Business and IT operational models in financial services: Beyond strategic alignment

An IBM Institute for Business Value executive brief
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Business and IT operational models in financial services: Beyond strategic alignment

Despite a growing emphasis on aligning business and information technology (IT) in the past decade, financial services companies report that operational conflicts continue to impede effectiveness. Although most firms consider strategic alignment vital, they must also understand that it isn’t a cure-all. Firms that align strategically without also creating alignment on an operational level will often be disappointed with the results. To improve the relationship between business and IT, financial services firms need to construct flexible operational models that define how business and IT work together every day and at every level of the organization.

Introduction

CIOs across industries have ranked business and IT alignment as a top issue for a decade. However, despite significant focus on achieving alignment, it remains difficult to find healthy working relationships. Cost pressures have led to increasingly centralized IT functions, aiming to capture cross-line of business (LOB) synergies. While centralization has eased cost pressures somewhat, it also has the unappealing side effect of reinforcing those ever-present barriers between business and IT.

In spite of frequent expressions of frustration, it’s interesting that many companies believe they have made great strides in aligning business and IT, particularly in financial services where 90 percent of top executives at retail banks and 73 percent in insurance described their companies’ business and IT strategies as “fused.” Despite these claims of strategic alignment, many IBM clients still consider their organizations to be ineffective at an operational level.

So, why is there no obvious payback from the alignment work that’s been done thus far? Where are things going wrong? Have financial services firms effectively aligned business and IT or not?
Designing an operational model that works

Traditionally, financial services firms have focused on alignment at the strategic level, believing that if business and IT were synchronized at the top, alignment would trickle down to the operational level naturally. But, sharing a common strategy isn’t sufficient. Companies also need a tactical level approach.

An effective operational model can bring business and IT together, avoiding many of the usual conflicts that can occur. Improved operational alignment cannot only reduce costs and increase efficiency, but more importantly, it can bolster a company’s ability to respond to customer needs on demand. When organizational hurdles are removed and employees understand what they need to do their jobs, the workplace becomes more responsive and resilient.

Creating strategic alignment remains an important objective for financial services firms. In fact, market leaders should go beyond traditional alignment approaches to create “fused” business and IT strategies. However, knowing that alignment must run deeper in the organization, companies must also determine how to better synchronize their operational models with their fused business and IT strategies. This is especially crucial in the financial services sector, where technology can act as a key differentiator in gaining competitive advantage.

An operational model is comprised of four core elements and three enablers (see Figure 1). Core elements are the mechanisms, controls and reporting functions for managing operations, while enablers set the tone of the operating environment.

**Figure 1. Components of the operational model.**

Source: IBM Institute for Business Value analysis.

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### Four signs your organization is not aligned at an operational level:

1. Frequent conflicts between business and IT with respect to decision-making procedures and authority.
2. Business is dissatisfied with the level and frequency of communication from IT.
3. Frequent finger pointing between business and IT when project delays or problems occur.
4. An “us vs. them” mentality prevails between business and IT staff.
Core elements provide tangible guidelines for how business and IT work together daily:

- **Governance** defines key decision-making mechanisms and forums and assigns levels of authority and accountability for decision making.
- **Process** establishes methodologies, identifies roles and responsibilities and sets expectations for project-based and ongoing work.
- **Communications** sets standards for the level, openness and frequency of dialog within and across business units, departments and teams.
- **Metrics** identify the quantitative and qualitative measures of performance to be shared across the organization.

Enablers are supporting elements that influence the level of cohesiveness possible between business and IT:

- **Skills** are the distinctive competencies residing in an organization which facilitate the performance of key processes and tasks.
- **Style** defines the norms that people follow when they interact with each other and with customers – it defines how work actually gets done.
- **Shared vision** aligns objectives and goals across the enterprise and serves as a guiding principle regarding what is important.

When conflicts between business and IT occur, many financial services firms attempt to jump in and address them at the lowest level of task execution without considering the big picture. These efforts will usually fail because they do not consider the root causes of the conflicts between business and IT. For example, many organizations attempt to resolve conflicts by creating joint steering committees and governance councils. While these committees can help improve communication, they do not address the fundamental issues that may be driving a wedge between business and IT. These issues commonly include misaligned views about the organization’s strategic context, disagreements about the role and orientation of IT or a poorly designed organizational structure. To create an effectively aligned operational model, firms must use a top-down approach that considers all of these factors (see Figure 2).
Step one: Identify the strategic context

The strategic context characterizes the environment in which the IT organization operates. It is defined by the importance of cross-LOB synergies, the degree of business overlap and the focus of technology in the organization. A firm can assess its strategic context by answering three key questions (see Figure 3).

The answers to these three questions will define the IT mandate — the role and orientation of technology in the organization.
**Step two: Understand the IT mandate**

The IT mandate is defined by the role and the orientation of the IT function within the overall organization. In a given enterprise, the role of IT will fall on a continuum between tactical and strategic. A tactical role focuses on executing business-defined plans, while a strategic IT role emphasizes driving competitive advantage. Similarly, the orientation of IT falls on a continuum between LOB-focused and enterprise-focused, depending on whether IT is focused predominately on serving the needs of individual LOBs or on enterprise needs.

There are four types of IT mandates, each exhibiting a different primary goal for IT (see Figure 4):

- **Utility** – Deliver effective, cost-efficient solutions across the enterprise
- **Project management** – Execute on LOB-planned programs and initiatives
- **Differentiated** – Drive competitive differentiation within each LOB
- **Transformational** – Drive overall business transformation at an enterprise level.

*Figure 4. Key characteristics of four IT mandates.*

Source: IBM Institute for Business Value analysis.
In most firms, the technology group provides a variety of services, including architecture, research, application development, infrastructure, testing, implementation and help desk support. The role and orientation of IT can vary for each. However, most organizations will demonstrate a dominant model based on where the majority of functions are mapped.

Misalignment between the strategic context and IT mandate can create conflicts between business and IT. For example, if a firm has a highly diverse set of business units where technology differentiation is critical for competitive advantage, then IT should have a differentiated mandate to support the needs of the business. However, very often, firms attempt to save costs by creating a centralized IT utility in this type of organization. The result is usually a high level of business user dissatisfaction and ongoing conflicts between business and IT.

Examining how technology services are performed can reveal such misalignment between a company’s strategic context and IT mandate. When the two appear incompatible, executives must reexamine expectations about IT’s orientation or role. Unresolved differences in perception can cause tension and lack of user satisfaction.

**Step three: Assess the IT organizational structure**

With the IT mandate well-matched to the strategic context, the next step is to assess how well the organizational structure maps to the IT mandate. Organizational structure types align with the IT mandate categories – utility, project management, differentiated, transformational – and each structure varies along three key dimensions:

- **Resource alignment** - Whether IT resources reside in a central group or are decentralized within LOBs
- **Reporting relationships** - Whether IT resources report to IT, LOB executives or both
- **Roles and responsibilities** - How responsibilities for key processes are divided between business and IT
Ideally, IT resources should reside where they can be most effective at fulfilling the IT mandate. For instance, to support a mandate that is strategic and LOB-focused, IT resources must remain close to the business, whereas a centralized IT group is more cost-effective if IT’s mission is tactical and enterprise-focused. Reporting relationships involving IT resources should also be aligned with the mandate – otherwise, IT may have difficulty delivering on its value proposition to the business.

Roles and responsibilities must conform in a similar way. For example, if IT’s mandate is differentiated, then IT will play a more central role in executing technology-related business functions and will be intimately involved in the development of a fused business and IT strategy. On the other hand, when IT has a utility mandate, IT staff will be more focused on execution. Business staff will play a more central role in determining the scope of and managing technology projects and business and IT usually develop their respective strategies independently.
Utility organizational structure

In a utility organization, IT resources are typically located in a centralized IT group to provide cost-effective services to all LOBs. Application development resources are usually assigned on a project-by-project basis and are not dedicated to specific LOBs. The business relationship management function provides the key linkage between the LOBs and IT (see Figure 5).

Figure 5. Example of a utility organizational structure.

Resource alignment
- IT resources reside in centralized group; usually aligned by competency vs. by BU

Reporting relationships
- IT resources have solid line to central IT group

Roles and responsibilities
- IT focuses on service provision; business has primary responsibility for determining the scope of and managing projects
- Business has responsibility for strategy development.

Source: IBM Institute for Business Value analysis.

Company A is a leading financial services firm that provides credit, investment and related financial services to individuals, small businesses and corporations. Despite a fair degree of diversity across LOBs, Company A is very focused on achieving cross-LOB synergies. As a result, Company A has structured IT as a utility, with a high degree of centralization.

Although the utility model allows certain synergies, user satisfaction is low in some business areas whose needs differ from those of the core business lines. As a result, Company A is becoming more differentiated to handle those diverse needs better. In some cases, key IT resources, such as application development staff, may be moved into the LOBs.
Project management organizational structure

In a project management-based organization, the majority of IT resources are located in a centralized group which sets standards, manages infrastructure projects and provides support for the enterprise. Operations are usually decentralized by LOB and while application development is usually located centrally, resources are often dedicated by LOB. Relationship managers may be located either centrally or within individual lines of business (see Figure 6).

Figure 6. Example of a project management organizational structure.

Resource alignment
- Most IT resources reside in centralized group, but may be dedicated by BU

Reporting relationships
- IT resources have solid line to central IT group; may have dotted line to business
- Relationship managers usually have dotted lines to both business and IT

Roles and responsibilities
- Business and IT share responsibility for scoping and managing projects
- IT is at the table for business strategy discussions, but not actively involved.

Source: IBM Institute for Business Value analysis.

Company B is a leading provider of auto, home and life insurance, providing products to more than 15 million U.S. households. There are significant degrees of overlap between LOBs, but each also has unique needs. Although infrastructure and application development are both centralized, each business unit has a dedicated relationship manager within application development who understands LOB needs and manages the interface with IT. Company B’s project management structure allows IT resources to leverage synergies while serving the needs of each LOB effectively.
**Differentiated organizational structure**

A differentiated organization decentralizes most technology functions and places them within business units, while maintaining a small, centralized IT group to set standards for the enterprise and provide common infrastructure support (see Figure 7).

**Figure 7. Example of a differentiated organizational structure.**

Company C is a diversified financial services company providing a range of services to individual and institutional investors – key LOBs include investment management, trust and custody. Technology leadership is a key competitive differentiator. Since each LOB has unique needs, over time the company developed a highly differentiated organizational structure. Each LOB had its own IT group, encompassing every function from infrastructure to application development.

However, recent market pressures heightened the need to leverage synergies across LOBs. As a result, Company C recently centralized its infrastructure group and office of architecture to set strategic direction for the enterprise. This modification of their diversified structure allowed the firm to realize some efficiencies while effectively meeting distinct LOB needs.
Transformational organizational structure

In a transformational organization, most technology functions reside in a centralized group, including a research team that is responsible for setting overall strategic priorities for future technology development. While application development is usually centralized in this model, the LOBs typically retain control of the business analysis function. In some cases, LOBs may have the option of sourcing application development from third parties (see Figure 8).

Figure 8. Example of a transformational organizational structure.

Company D is a diversified financial services firm offering a wide variety of business lines to both retail and institutional customers. Known as a technology leader, it invests heavily in IT. Company D has a transformational IT mandate and organizational structure which are designed to drive technology innovation across the enterprise. Most IT functions are centralized; however, LOBs maintain control of the business analysis function. To help ensure access to best-in-class resources, LOBs have the option of sourcing application development from the central IT group or from third-party vendors. Each LOB has a representative in a centralized research function that provides technology leadership across the organization.
When assessing their IT organizational structure, many financial services firms will find that there is some degree of misalignment between the strategic context, IT mandate and current IT organizational structure. Necessary changes in resource alignment, reporting relationships or key roles and responsibilities should be identified and executed as part of aligning the operational model with the IT mandate.

**Step four: Define the IT operational model**

Once the organizational model has been aligned, the remaining step is to tailor individual components of the operational model. The first step firms should take is to conduct a baseline assessment of their existing operational model to identify problem areas. Appropriate changes can then be made to address areas of misalignment.

In a well-aligned firm, core elements and enablers will vary depending on the IT organizational model they support (see Figure 9). For example, in a utility model interactions between business and IT are highly structured with a strong emphasis on process and formalized decision making. The project management model is characterized by a high degree of project management discipline and structure while differentiated models are more relationship-based and feature fewer formal decision-making forums. A transformational model is even less formal and typically relies on free exchange of ideas between business and IT staff at all levels.
<table>
<thead>
<tr>
<th>Operational model components</th>
<th>Utility</th>
<th>Project management</th>
<th>Differentiated</th>
<th>Transformational</th>
</tr>
</thead>
<tbody>
<tr>
<td>Governance</td>
<td></td>
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<tr>
<td></td>
<td>Multiple formal business/IT governing bodies drive decision making across all organizational levels; executive-level decision making is driven by the business</td>
<td>Business/IT governing bodies are mostly focused on the project and operational levels</td>
<td>Few formal business/IT decision making forums</td>
<td>Governing bodies are mostly focused on the executive and management levels to identify and drive organizational transformation</td>
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<tr>
<td>Process</td>
<td>Process roles and definitions are highly formalized; IT focuses on tactical execution, business plays more strategic role</td>
<td>High degree of process discipline around project management; IT participates in decision making but does not play central role</td>
<td>Established processes that outline roles and responsibilities; methodologies are mutually agreed to, but not strictly formalized</td>
<td>Informal interaction driven by close working relationships and shared responsibilities</td>
</tr>
<tr>
<td>Communications</td>
<td>Formalized, regular and standardized reporting details status of IT operations</td>
<td>Formalized, regular and standardized reporting around project completion, budget and issues</td>
<td>Open and frequent communication; not driven by formal reporting function but informal dialog</td>
<td>Informal, constant dialog surrounding business and IT strategic needs</td>
</tr>
<tr>
<td>Metrics</td>
<td>Not shared; IT metrics focus on operational support of business, not broader business results</td>
<td>Metrics for business and IT measure the project’s success in meeting both IT and business objectives</td>
<td>Shared metrics surrounding business success</td>
<td>Shared metrics surrounding business success</td>
</tr>
<tr>
<td>Skills</td>
<td>Business must develop industry-specific technology expertise and project management skills; IT skills are functional vs. industry specific</td>
<td>Business and IT must have strong project management skills</td>
<td>IT must have strong business-specific knowledge and strong internal networking skills to coordinate interface with the central IT group</td>
<td>Business and IT must have strong research and thought leadership skills</td>
</tr>
<tr>
<td>Style</td>
<td>May have separate cultures and styles</td>
<td>Team-focused culture driven by projects</td>
<td>Shared culture and style</td>
<td>Entrepreneurial, technology-focused culture</td>
</tr>
<tr>
<td>Shared vision</td>
<td>Efficiency and scale drives savings for the business unit and enterprise</td>
<td>Technology is a key enabler of business success</td>
<td>Technology leadership drives business success</td>
<td>Leverage IT to drive enterprise business transformation</td>
</tr>
</tbody>
</table>

*Source: IBM Institute for Business Value analysis.*
Take a look at your own alignment

As a first step in determining how effectively your own business and IT functions are aligned at an operational level, consider the following questions:

• Is your company’s strategic context commonly understood and clearly communicated throughout the enterprise?
• Is there a common understanding between business and IT regarding the role and orientation of IT?
• Is the IT mandate consistent with the strategic context?
• How well does the current IT organizational structure support the IT mandate? How will you change your IT organizational structure in response to shifting business priorities?
• Are the core elements and enablers of your operational model consistent with the IT organizational structure?

An operational model for business and IT interactions can align expectations, clarify roles and responsibilities and establish accountability and a shared code of conduct. Financial services organizations that implement effective models can improve the quality of IT services, increase trust among colleagues and raise business customer satisfaction.

Yet, operational alignment cannot remain static – business and IT must keep in mind that their model has to continually transform over time as strategic goals and working relationships change. It’s all about making strategy a reality by driving alignment from the top all the way down to day-to-day operations.
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References

