Is IT Cost Accounting Worth The Effort?

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Presentation Overview

- Principals Of IT Cost Accounting
- UCLA IT Service Costing
- Cost Allocation – A University Perspective
Principles of IT Cost Accounting
Why Allocate IT Costs?

IT Cost Allocation will enable leadership to make, sponsor and enforce the right decisions by providing timely and actionable IT service information.

By unveiling the true and total cost of IT services... ...IT Cost Allocation supports the following business and IT imperatives

• Identification of opportunities to reduce IT spend
• Increased cost accountability within Service Management by increasing financial transparency between the provider and consumers
• Improved resource and asset utilization by enabling financial and non financial service performance reporting capabilities
• Improved sourcing decisions / supplier management by increasing benchmarking capabilities
• Improved customer relationship management capabilities by efficiently demonstrating value provided to the business
• Simplified service planning and financial budgeting processes by providing a multidimensional view of actual vs. planned performance

Common practice: Total cost of service is often hidden

[Image of an iceberg, with only a small portion above water, representing the hidden costs of IT services.]
Analysis of IT Costs involves the identification and segregation of a number of different cost components.

**IT Cost Components**

- **Labor**
  - Direct
  - Indirect
  - Benefits

- **Expenses**
  - Accounts Payable

- **Capital**
  - Equipment Depreciation

- **Service Catalog**
  - Service Lines
  - Sub Services
  - Activities
  - Customer Facing Services
  - IT Facing Services

- **Projects**

- **IT Department Overhead**
### Sample Service Catalog

Determining the services/subservices that will be tracked for cost analysis is a key first step.

<table>
<thead>
<tr>
<th>Service</th>
<th>Subservice</th>
</tr>
</thead>
<tbody>
<tr>
<td>Academic Learning</td>
<td>Blackboard</td>
</tr>
<tr>
<td></td>
<td>Canvas</td>
</tr>
<tr>
<td></td>
<td>Clickers</td>
</tr>
<tr>
<td></td>
<td>ClickShare - Barco</td>
</tr>
<tr>
<td></td>
<td>eText Digital Learning</td>
</tr>
<tr>
<td></td>
<td>Everspring</td>
</tr>
<tr>
<td></td>
<td>Keep ToolKit ePortfolio</td>
</tr>
<tr>
<td></td>
<td>Starfish Appointment Scheduler</td>
</tr>
<tr>
<td></td>
<td>VoiceThread</td>
</tr>
<tr>
<td>Classroom Technology</td>
<td>Classroom Media Controllers</td>
</tr>
<tr>
<td></td>
<td>Crestron - Extron</td>
</tr>
<tr>
<td></td>
<td>Instructional Design</td>
</tr>
<tr>
<td></td>
<td>Media Equipment</td>
</tr>
<tr>
<td></td>
<td>Mobile Lab (check-out cart)</td>
</tr>
<tr>
<td>Video Services</td>
<td>Adobe Connect</td>
</tr>
<tr>
<td></td>
<td>Conference Room Setup</td>
</tr>
<tr>
<td></td>
<td>Echo 360</td>
</tr>
<tr>
<td></td>
<td>Immersive Telepresence</td>
</tr>
<tr>
<td></td>
<td>MediaHub</td>
</tr>
<tr>
<td></td>
<td>Tandberg</td>
</tr>
<tr>
<td></td>
<td>UC Lync</td>
</tr>
</tbody>
</table>
Sample Activity List

Tracking costs to the Activity level can provide IT management useful information regarding where their staff spend their time.

<table>
<thead>
<tr>
<th>Partial Activity List</th>
</tr>
</thead>
<tbody>
<tr>
<td>Administrative Support</td>
</tr>
<tr>
<td>Asset Management</td>
</tr>
<tr>
<td>Backup/Data Restoration</td>
</tr>
<tr>
<td>Coding/Build</td>
</tr>
<tr>
<td>Communication</td>
</tr>
<tr>
<td>Consulting</td>
</tr>
<tr>
<td>Customer Support / Troubleshooting / Security Assistance</td>
</tr>
<tr>
<td>Design</td>
</tr>
<tr>
<td>Installation/Implementation</td>
</tr>
<tr>
<td>Maintenance</td>
</tr>
<tr>
<td>Monitoring</td>
</tr>
<tr>
<td>Planning/Information Gathering</td>
</tr>
<tr>
<td>Project Management</td>
</tr>
<tr>
<td>Reporting</td>
</tr>
<tr>
<td>Testing</td>
</tr>
</tbody>
</table>
Design Principles

An IT Cost Allocation model should be built around a number of key design principles.

- Service costs must represent full cost and must include both direct and indirect costs, including an appropriate portion of overhead.
- Service costs should be based on the principles of Activity Based Costing to estimate the true cost of the service.
- The service cost model should leverage acceptable estimates for cost elements where specific data metrics are not easily obtained.
- Service costing should be based on prior-fiscal year actual transactions and include justifiable adjustments based on known future conditions.
- Internal services consumed shall be taken into account and included in the cost of service – however, circular allocations will be avoided.
- Consistent service costs should be used for both internal and external customers.
- The calculations behind the rates must be transparent so that customers have confidence that they are equitable and reasonable.
Cost Flow Model

Direct Costs
- Direct Labor
  - Labor & Benefits
- Direct Non-Labor
  - A/P Purchases

Indirect Costs
- Indirect Administrative
  - Overhead
- Indirect Infrastructure
  - Overhead

Sample IT SERVICE

HR / Finance / CIO
- Labor & Benefits
- A/P Purchases

Data Center / Network / Security
- Labor & Benefits
- A/P Purchases

Time Capture System
- CC / Project / Activity

A/P System Entry
- CC / Project

Allocation Process

Indirect Infrastructure
- Overhead

Indirect Administrative
- Overhead

Direct Labor
- Labor & Benefits

Direct Non-Labor
- A/P Purchases

A/P System Entry
- CC / Project
### Outcomes

Once all costs are accounted for, funding vs. expense analysis can be performed.

<table>
<thead>
<tr>
<th>Cost Driver</th>
<th>Service 1</th>
<th>Service 2</th>
<th>Service 3</th>
<th>Service 4</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Employee Cost</td>
<td>$100,000</td>
<td>$50,000</td>
<td>$250,000</td>
<td>$25,000</td>
</tr>
<tr>
<td>Transaction Cost</td>
<td>$30,000</td>
<td>$45,000</td>
<td>$60,000</td>
<td>$15,000</td>
</tr>
<tr>
<td>Capital Asset Cost</td>
<td>$15,000</td>
<td>$10,000</td>
<td>$20,000</td>
<td>$5,000</td>
</tr>
<tr>
<td>Overhead Allocation</td>
<td>$10,000</td>
<td>$8,000</td>
<td>$15,000</td>
<td>$3,000</td>
</tr>
<tr>
<td>Total Cost</td>
<td>$155,000</td>
<td>$113,000</td>
<td>$345,000</td>
<td>$48,000</td>
</tr>
<tr>
<td>Funding Source 1</td>
<td>$95,000</td>
<td>$35,000</td>
<td>$255,000</td>
<td>$5,000</td>
</tr>
<tr>
<td>Funding Source 2</td>
<td>$55,000</td>
<td>$80,000</td>
<td>$90,000</td>
<td>$45,000</td>
</tr>
<tr>
<td>Total Funding</td>
<td>$150,000</td>
<td>$115,000</td>
<td>$345,000</td>
<td>$50,000</td>
</tr>
<tr>
<td>Difference Between Cost and Funding</td>
<td>($5,000)</td>
<td>$2,000</td>
<td>--</td>
<td>$2,000</td>
</tr>
</tbody>
</table>
Huron’s approach to performing cost allocation projects:

1. Gather Prior Year Actual Data
2. Build Model In Excel
3. Analyze Results
4. Refine The Model
5. Operationalize The Process
IT Services

- Central IT service provider for the university (but not the only IT group on campus)

- Four primary service lines
  - Application Services
  - Information Management Services
  - Infrastructure Services
  - Networking & Communications

- Five secondary service lines
  - Customer Support
  - Service Management
  - Program Management
  - IT Architecture
  - IT Security

- 395 employees and contractors
- $63.2 million operating budget

- Over 42,000 students
- Ranked second among public universities and most applied to university in the world (105,000 applications for Fall 2014)

- UCLA Health System ranked in the top five of US hospitals and “Best in the West”

- Over $1 billion in annual research funding (5th in the nation) and more than 100 companies created based on technology developed at UCLA

- 13 Nobel laureates, 111 NCAA championships and 250 Olympic medals by student athletes

- $5.4 billion annual operating budget
IT Costing Challenges

Run IT like a business, promote growth and expand market share in the University’s opt-in environment

- Promote greater IT cost efficiencies and increase the value of services while continuing to support the University’s mission
- Foster a customer-focused environment where IT Services acts as a market driven service provider and/or broker
- Align rates with service costs, ensure accurate cost recovery and increase the transparency of recharge, billing and financial reporting
- Enable effective decision-making regarding service development and support
IT Costing Project Objectives

- Update the existing service portfolio structure, supporting cost data and allocation mechanisms
- Design a service cost model that captures the full cost of IT services and enables:
  - Cost allocation and chargeback / showback
  - Cost accounting, analysis, budgeting, and forecasting processes
  - IT financial management and reporting
- Build service cost models and rates for high value IT services
The costing project at UCLA was initiated last November

- Data gathering, defining the service catalog, and creation of an initial excel-based costing model – six months
- Calculation of revised chargeback rates, requirements definition and software selection for operationalizing the model – five months
- Implementation of solutions to automate the model and related reporting (TBD)
  * Expanded time reporting
  * More detailed financial transaction tagging
  * TBM solution implementation (Apptio TBM or VMWare ITBM)
  * Integration with service management (ServiceNow)
  * Improved planning, budgeting and analytics
### Project Value

The new service-based costing models were designed to remedy gaps encountered with the previous state and take into account requirements for rate setting processes.

<table>
<thead>
<tr>
<th>Theme</th>
<th>Issue</th>
<th>Resolution</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Accuracy</strong></td>
<td>Out-dated allocation mechanisms</td>
<td>Relevant and transparent allocation mechanisms</td>
</tr>
<tr>
<td></td>
<td>Cost center based approach</td>
<td>Service-centered approach</td>
</tr>
<tr>
<td></td>
<td>Historic classification of indirect services</td>
<td>Updated classification and distinction of what constitutes an indirect service</td>
</tr>
<tr>
<td><strong>Simplicity</strong></td>
<td>Outdated, complicated service catalog</td>
<td>Simplified customer focused service catalog</td>
</tr>
<tr>
<td></td>
<td>Inconsistent allocation of indirect costs</td>
<td>Systematic approach to allocating indirect costs</td>
</tr>
<tr>
<td></td>
<td>Inconsistent service cost calculation between customers</td>
<td>Consistent service cost calculation regardless of customer</td>
</tr>
<tr>
<td><strong>Transparency</strong></td>
<td>Limited reporting capabilities for some services</td>
<td>Total cost reporting capabilities for individual services</td>
</tr>
<tr>
<td></td>
<td>Limited documentation to substantiate processes or calculations</td>
<td>Step-by-step documentation and explanations detailing decision making and methodology</td>
</tr>
</tbody>
</table>
Benefits to Date / Expected

- Modernized and rationalized the service catalog
- Explicit business rules for handling costs (direct, indirect, overhead, fixed and variable), service types (customer facing, internal and mixed), depreciation for renewal and replacement
- Alignment of services and rates with multiple and various funding sources (central funding, recharge, technology tax, contracts and grants)
- Improved service portfolio management capabilities supported by customer, business, and IT views of the catalog
- Enhanced credibility with customers, stakeholders, budget office and IT governance committees
- Foundation for benchmarking and assessment of competitive position
Cost Allocation –
A University Perspective
“Towering Toward the Blue”

- Founded in 1865
- Member of Association of American Universities since 1909
- 28,000 students, 2,600 faculty and 10,000 staff on five campuses
- Students from all 50 states and 105 countries
- 13 schools and more than 360 degree programs
- 26 Rhodes Scholars
- #1 ranked programs: Special Education, City Management & Urban Planning
- #4 in NIH grants and contracts for pharmacy research
### Institutional Background

#### Accountability
- Tuition costs continue to rise
- For public institutions, state appropriations dropping
- Much of this expense is shouldered in the form of student debt
- These costs make students question the value of a 4 year education

#### Responsibility
- White House initiatives to make college more affordable, degrees more beneficial
  - Paying for performance
  - Demonstrating value
  - Tracking causes for success and failure
  - Controlling and driving down costs
  - Increasing efficiency

#### Opportunity
- Changing for Excellence
  - IT Centralization
  - Demonstrates service utilizations, and “Open Dialogs”
  - True “Showback” costs
- Cost Savings
  - Accurate analysis on outsourcing vs. insourcing
  - True capital asset and time tracking
  - Not About Defending IT, about Value of IT
### Impact of Cost Allocation

#### Before
- No real accounting of TCO or ROI
  - IT and external departments made uninformed / under-informed investments
  - Value of products and services largely unknown
  - Trying to keep up with maintenance expenses
- Siloed investments did not contribute to University strategic plan

#### After
- High assurance of actual cost
- Responsible steward of funds
- Enabling academic and research missions
- Able to answer hard questions up front, with facts to back answers
- Thoughtful and prepared to address campus needs
Project Timeline

The IT costing project at KU began in August of 2013. The general timeframes required to complete the key activities have been as follows:

- Data gathering, definition of service catalog, and creation of the excel-based initial costing model – 3 Months

- Expanding the model, implementing a time capture system and creating an automated solution to operationalize the costing model and process – 9 months

- Pilot group of IT staff began tracking and recording time in June, 2014

- All IT staff began tracking and recording time in July, 2014
Benefits to Date

- Transparency for customers
  - Showback for centralized resources
  - Justification for rates
- Accurate data for informed decision making
- Identify “hot spots” in the market
- Reallocate resources to balance workload
- Prevent double counting
Lessons Learned

- Keep It Simple
  - The bigger the list of services/subservices, the more complex the model will become

- Clarify Scope
  - IT Costing, Project Reporting & Management Reporting all overlap in this space

- Work With Actuals, Not Budgeted Amounts
  - Actuals allow for balancing with financial reports

- It Is Possible To Leverage Existing Systems
  - Hyperion, Cognos, FMW, Apptio all support an operational model
Lessons Learned

- Aligning the services, cost model and funding sources takes substantial effort from outside-in, top down and the bottom up.

- Identifying unit drivers and gathering consumption metrics is a significant effort.

- Developing capabilities for proactive service and service line management in a public university is a considerable challenge.

- Automating all the parts related to effective IT business management is a big task that needs to be phased and evolutionary.
Lessons Learned

- **Leadership**
  - Easy to derail without leadership commitment

- **Internal & External Resources**
  - Don’t underestimate resources needed to exact organizational change
  - Have clear understanding of roles, responsibilities, and accountability when using an external partner

- **Cross-Functional Project Team**
  - Identify key internal and external team members
  - Diversity on the project team will provide better insights and lead to better decision making
  - Keep campus partners in the loop throughout the process
Help Us Improve and Grow

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