetti' organisation, Foss, 2003).

The overall emphasis is on firm-specific capabilities of change, dynamism and innovation as the main source of competitive advantage (see 'Dynamic Capabilities' Teece, Pisano and Reece, 1997.)

## 2.6 Mapping structure and process

The various design permutations above are now depicted in Figure 2. across two continuums. First, relating to structure; centralised vs. decentralised. Second, relating to process; the facilitation of interdivisional communication, co-operation and horizontal integration vs. the creation of competitive tensions (between individual divisions) through comparative evaluation. The former being managed through vertical information flows with relatively little horizontal interaction.

Figure 2. Organisation design options



## 2.7 Common Business Services

But, whatever the design of choice there is, to a greater or lesser extent, a central role in enabling information flows within the organisation and supporting top management in, planning overall strategy direction, and co-ordinating and controlling individual divisions. For example, corporate level policies will be necessary to standardise data formats and protocols. However, maintaining a range of staff functions such as HR, Finance, IT, Purchasing, etc., is expensive and could ultimately result in an overly bureaucratic regime, (Williamson's 'Corrupted M-form').

Likewise, leaning towards the decentralised pattern incurs the duplication of support services across divisions, thereby reducing efficiency in the first instance, and eventually the overall effectiveness of the firm as initiative is stifled by the lengthening of vertical communication channels. One means of addressing systems duplication is by sharing divisional and central support services. The next section describes the form and nature of the typical SSC model in which support activities are transferred to a single, quasi-commercial, centre.

## 3. Shared Business Services

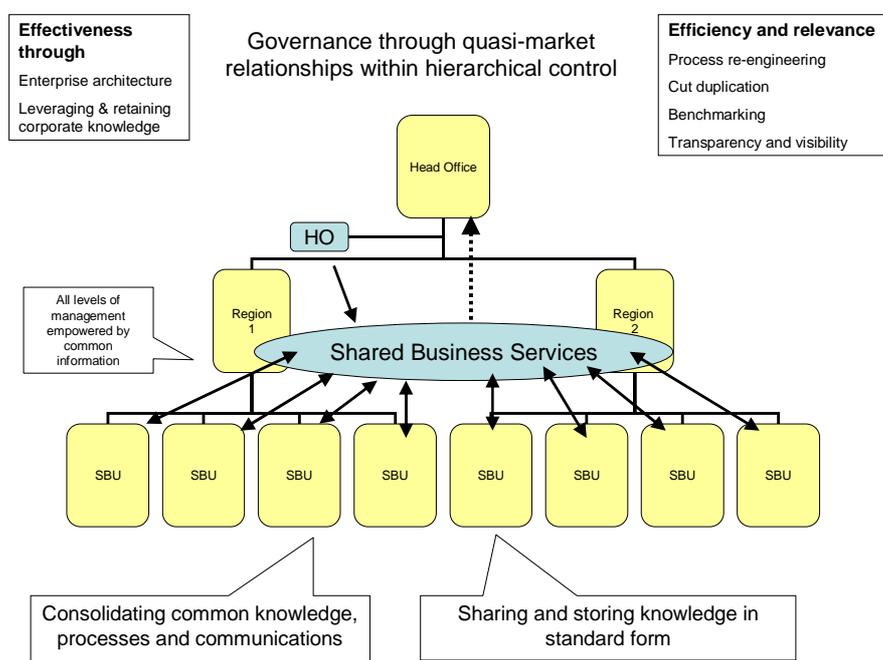
The essential form of the arm's length, customer-focussed, SSC is that ownership of processes and system resources, such as credit control processes and personnel, are distinct from the divisional users who still 'own' the business outcome, such as cash collected on time. The SSC's costs are then shared, on some equitable basis. By avoiding contractual commitments with third parties the SSC model avoids the risk of exploitation and retains operational flexibility. Bergeron, (2003. p. 3) defines a SSC thus;

[S]hared services [sic] is a collaborative strategy in which a subset of existing business functions are concentrated in a new, semi-autonomous, business unit that has a management structure designed to promote; efficiency, value generation, cost savings and improved service for internal customers of the parent corporation, like a business competing in the open market.

Efficiency centred aims usually include; achieving economies of scale through reducing accommodation and staffing costs, eliminating duplicate systems, standardisation of systems and data formats, process re-engineering, leveraging technology and fostering an ethos of continual improvement underpinned by

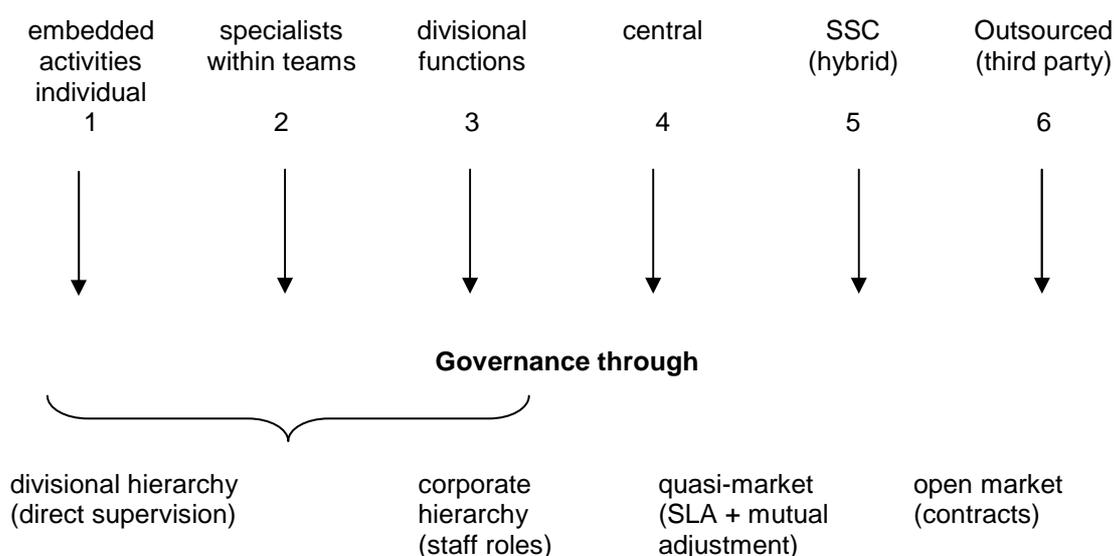
benchmarking against other SSCs. But, in addition to efficiency savings, the overall effectiveness of the organisation might be increased by; allowing operating units to focus on core operations; improving support services through specialisation; creating visibility of back-office costs and raising the transparency of divisional activities (Schulman, et al., 1999; Leach, 2004). SSCs can facilitate lateral information flows across the divisions, and vertical flows between the centre and divisions (Ulbrich, 2006: 192) but, and perhaps crucially, knowledge forming part of the corporate 'enterprise architecture' is retained within the firm, see Fig. 3.

**Figure 3. The SSC Model**



The SSC, with its twin foci on divisions and the overall group, represents a hybrid form between hierarchical control and the open market position involving third-party outsourcing to achieve the best of both worlds.

The SSC can be positioned within a continuum of internal and external approaches to organising support activities. This is shown in Figure 4. together with possible modes of governance. The working relationship with SSCs is usually guided by a Service Level Agreement (SLA), but with a higher degree of mutual trust and operational accommodation than would normally be possible with a third party outsourcing contract.

**Figure 4. A continuum of approaches and governance modes**

Malcolm (1999) describes the development of SSCs in the context of the wider process of corporate restructuring comprising three distinct but overlapping phases, centralisation (1950-86), decentralisation (1980-99) and SSCs (1985 to 1999). There are two concerns for this paper. First, how a flexible sourcing approach for business services combining the benefits of market-orientation and hierarchical control might operate. Second, how the SSC model might contribute to such a policy. The following section presents some early evidence from an ongoing field study into a multi-national financial service company which has adopted the SSC model within a range of approaches to sourcing business support services.

#### **4. Case Study - Bankco**

##### *4.1 Research method*

The empirical data presented in this section is from an ongoing, longitudinal, study of SSCs comprising ten case organisations employing a multi-method approach; mostly comprising interviews with key participants, but also including inspection of internal documents and some quantitative surveys of SSC 'customers'.

The Bankco (name disguised) approach is not untypical of the general form of the SSC model and the use of SLAs. However, in terms of flexible sourcing, Bankco is particularly interesting because it has embraced the market model with divisions enjoying a significant degree of latitude in sourcing business support services.

Indeed, there are two SSCs with an element of competition between them and at the time of the field work (2008-09) there was a fundamental scrutiny of back-office costs

due to the difficulties in the financial services sector. Research visits were made to the NSC and a business division in a European capital city.

#### *4.2 Bankco context*

Bankco is a European bank with retail, investment and trading operations in all of the major global financial centres. There is a large off-shore SSC (OFSC) in Asia with several thousand staff and a smaller, more recently established, near-shore SSC (NSC) in a mid-European country.

The OFSC largely undertakes routine, back-office, transaction processing utilising a low cost labour force, albeit one with generally good levels of education. The NSC enjoys a moderately low cost environment but with higher levels of business and language capability, together with regional air links that allow face-to-face connectivity with European business divisions, and scalable infrastructure costs. The client list of the surrounding business park has a strong compliment of blue-chip companies.

The NSC undertakes a range of back- and near-front office activities, most of which are either process (flow) based, e.g. financial transaction processing, account reconciliations and financial reporting. Increasingly, some activities are of a semi-routine nature, such as preparing detailed customer contracts by customising document templates. A third category might be termed 'craft' activities such as; producing bespoke client presentations, IT systems development and financial analysis for customer-facing banking personnel using secondary data sources.

An alternative way of delineating activities is between; services in which a staff pool is shared across Bankco's various divisions and captive services, in which dedicated staff are responsible for a transplanted activity from a particular Bankco division. In addition to the SSCs, Bankco utilise around 3,000 contingent workers mostly through third-party agents. The NSC's aim is to 'move up the 'food chain' by which they mean to undertake higher cognitive work more closely associated with mainstream investment banking activities and its ancillary professional services.

Whilst professing to be market-oriented, in practice a SSC might simply represent an as an internal monopoly. However, in the case of Bankco, both SSCs are obliged to pitch for business directly to business divisions who have some freedom to retain the work within divisions or use specialist third parties. That having been said, there is an

implicit assumption that shared services makes sense overall for the organisation, with the SSCs being 'good enough' now and with the potential for improvement in the future. In sum, the case to business units is made on the basis of *why* a particular SSC should do a particular task? rather than *why* Bankco should use a SSC approach *per se*. Consequently, the sales pitch is somewhat understated.

When migrating a service, the SSCs have their own specialist transition teams that document processes thus making tacit knowledge in the business operations explicit and capturing it centrally for the overall benefit of the firm. SLAs are used to plan and monitor the service provided. There are no contractual penalties as such but any disputes can be escalated up the respective chain of command on either side. The NSC manager explained that there is a significant element of [process] re-engineering and establishing a proper controlled approach on migration. Indeed, the process off-shoring has put more controls in place, together with the process documentation. The following data has been extracted from the transcript of a conversation with the Director of Legal Services in a Bankco division.

#### 4.3 Legal Services

The department has a need for around 30 (full-time equivalent) staff possessing both legal qualifications and language skills. Knowledge of financial services is also important but is not a pre-requisite at the time of recruitment. At the time of the visit in March 2009 there were approximately eight on-site employees, six at each SSC, five individual freelance agents (contingent workers) and five workers at a third-party law firm. The Director (DD – *name disguised*) was confident that the mixed approach to sourcing gives an appropriate balance between cost, expertise and flexibility, given the variety of tasks and customer profiles. He explained Bankco's overall approach.

*'We've ended up using the OFSC in Asia for more process orientated work; higher volume/higher headcount work. Whereas, we favoured Mid-Europe, for some of the more complex, client facing, work, it's drifting that way, but it's more of a drift than a conscious decision to go that way. Horses for courses, whatever works best.'*

We enquired as to the motives for alternative sourcing options.

*'We started this [flexible sourcing] two or three years ago, the market changed completely and we went from one of historical growth of 15% year-on-year, to being told 'actually its going the other way'.... We've [now] made real headcount savings, and therefore cost savings.'*

*'It became clear very quickly that it wasn't going to work onshore because we [already] had people who were very skilled, some highly qualified lawyers, and expected to do these tasks, but not wanting to do it, and therefore not doing it very well. And, not doing it on time.'*

Legal services involves complex high value support work and it was clear that significant effort is put in to ensuring that employees of the SSCs understand and share the values of the corporation. All Bankco offices have an identical look and feel throughout the world. LD, or his senior assistant, is involved in both the recruitment and induction process for new employees at the SSCs. LD explained.

*'It's the same as for people working here. It's about how people work, how well they do their work, how detailed they are, how they're dealing with clients, communication, their attitude, it's all those normal kinds of things. It's much more difficult when it's remote, clearly.'*

*'The guys in Asia are all graduates, around 30-40% have got MBAs. Even though we're talking process work, it is actually complex process work. We struggled to get this message over. When we originally recruited we had to emphasise: don't look at this as a traditional BPO – it's not yet legal process outsourcing – we're kind of in between. It was quite difficult to recruit the right level of people. If we'd have tried to do this onshore we'd have to employ to similar graduate level people but that would be five or six times the cost in Asia. Frankly, I also don't think we'd get the attitude or the application'*

LD regarded the SLA as helpful in terms of 'scoping' the service to be provided and clarifying the eventual recharge for budgeting purposes. However, he suggested that it had little application as a working document, adding;

*'If I have to resort to it during the year it means that the service has already failed, and we cannot afford that to happen'.*

He explained that there was a significant level of trust involved in making things work and highlighted the importance of good personal relationships with the SSCs. It appears that the SLA is viewed more as a periodic touchstone than a working document and this is particularly interesting given that this is a director of legal services talking. It was noted that relationships with the third party agents appear slightly more formal, although there is also a strong professional relationship as the basis for day-to-day working. We asked if the 'real contract' was based, *de facto*, on natural 'hard' points in the systems, for example, monthly progress reports available on the xth day of each month. LD replied.

*'Yes, there are. Some things are daily processes which have to be done that day. We get KPI's back, but we introduced what is called a quality survey, basically about the softer skills - initially monthly and then every three months.....It includes those things that you can't measure by stats. It was introduced because we got fed up with people pushing us about asking for stats, when it's actually about how you deal with work, how you deal with the clients, how you deal with queries, how quickly you react, how proactive you are – all those kinds of things that you can't measure'.*

*'SLAs are something that were not mandatory, but we had to have them! Frankly, they're not something that I pay a lot of attention to. We have them for different processes and for different product areas, along with associated documentation. They are a framework for the offshore centres, but they don't for my mind add a lot of value. For instance, I don't have a SLA for the people that work for me here and these guys in the SSCs are also part of the team. I suppose, it works for the data capture processes, but when you're talking about sending documents out to clients, and maybe you chase them six times or so, then its difficult to have a meaningful SLA for that. I'm therefore much more interested in how we perceive that people are doing the job'.*

In terms of recharges we asked if the divisions saw a specific cost coming back and whether that might reflect planned or actual activity? LD replied.

*'The SSCs costs get split globally, between Europe, the US and rest of the world. You could spend a lot of time trying to measure things by looking at actual work loads but you'd end up with the same figures pretty much. And you can't actually measure some of it anyway. Say, you've got one client document to do in London, and one in the US; the first might take you three days to get signed, whilst the other three weeks and you could have chased that client ten times or twenty times. How do you measure that in terms of hours? So we have a fairly simple split.'*

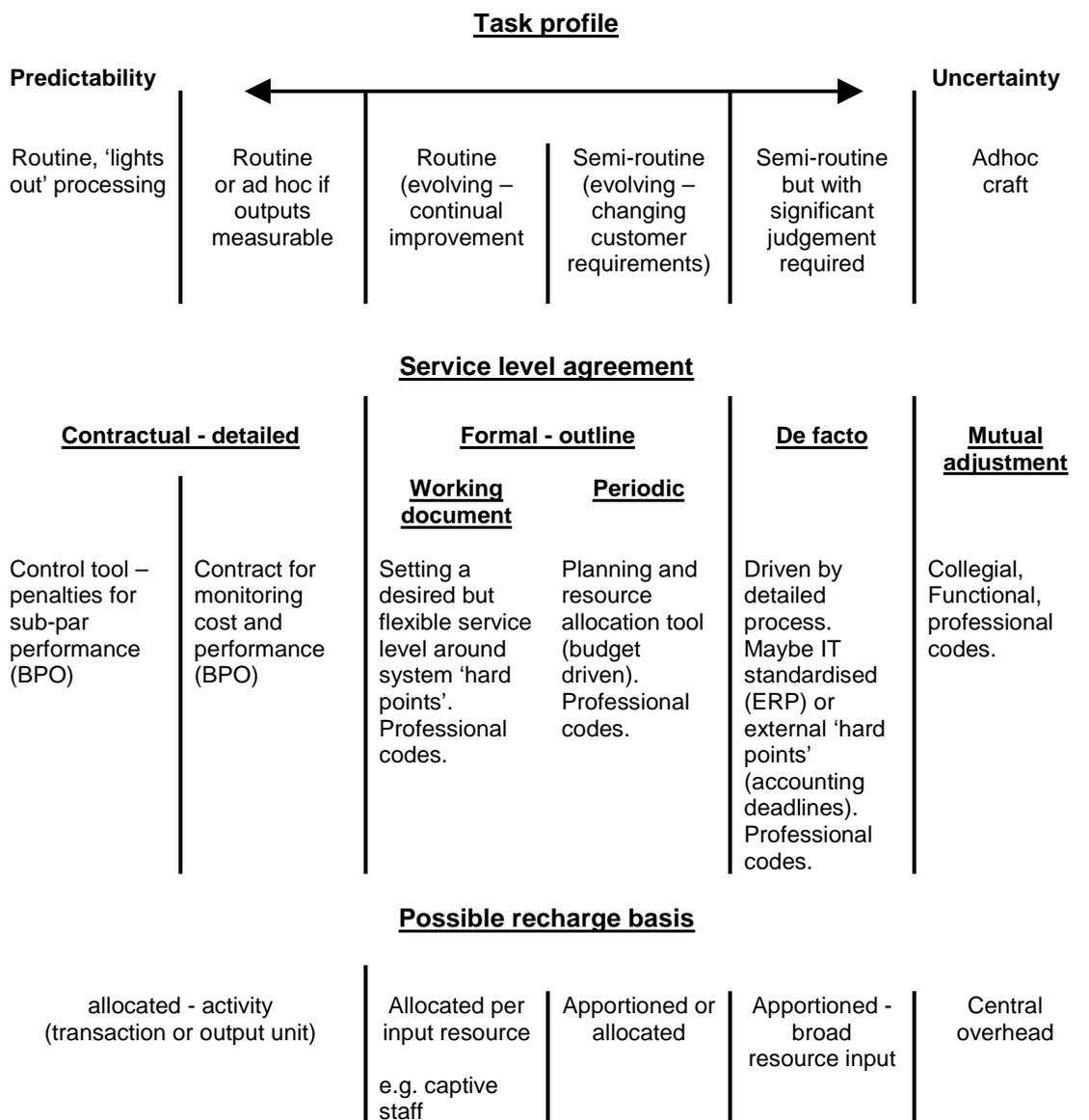
The next section discusses the case further and presents a framework of governance forms and mechanisms.

## **Discussion**

The changing business environment had caused the management at Bankco to reappraise the way in which business support services were undertaken. The new strategic imperative was directed towards preserving market share whilst pursuing internal efficiencies. The structure had changed towards the market model. Divisions were less inclined to undertake service work themselves and were now using a range of sourcing options. This had caused work processes to become re-engineered, standardised and documented. The physical separation of divisional management and workers had caused new controls to be put in place and performance statistics were being produced.

However, in terms of the main governance mechanism with the SSC, LD at least did not look to the SLA as a means of controlling the minutia of activities and outputs, rather the SLA functions more as a scoping and planning tool. Specific controls arise through system 'hard points', KPIs or the qualitative survey initiated by the division. The Director of Legal Services made the point that SLAs are not employed to monitor the relationship with divisional or freelance workers as there is a strong sense of professional understanding of the job and necessary behaviours. Figure 5. suggests a continuum of options for the design of SLAs, on a continuum from task predictability to task uncertainty in the manner of Galbraith (1973).

**Figure 5. Continuum of tasks and relationships**



ERP - Enterprise Resource Planning system

BPO – Business Process Outsourcing

The direct relationship between divisional management and the SSC's workers reflects the extent to which behaviours are seen as important. Perrow, (1986) argued that the market vs. hierarchy dichotomy can be a false one and thus it would appear that the SSC has the facility to represent a practical hybrid arrangement positioned between hierarchy and market.

At Bankco, business support services are undertaken using a mixed service model and whilst financial services is generally a highly structured and controlled environment, nonetheless, for some functions at least there is a resonance with the N-form model with its accent on myriad connections 'glued' together by common knowledge and personal relationships.

One view might be that the SSC model is just another manifestation of the Unitary-form with divisions being forced to use an internal monopoly, with a tendency towards the 'Corrupted M-form' (Williamson, 1975). However, consistent with the overall SSC enquiry, at Bankco managers at both the SSC and the division believe that the SSC model has a distinct rationale based on a customer-led market place. Obviously, a specific activity such as legal services is different to some of the high volume transaction based processes, nevertheless, the nature of the SSC service in terms of its ethos of continual improvement underpinned by a collegial atmosphere of mutual adjustment within a broadly framed SLA.

There is significant potential for Bankco to adopt a range of back- and near front-office support services both at a strategic (location level) and a micro (process/task level). At present business units need to be convinced of the benefits of using the SSCs on a case-by-case basis, but one could easily envisage a strategic level push to move a significant volume of back and near-front office operations out of divisions.

## **Conclusions**

This paper has presented a theoretically-informed case study of an MDF that has adopted a SSC model. More generally, the paper argues that the SSC model can be seen as a part of the evolving theory of the MDF. On the basis of this case, properly designed SSCs can have a mission beyond crude cost and headcount reduction, or being a halfway-house to third party outsourcing. Fully developed, it can underpin corporate governance by operating as a quasi-commercial business based upon SLAs, but with a flexible approach dependent on the nature of the task. It also adds value by uncluttering front-line divisions whilst retaining knowledge, sharing best practice and improving governance and control over the way in which the overall company does what it does.

Further work on SSCs might seek to elaborate on the traditional 'make-or-buy' decision. Outsourcing has been promoted on the basis that it is the efficient way to

bundle and deliver support services in comparison with a dispersed and inefficient in-house provision. However, further exploration of the form and nature of the SSC model and governance structures will allow a more informed choice on the possibility that an in-house hybrid (i.e. 'making') may actually be preferable to an outsourcing (i.e., 'buy') choice.

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