Xyberspace consulting, inc. essay sample

Business, Strategy

Laura Barnes finished her chicken fajita and looked out upon Town Lake, shimmering under the fierce Texas sun. She had recently relocated to Austin from Silicon Valley to head up the Accounting Department for Xyberspace, a rapidly growing technology-consulting firm. Only two weeks on the job, she was being asked to resolve a controversy within the company. The controversy centered on the allocation of the costs associated with the company's Training and Education Service Group to each of the company's profit centers that used those services. Opinions on the issue were heated, and she had come to the lakeshore with her notes to calmly sort out the facts and consider the relevant issues. Her manager and Xyberspace's CFO, Martin Henry, had made it clear he expected a quick resolution of the controversy, which he felt was hurting company morale and had large strategic implications for Xyberspace. Background

Xyberspace was a successful Internet consulting firm located in Austin, Texas. The company's Consulting Group provide e-strategy solutions to corporate and non-profit clients, while the Customer Care Group performed IT implementation and provided telephone, e-mail, and on-site client support. As Austin became home to an increasing number of Internet start-ups as well as established high-tech firms, Xyberspace had grown rapidly. The company employed 800 people, 500 of whom were consultants and 250 of whom were Customer Care Technicians. The remaining 50 were either corporate officers or performed corporate functions such as accounting, marketing, training, and public relations. The company owned its own building in downtown Austin.

Training was an integral part of the company's strategy, and Xyberspace was wholeheartedly committed to training and continuing education. According to Richard Malinovich, the company's founder and CEO, " Our goal is to have absolutely the best-educated consultants in the marketplace. We think this will set us apart from many firms who no doubt have bright people, but who don't invest anywhere near what we do in education. And I am absolutely convinced that training our consultants in-house is critical to achieving this goal." All employees of the Consulting and Customer Care Groups were required to receive one full week of computer training twice a year on Internet-related languages such as html, xml, perl, and cgi scripting, and Java as well as tutorials on software packages from Oracle, Vignette, Siebel, and other firm partners. The actual content of the classes depended on the newest software developments as well as the Consulting and Customer Care Group's strategic focus areas. For example, the health-care practice of the Consulting Group had recently received customized training in the latest hospital automation software. The Training and Educational Services Group spent much effort and resources to design courses for its consultants built around Xyberspace's client needs.

Classes generally lasted one week and could cover a number of different topics. The normal class size was ten people, and three classes were typically going on at any one time. The Training and Educational Services Group had found that trainees generally preferred smaller "class sizes, which tended to work better because courses were often designed around specific needs the trainees had in serving their clients. Company policy stated that all employees received two weeks of training, but experience had shown that, on average, 75% of employees actually were able to complete the training, and this way the figure used in budgeting for the Training and Educational Services Group. Employee turnover played a part in determining the participation rate, as did the fact that some employees on long-term assignments simply could not find the time to undergo training. Others were able to complete one week of training but not two.

The Training and Educational Services Group Budget

The total Training and Educational Services Group budget for the prior year was $497, 700 (see Exhibit 1). The budget was based on the company’s estimate that the Training and Education Services Group would conduct training sessions for 450 employees during the course of the year. It was estimated that 300 consultants (75% of the projected annual average employment total of 400) and 150 Customer Care employees (75% of the projected annual average employment total of 200) would received two weeks of training each year for a total of 900 training sessions. During the balance of the year, trainers prepared course materials and devoted time to learning new software, languages, and systems. The budget consisted of the following items:

Salary ($250, 000): One group manager made $75, 000 per year, an office assistant made $25, 000, and three full-time trainers made $47, 000, $48, 000, and $55, 000, respectively. The office assistant scheduled the training for the company’s employees and handled administrative functions for the group. The group manager oversaw the other four employees, set training priorities and teaching schedules, and acted as a trainer herself as needed.

Benefits ($50, 000): Employee benefits such as health insurance, etc. were 20% of salary. Software Licenses ($20, 000): Generally, half of the software licenses were negotiated in advance. However, since Xyberspace liked to make sure that its employees stayed up-todate on the latest releases, an additional $10, 000 was budgeted to cover additional software that may need to be purchased during the year. The software license covered Training and Educational Services Group computers only.

Depreciation ($28, 000): 35 computers were purchased at $4, 000 each and were depreciated on a straight-line basis for five year.

Maintenance Contract ($2, 000): This annual fee paid to the computer vendor covered all of the computer equipment and provide for repair or replacement of defective hardware within 24 hours. Course Development ($12, 500): Since the Training and Educational Services Group developed many of its own training materials specifically for company use, trainers worked with outside editors, graphic artists, and print shops to develop course materials. Professional Development ($10, 000): This included membership in professional associations and fees to attend conferences and training sessions to facilitate their staying current with software developments and enhancements and to learn new software programs and languages as needed.

Travel ($8, 800): This included travel expense for travel to attend conferences and/or workshops.

Phone/Fax ($2, 600)

Office Supplies ($800)

Training Supplies ($67, 500): It cost the Training and Educational Services Group $75 per trainee to print and distribute new manuals and workbooks. Lunch ($45, 000): Catered lunches were $10 per person per day, or $50 per trainee, for each 5-day training session. Since the training was intensive and many participants preferred to work through lunch, catered meals were much appreciated. In addition, past experience had shown that allowing class participants to go off-site for lunch often resulted in participants being late for afternoon sessions.

Other ($500): this amount covered miscellaneous expense not covered elsewhere.

Based on the Training and Educational Services Group’s budget of $497, 700 and expectations about training usage of 900 sessions, the expected allocation rate per training session was $553 (Exhibit 1).

Allocating Costs Associated with the Training and Educational Services Group While the Training and Educational Services Group prepared a budget at the beginning of each year, actual costs were allocated at the end of the year based on the Training Group’s actual expenses and the user departments’ actual usage of training services. Exhibit 2 reports that actual expenses for the Training Group for the prior year totaled $548, 625. In addition, the Consulting Group received 600 training sessions, and the Customer Care Group received 225 training sessions during the year. As a result, the actual allocation rate charged to the user departments was $665 per training session.

The Controversy

Laura Barnes recalled the meeting she and Martin Henry had yesterday with Regina Rosethal, David Anderson, director of Xyberspace's Consulting Group, and Rajit Gupta, director of Xyberspace's Customer Care Group. Neither Barnes nor Henry had anticipated the objections raised by David Anderson to the costs of Training and Education Services that had been allocated to his group for the prior year:

" First of all, I was charged $665 per training session last year when I had budgeted $553 per session… I don't get it. I used 600 training sessions, just like I had planned to. And not only that, I can get outside training for $500 per session, which is even less than we budgeted to start with. I was willing to swallow the additional cost because I think the trainers do a good job. And I like the extent to which they can customize the training to the needs of my consultants. However, it does hurt to pay above market rates, especially when you're running profit center like I am. I can't keep training my people here when I can go somewhere else for only $500 per sessions.

Rosenthal, however, didn't think the cost was too high:

" I have a lot of fixed costs that I work hard to control, but they are going to occur whether we train 50 people or 500 people. Granted, our costs may be higher at this point than some outside companies, but with the growth in our company I think the fixed portion of our costs will be allocated across more training sessions, and the rate should go down. And besides, there are huge benefits to training inside."

Barnes thought that Rosenthal was onto something with her distinction between fixed and variable costs. In her experience, many companies separated these costs, allocating fixed costs from support to user departments as a lump sum and charging user groups based on the variable costs of each incremental service. She was determined to take a close look at this particular situation and recommend a cost allocation system that would be fair to all sides. While Rosenthal said she didn't think that her department would again exceed its budget by 10%, she did believe that the increases in last year's spending had been necessary to maintain the quality and quantity of training demanded by her clients.

" It's true we did have to hire a new assistant last year and that cost us more than we expected…. In addition, we had to increase the salaries of our trainers more than expected to remain competitive. With software licenses, we try to be conservative in our budgeting but sometimes we are simply told by the Consulting and Customer Care Groups, ' You need to buy this software and train our people in it.' It is very much a function of what is hot at the moment and we have no control over that. Professional development and travel expenses were higher than last year, but again that was because of new software products that we had to get up to speed on. In order to deliver the best possible training, we need to get trained ourselves and stay up-to-date on the newest releases. Regarding the telephone expenses and the increased price of the catered lunches, these are things we will try to control better this year. Our food vendor foisted a price increase on us during the middle of last year, and we didn't have time to shop around for a new vendor because we were too busy."

While Rosenthal admitted that some expenses were controllable, she believed the groups should be allocated actual training costs. “ If the group managers are going to demand we do certain things, then they need to bear those,” shreasoned. “ Of course I can stick strictly to the budget, but then my clients won’t get the services they want and will be disappointed.” Anderson disagreed, saying that allocating actual training costs gave the Training and Educational Services Group no incentive to control costs. “ Part of the reason their costs are so high is that they can simply pass them off to other groups…. I’m not saying they are not telling the truth when they say that they need to spend money to do a good job but if they have to bear the brunt of budget variances, they may think twice before going to another conference or paying extra for meals.”

Barnes would see both points of view. Anderson didn’t want to put himself at the mercy of the Training Group’s spending, especially since he was compensated based on the profitability of his group. Rosenthal also didn’t want to be hamstrung by a provisional budget, especially if her "spending depended on the sometimes rapidly changing needs of the user groups. Using budgeted rates would force the Training Group to stick to its budget, but would limit its flexibility to respond to client demands.

Anderson continued: “ Our having to cover the Training Group’s cost overruns is bad enough… but we also get penalized if the Customer Care Group doesn’t use as much training as they say they’re going to. Last year, we used 600 training sessions, just like we had originally budgeted. The Customer Care Group though, only used 225 sessions, so we ended up paying quite a bit more per session. It isn't fair that we have to cover more of the Training's costs just because the Customer Care Group used less of their services this year. Again, this is something over which I have no control. I used exactly the amount of services that I said I would, and I'm being penalized for that. Maybe next year I'll just wildly overestimated the amount of training we'll need, so that I can use less and make the Customer Care Group pay the difference."

The Customer Care Group's Manager, Rajit Gupta, argued that the Consulting Group should bear a higher portion of the Training Group's cost. " Granted, we had trouble sending people to training last year," he admitted. " But we should not be charged for services we didn't use." On this point, Rosenthal made no argument. In previous years, both groups had come very close to their budgeted usage amounts, so it hadn't been an issue. The Customer Care Group, however, had been going through significant turmoil last year due to a high amount of employee turnover and had not managed to send a sufficient number of employees to training. Questions

Prior to leaving for the lakeshore for the weekend, Barnes had collected data on the actual costs incurred during the prior year by the Training and Educational Services Group and summarized several statistics regarding actual training sessions attended by the Consulting and Customer Care Groups (see Exhibit 2). She was sure she would find this information helpful as she reflected on the issues.

It seemed to Barnes that there were key allocation questions involved in the controversy at Xyberspace. First of all, did the training and Educational

Services Group's use of a single rate cause its services to look too expensive to the Consulting and Customer Care Groups? Would a dual rate, which separated fixed from variable costs, better capture the true costs of the training? Second, should budgeted or actual rates be used to allocate training costs to the user groups? Finally, should the user groups be allocated training costs based on their budgeted or actual usage of services? Just how should the costs of the Training and Educational Services Group be allocated?