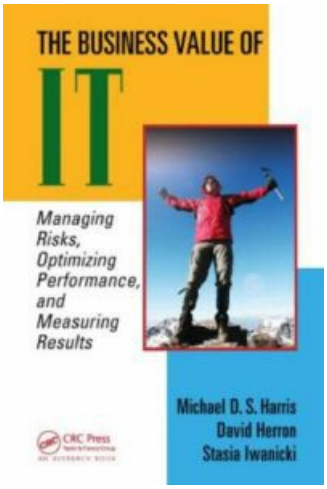

Book The Business Value of IT

Managing Risks, Optimizing Performance and Measuring Results

Michael D.S. Harris, David Herron and Stasia Iwanicki
Auerbach Publications, 2008

Recommendation

Too often, companies suffer from strained relationships between their businesspeople and their information technology (IT) staffers. Much of this irritation stems from differences in the way they view IT's contributions. Experienced IT executives Michael D.S. Harris, David Herron and Stasia Iwanicki's useful handbook explains how to get IT team members and organizational personnel to understand each other, initially by clearly defining IT's contributions in business terms. Besides valuable information, graphs, charts and chapter summaries, the authors include the references for everything they cite so you can dig more deeply into areas that affect your work. *BooksInShort* praises their ability to express their thesis in human terms rather than lapsing into dreary technical recitations, although the writing is sometimes awkward. While utterly focused on IT, their book is not too technical for managers who deal with those in the field. This book enables you to explore the strengths and weaknesses of a variety of IT-finance, data and measurement models so you can select the ones that fit your situation.

Take-Aways

- Organize your information technology (IT) department so that it can demonstrate its value to your business.
- Use a financial model that allows you to assess your real return on IT costs.
- IT spending must be flexible, but less than 1% of your firm's gross revenue is too little and more than 15% is too much.
- IT governance involves deciding who makes IT decisions and how, and holding them accountable.
- Outsourcing service agreements must support your business objectives and not just assure levels of performance.
- To manage IT wisely, you must measure and analyze its performance.
- Compare your IT against your industry peers' to find areas to improve.
- Prepare IT changes well. Keep everyone affected fully informed.
- Using IT to manage risk can prepare you to handle adverse events.
- Cultivate strong working relationships between business personnel and your IT team to eliminate conflict.

Summary

Can IT Provide Real Business Value?

In most companies, the information technology (IT) department does not make a direct financial contribution, but it does provide the communication and data infrastructure that enables nearly every transaction. For your firm to realize a good return on its IT costs, the IT unit must:

- Provide solid information for all levels of decision making.
- Show that it earns real value in exchange for its expenditures.
- Assist in risk management with the right infrastructure, expertise and information.
- Document and assess all the business processes that run through its infrastructure.
- Respond to business needs and support its end users.
- Help the company compete by being innovative and improving its systems.

The Value Metrics of IT

Businesses live and die on hard numbers, so IT managers must be able to explain clearly how their work contributes to the company's business value, and how IT systems and processes fit its goals. Many financial models can help you demonstrate IT's real bottom-line return, including:

- **"Total Cost of Ownership" (TCO)** – This model tracks costs from the time that the firm buys an "IT asset" until that asset reaches the end of its useful life. Future costs are hard to predict, but this is a good way to compare alternatives.
- **"Return on Investment" (ROI)** – This metric quantifies how the firm realizes business value for its IT costs. ROI expresses the value of hard costs better than it conveys the impact of intangible savings.
- **"Economic Value Added"** – This metric works like ROI, but it is based on the opportunity costs (the costs you indirectly incurred by not investing the money differently) instead of on the internal rate of return.
- **"Real Options Valuation"** – This metric calculates an IT project's value by weighing its ongoing and future fiscal impact. It is particularly helpful in evaluating the choices involved in start-up projects.
- **"Return on Assets" (ROA)** – This is the net income an IT project generates divided by the total cost of the assets it used to earn that income.
- **"Return on Infrastructure Employed"** – This works like ROA, but it bases its ratio on the cost of IT services instead of the cost of IT assets.

Getting the Right Return from IT

Your business must obtain all the information technology it needs at the best possible price and use of time and other resources. Too many firms become so focused on IT that they lose sight of their goals, letting their IT systems turn into black holes that pull their companies into a void. Instead, define the role IT should play in helping your firm reach its goals, what its budget should be (including maintenance), and how to adapt its systems to competitive realities. Your objective is to build a robust but supportive IT function with contained costs. Strict cost management is the only way to get a good ROI. Every firm is different, but the following broad guidelines indicate appropriate levels of IT spending. Check your IT budget against gross revenues. This is like a "miles-per-gallon rating for your technology investment." If the IT budget is:

- "Less than 1%" of gross revenues, you are starving IT and cheating your business.
- Between "1% and 2%" of revenues, IT is merely in survival mode.
- At "2%-3%" of revenues, large firms can fund IT at this level, but not small firms.
- With "3%-6%" of revenues, you can have a robust IT unit pursuing strategic projects.
- If you spend "6%-15% "of revenues on IT, ask if that cost level makes strategic sense.
- At "more than 15%" of revenues, you definitely need to get a grip on IT expenses.

IT Governance Models

To creating a thoughtful, IT governance program, first select your basic IT "operating model." Designate the goals you think a good IT operation should accomplish, the budget it will need, how your firm will track and manage that budget, which managers and staffers should make IT decisions, and how the company will evaluate their decisions and hold them accountable. No IT operating model is perfect, so weigh your choices in terms of clear benefits for your company. Your operating-model options include:

- "Capability Maturity Model Integration" (CMMI®) evaluates your company's IT maturity and provides a road map for developing IT operations to full capacity.
- "Control Objectives for Information and Related Technology" (COBIT®) is designed for auditors. It enables companies to manage IT security and governance issues.
- The "IT Infrastructure Library" (ITIL®) is a source of information on best practices. Refer to it for information on designing and implementing IT processes.
- The "International Organization for Standardization" (ISO) provides more than 16,000 benchmarks for assessing how well your IT program meets industry standards.
- "Project Management" operating strategies are increasingly based on measurable parameters. This is crucial with IT projects that span organizational boundaries.
- "Six Sigma" is a widely used method for increasing quality and reducing variability. Its goal is to create processes with fewer than 3.4 defects per million operations.

IT Outsourcing

The decision to outsource IT or other functions rests upon identifying which tasks are central to your organization's "value proposition" and which jobs you can delegate to expert service providers. While you may examine which functions your competitors outsource, your firm probably needs its own distinctive mix of in-house and outsourced services. First, determine which in-house operations an easily available vendor could provide at a lower cost. To outsource any function, including IT, you need to create a service level agreement (SLA) defining what the vendor will deliver. Set quality standards, deadlines, costs and processes. Align the SLA with your company's goals and carefully define a method for monitoring the services you are buying.

IT Tools

Select software and systems that enable you to deliver high-quality IT efficiently, effectively and economically. To evaluate such tools, first determine how they meet your needs, whether they fit your existing systems, whether you can adapt them as those needs change and what support costs they involve. Whether you will use these tools for "service support" or "service delivery," make sure they comply with relevant industry standards. Take the time to get this right, because undoing the purchase of unsuitable IT software and systems is costly and time-consuming.

The Performance Metrics for IT

Measure the value of IT's performance at the organizational level where it is delivered. The four crucial metrics are "cost, quality, duration and customer satisfaction." To assess customer satisfaction, survey your customers and monitor their after-sales service activity.

> "It is natural for businesses to treat IT architecture as unfathomable technical babble. However, it is important for business leaders to ask questions in nontechnical language and require answers in equally nontechnical language."

The measurement data you collect can help increase productivity, demonstrate IT's value and provide criteria for business decisions. To derive information you can really use, gather both quantitative (hard number) and qualitative (subjective) measurements. Use quantitative data to establish baselines, and use subjective analyses to assess and demonstrate your capabilities. In combination, these analyses will enable you to track changes and trends in your results, identify improvements and diagnose areas that need corrective action.

How Do Your Industry Peers Handle IT?

Examine the way other companies in your industry manage IT to scout for lessons. Going beyond your direct competitors, you may want to consider the IT practices of your vendors, customers, and other organizations of similar size, geography or regulatory circumstances. Obtaining this information will take time and effort, so you may want to work with an IT consulting firm. To get the most use from the data, create baselines for the organizations you intend to study, and track their performance over time against yours.

IT Change Management

Your firm's internal needs, like upgrades, expansion or business model shifts, can provoke IT change, as can external forces, such as new regulations, standards or competitors. Use the "seven principles of managing change" to handle your IT upgrade project. They are:

1. **"Two levels of management support"** – Change requires support from the company's top people. To make it last, get support from two layers of administrative authority.
2. **"Proper funding"** – Creating change requires having the right resources, including an adequate budget with emergency reserves to handle the unexpected.
3. **"The business case"** – Writing your argument for change will help you see its implications and assess the validity of your plans.
4. **"Setting and managing expectations"** – If you don't help your top managers and your stakeholders see and accept your vision for change, they will impose their own.
5. **"It's about the people"** – To enlist cooperation despite people's natural resistance to change, make sure those affected know and accept what change will bring.
6. **"Communicate, communicate, communicate"** – Give all of the people who are involved with your transformation project all the information they need.
7. **"Measurement is key" –** You can't manage what you can't see and you can't see what you don't measure. Determine what factors matter to your project and measure them.

IT Risk Management

Risk is the probability that the future will not conform to your plans, and the degree of risk is how much it will deviate. Your goal is to minimize your exposure to risks that will thwart your IT projects or impede your operations. Use experts within your firm or retain risk management consultants to help you assess the hazards you face and their likely impact if they occur. Look at the risks involved with your company's financial health, reputation and legal liabilities. Assess risks ranging from the impact of losing knowledge when a key employee leaves to the ways that a natural disaster might affect your firm. You can implement internal policies and procedures to minimize some risks. In other cases, you can shift risk by outsourcing some functions to external sources. Of course, you must have the right insurance to protect against catastrophic loss.

Identifying a Great Chief Information Officer (CIO)

A Chief Information Officer's ability to lead a technical staff is a given, but the right CIO will go beyond that to provide a vision of IT that supports your company's goals and inspires its people. Your CIO must be able to manage the technical and human aspects of the IT department and to communicate correctly with everyone involved. Nontechnical people should be able to grasp your CIO's ideas easily while technical folks must be reassured that he or she thoroughly knows the field. Your firm's other C-level executives will expect the CIO to understand the principles of your business. The CIO needs the right local, national and international experience and connections, and the ability to attract, hire, develop and keep strong IT talent.

What Does IT Need from the Business End?

Too many IT staffers have poor relationships with people in the business operations they support. Do not let this happen. Make sure your IT managers and employees understand your business and what it needs from them, and be sure your operational people know what the IT team needs and how its technical functions crucially support their work. Ensure that the people on the corporate side and the IT side of your business work together well and see themselves as members of the same team with the same objectives. Cultivating mutually supportive working relationships will solve most of the usual difficulties between business-end staffers and information technology providers.

About the Authors

All three authors are experienced IT executives. Engineer **David Herron** co-founded and **Michael D.S. Harris** owns the David Consulting Group. They work with IT Decisions Coaching, where Harris is a partner. Herron has co-written two books and numerous articles on functional measurement. **Stasia Iwanicki** is a Six Sigma Black Belt with 18 years global IT experience.