EXECUTIVE INSIGHTS

Navigating Operating Model Complexity in Residential and Facilities Services

As service companies grow organically and through acquisition, be it of sole proprietor mom-and-pops, scaled local companies or national-level providers, many find themselves struggling to settle on an optimal operating model. Indeed, many tend to approach operating model design in a way that is ad hoc at best.

This is a missed opportunity. Service companies with effective operating models generally have greater agility and higher levels of employee satisfaction. They also financially outperform service companies with less effective operating models.

That is what emerged from a series of in-depth discussions L.E.K. Consulting had with several branch-based service companies, both residential- and commercial-focused. Designed to identify common patterns that lead to successful operating models following a transition, these discussions made clear how important it is to align capabilities with bandwidth, ensure the accountability of leadership and deploy effective sales strategies.

While there is no silver bullet, there are systematic tradeoffs, inflection points and purposeful — as opposed to ad hoc — choices that branch-based services organizations should take into consideration along the way.

Many service organizations struggle to make operating model choices

There are a number of key questions that service companies are faced with as they grow, the answers to which will ultimately determine what their ideal operating model should comprise. From strategic objectives (e.g., What are the primary goals we hope to achieve through expansion?) to the desired execution timeline (e.g., How quickly do we want to fully integrate new branches/acquisitions?) to labor retention (e.g., How do we ensure that we retain key personnel?), a successful operating model will provide satisfactory answers to all these questions (see Figure 1).

Figure 1

Key questions impacting operating models

Expansion considerations

Key strategic objectives

- What are the primary goals of expansion (e.g., margin improvement, operational efficiency, topline revenue growth)?

Customer relationships

- How do we service multiregional customers?
- How do we best maintain existing relationships while pursuing new customers?

Primary expansion method

- What is our primary expansion method (e.g., organic, inorganic, hybrid)?

Execution time

- What is our desired time-line to accomplish key strategic goals?
- How quickly are we aiming to fully integrate new branches/acquisitions?

Playbook

- What is the best route to assemble a playbook of best practices?
- How do we ensure the playbook is dynamic and accounts for changing market conditions?
- How do we best dis-seminate the playbook throughout the company?

Resource requirements

- What is our access to funding for expansion (inorganic and/or organic)?
- How do we distribute equipment between new and existing branches?
- What are the real estate, personnel and equipment requirements to enable expansion?

Labor/ownership retention

- How do we best retain key personnel?
- How do we standardize practices while main-taining local culture?

Source: L.E.K. research, interviews and analysis

The most common pain points are around managing talent/labor management, aligning goals, ensuring effectiveness of the sales force and establishing ways to share best practices across the organization (see Figure 2).

Figure 2

Common pain points (1/2)

Pain point	Talent/labor management	Goal alignment
Description	Companies are increasingly struggling to find and maintain quality labor, especially as companies grow and need to meet elevated demand or want to expand their service offering	There can be disconnects between leadership, branch managers and technicians/salespeople around strategic goals and objectives as companies grow/integrate newly acquired companies
Example variability by company factors	• Companies focused on more complex/technical service industries may face greater labor challenges • Smaller companies with lower recruiting budgets may also face outsized challenges when competing against larger companies	• Aggregator companies pursuing an M&A strategy are more prone to integration issues than those focused on organic growth with legacy cultures • Similarly, acquisitive players that retain legacy branding of acquisitions may face additional integration challenges
Potential mitigation strategies	Companies can prioritize employee retention initiatives (e.g., improved benefits, incentive structure) and training academies to mitigate labor issues	Integrating key functions (e.g., IT) quickly while allowing for greater flexibility with other functional decisions (e.g., commission structure) can streamline integration while achieving organizational goals

Note: IT=information technology
Source: L.E.K. research and analysis

Figure 2
Common pain points (2/2)

Pain point	Sales force effectiveness	Establishing best practice sharing
Description	Sales functions can vary in terms of effectiveness (e.g., lead generation, account maintenance, effective cross-selling)	Best practices and procedures can remain siloed at individual locations, which may minimize the effectiveness of the overall organization
Example variability by company factors	• Residential providers often invest in more customer-facing personnel given greater customer fragmentation and less recurring revenue • Commercially focused companies can target larger customers with fewer (albeit highly skilled) salespeople	• Companies with a greater scope/scale of local functional roles may face higher risk of valuable local knowledge remaining siloed • Rapidly growing companies, especially those with poor IT integration, may face issues tracking KPIs and sharing best practices as they scale
Potential mitigation strategies	Retaining the entrepreneurial spirit of salespeople (especially post-acquisition) via incentives while providing centrally or regionally led structure and training improves effectiveness	Monthly sessions with key personnel to collate best practices within functional areas that are then disseminated can provide structure to best practice sharing

Note: IT=information technology; KPIs=key performance indicators
Source: L.E.K. research and analysis

Goal alignment, for example, can be particularly challenging for growing companies, especially those pursuing M&A, as one executive told us:

"Proper goal alignment is one of our biggest pain points and risks. Especially when we acquire someone and the owner just got paid, how do we a) keep them around and b) make sure they are still working hard. In addition to financial incentives, we try to message to them that we are taking the annoying administrative stuff off their hands while letting them do 'fun' stuff like working with their customers and employees …"

But the real work begins when branch-based service organizations start to grow. As they reach critical inflection points in their life cycle, such as operating across multiple regions and/or offering multiple service lines, they are faced with a new set of operating model considerations around what to scale and centralize, on one hand, and where to enable local autonomy — for example, by evaluating the importance of national accounts and/or deciding whether or not to deploy regional leaders — on the other. To inform their operating model decisions, there are several areas of consideration that growing organizations can assess, among them strategic objectives, customer relationships, execution time, labor/ownership retention and their preferred methods of expansion.

When it comes to operating model considerations, there are a limited number of fixed rules. One is assigning clear decision-making responsibilities, irrespective of who they are assigned to. Another is investing in talent acquisition. Indeed, labor comprises some 70% of service companies' expenses, and the tight labor pool makes acquiring labor difficult. So regardless of where that function sits, it is essential to ensuring that companies can draw from local talent pools and flex labor to meet fluctuating demand.

The degree of centralization that service organizations want to engage in, as well as how to house different functions are considerations that are handled on a case-by-case basis. Indeed, no set approach works for all companies. But depending on the service focus, and the degree to which interfacing with local customers is essential to operations, certain functions may be better suited for centralization than others. Commercial service organizations that don't use a franchise model and maintain a focus on large customers may not need a robust localized sales force, for example.

Unique considerations are often the result of the organization's primary growth strategy, such as whether its model is inorganic or organic/franchise. Highly acquisitive aggregators, for example, must consider how to adapt their operating models to deal with newly acquired companies — from maintaining the legacy brand (if it is to be retained) and dealing with legacy ownership/relationships to developing a robust integration playbook that can be applied across all of the acquisitions they make. Common considerations include those that come with scale; as a company grows, whether or not it needs to develop distinct regional leaders and/or business units is just one decision that must be made. Notably, the outcome of such considerations will be highly dependent on both the organization's ownership model and the types of service(s) it provides (see Figure 3).

Figure 3
Operating model strategy inflection points

INFLECTION POINTS

- Multiregional scale
- Critical mass of branches/legacy companies
- Service-line expansion /diversification
- New growth targets

	Areas of debate and considerations for decision-making	Examples of common choices	
National accounts	What is the role of national account functions, if any? How closely should they work with other customer-facing personnel?	National accounts team handles large customers and drives service business for local branches	Local branches handle sales and service regardless of customer size to maintain strength of relationships
Degree of local knowledge	How important is developing and maintaining strong local relationships with customers and the community in the geographies/service areas of focus?	Marketing driven by central organization with limited branch input given focus on large customer accounts	Marketing driven by local branch within guidelines set by central organization
Number of service lines	Are there adjacent service lines that can be pursued? Is it better to expand within core service lines or pursue growth through breadth expansion?	Adapting operating model to enable pursuit of service lines beyond traditional core focus (e.g., creation of service-line BUs)	Maintaining operating model structure to support existing core service focus(es)
Purchasing agreements	What level of benefit could be gained by increasing negotiations with suppliers/centralizing purchasing?	Procurement handled at highest organization level to maximize cost savings and allocated to individual branches based on needs	More purchasing autonomy at branch level with access to volume discounts/national pricing information
Regions as owners vs. coaches	How heavy-handed should the regional administration be? Do they control and make decisions for local branches or serve as a mouthpiece for the central organization to ensure compliance and facilitate best practices?	High degree of control from regional leader over local branches across strategic and operational decisions	Regional leaders serve as a "coach" to branches and act as a mouthpiece for the central organization

Note: BUs=business units
Source: L.E.K. research and analysis

There are a number of ways to mitigate the most common operating model pain points that service organizations experience as they grow, such as:

- Prioritizing employee retention through improved benefit offerings, incentive structures, investment in apprenticeship programs and developing training academies

- Integrating key functions (e.g., IT, HR) quickly while allowing for greater flexibility with other functional decisions to be executed at the branch/regional level (e.g., commission structure, marketing budget)
- Providing centrally- or regionally-led structure and training to ensure sales force effectiveness while maintaining a sense of entrepreneurship at the local level
- Establishing recurring best practice sharing sessions across operating companies

Operating model decisions are usually made on a case-by-case basis

When it comes to making operating model decisions, different approaches — for example, centralized vs. decentralized operations or organic vs. inorganic growth — involve different trade-offs that branch-based service organizations must weigh (see Figure 4).

Figure 4
Trade-offs across operating approaches (1/2)

Note: P&L=profit and loss
Source: L.E.K. research and analysis

Figure 4
Trade-offs across operating approaches (2/2)

Role of business units

Business units

Advantages
- Typically enables greater degree of service/category expertise among leadership
- Can assist with pooling of resources across potentially complex service areas

Disadvantages
- Introduces added complexity and potential friction/redundancy if regional units also exist
- May be mutually exclusive with regional organization

No business units

Advantages
- Can simplify operating model processes and oversight, especially in less technical categories

Disadvantages
- May result in misalignment of leadership capabilities and requirements
- May create issues in scaling/expanding service lines

Midlevel leader role

P&L owner/stronger role

Advantages
- Empowers leaders to make critical strategic decisions without additional bureaucratic steps
- Allows leaders to focus time/resources on areas of underperformance

Disadvantages
- May result in greater variations in performance/operations given potential talent disparities

Lighter touch role

Advantages
- Greater alignment across business units/regions given stronger adherence to central mandates
- Typically associated with greater degree of best practice sharing across organizations

Disadvantages
- Can complicate decision-making process and handicap the ability of leaders to make decisions based on BU/regional/local nuance

Note: P&L=profit and loss; BU=business unit
Source: L.E.K. research and analysis

Assigning responsibility for different company functions at varying geographic levels — local, regional and central — requires making various trade-offs as well (see Figure 5).

Figure 5
Local vs central trade-offs (1/2)

Trade-offs of housing responsibility for different functions at each level

Function	Local	Regional	Central
IT	Enables greater system flexibility/minimizes disruptions from integration but can create difficulties in communication and alignment on KPI metrics across branches	Allows for greater oversight at regional level if stronger regional organization role, but relatively uncommon	Drives greater efficiencies of both technology and scale to have systems aligned across organization and to not have local/regional personnel; integration of systems can be difficult
HR	Handling some functions at the local level (e.g., recruiting) can be critical given the need for local knowledge, but less-sophisticated organizations may struggle with some HR functions	Regional leaders may have HR reps to oversee the function, but this may only be efficient at large companies	Many back-office HR functions can be centralized to drive efficiency (e.g., talent development, benefits) but can limit local knowledge
Finance	Operating simple functions such as payroll and AP at the local level can improve accuracy of payments at the expense of potential centralization benefits; local budgeting can also increase budget accuracy and feelings of ownership	Regional finance roles may help regional organizations drive P&L performance but can be expensive if they exist across regions	More complex roles such as treasury typically handled centrally; central payroll functions may drive cost savings but can result in inaccuracies
Marketing	Local marketing budgets can be critical for reaching local customers effectively via customized content but can result in conflicting/poor marketing tactics	Regionally based marketing roles can benefit from greater geographic-specific knowledge while also being easier to coordinate; however, regional roles may be too expensive for any but the largest organizations	Centralized marketing functions can enable companies to develop greater functional expertise and more-sophisticated digital marketing techniques and promote a coherent national strategy but may lose local knowledge and nontraditional marketing routes (e.g., event sponsorships)

Note: IT=information technology; KPI=key performance indicator; HR=human resources; AP=accounts payable; P&L=profit and loss
Source: L.E.K. research and analysis

Figure 5
Local vs central trade-offs (2/2)

Trade-offs of housing responsibility for different functions at each level

Function	Local	Regional	Central
Supply chain	Some activities may be better managed locally to increase accountability and tailor to local needs given the amount of direct interaction local personnel have with such activities as inventory management; however, this may result in variability	Regional supply chain duties may be optimal for supplier management and purchasing if suppliers are highly regional, but may not maximize cost savings	Companies often drive efficiencies via centrally led purchasing and development of quality management and other best practices; managing a large number of branches can be difficult, can create risks in concentrating supply, and decreases local autonomy
Sales	Having a sales force with a strong local presence is especially critical in industries with a more fragmented customer base and highly localized competition; local sales personnel may struggle to handle large accounts	Regional sales managers are often critical in driving best practices among local reps; the scope of direct customer-facing roles at the regional level may be limited	A centralized sales platform consolidates resources and can act as an invaluable lead generator for local branches as well as acquire/manage national accounts, but may lack intricate local knowledge to interface directly with customers
Operations	Most companies handle/staff operational execution at the local level (e.g., facilities management); however, handling operations planning and other operations management duties at the local level can inhibit best practice sharing	Allowing regional organizations to own operations management can be beneficial given there is some degree of local nuance required to optimize planning; variability may still exist across regions	Centralized operations management can drive some cost savings/efficiency, especially for relatively distinct functions such as real estate and site planning; however, fully centralized operations can result in decisions incongruent with local needs

Source: L.E.K. research and analysis

One common consideration service organizations that are seeking to optimize their unique operating model cite is that while deploying a highly centralized sales function may increase the efficiencies of dealing with large accounts, it can limit the ability of salespeople to utilize potentially important local knowledge and/or relationships. In service areas where large accounts are more common/important — think certain commercial service areas, such as facilities, that serve customers with many national locations — service organizations may choose to deploy a centralized sales function, whereas those targeting homeowners may typically retain a greater "on-the-ground" presence, albeit often one backed by national or regional marketing campaigns.

Strategic operating model decisions also have pros and cons. For example, aside from whether or not to centralize operations, whether or not to deploy business units is one of the most pertinent decisions service organizations are faced with. Based on the conversations with service organizations that we have had, while some companies with complex and highly distinct service offerings may benefit from creating distinct business units beyond regional organizations, doing so introduces another level of complexity that can result in inefficiencies. That said, service organizations with national scale and the resources to hire and retain leadership with the requisite expertise in both service execution and business unit/P&L management tend to be more likely to create business units.

To help safeguard against commonly experienced downsides of operating functions with a high degree of local consistency/autonomy, branch-based service organizations can take a variety of steps. One is ensuring that their local employees have formalized pathways for communicating relevant local knowledge that is essential for HR processes, such as effective people management, recruiting, etc.

Despite the case-by-case approach, there are common themes

Service organizations with high-performing operating models tend to have the same key success factors, among them customer-centric, consistent execution; robust training models; formalized playbooks/best practices; KPI tracking; influential and empowering leadership; and effective recruiting/labor management. And those factors often involve incremental considerations as the organizations scale.

Many of the most commonly cited key success factors are underpinned by data and KPI tracking, people/talent management and strong service performance and can be measured by tailored criteria sets to assess organizations' adherence to them. For example, whether or not a service organization is achieving consistent execution — defined as consistently delivering high-quality/efficient service to which marketing/sales initiatives are aligned — can be assessed based on the time it takes to complete jobs, the average amount of driving required to complete each job and the customer satisfaction scores those jobs subsequently receive (see Figure 6).

Figure 6
Scaling common success factors (1/2)

Key success factors to enabling an effective operating model

	Key assessment criteria highlighted	Scaling considerations
Customer-centric model	• Customer retention rates • Average customer lifespan • Customer satisfaction scores	• Strategize how to best maintain relationships with legacy customers as they acquire larger customers • Consider deploying call centers and the impact of how that impacts relationships with local customers
Execution consistency	• Time to complete jobs • Average driving time • Customer satisfaction scores	• Gather best practices for service execution and disseminate to branches • Track execution KPIs and ensure branch level leadership is monitoring and actioning areas for improvement
Robust training model	• Number of employee trainings • Share of managers from in-house • Employee training completion rates	• Capitalize on scale by hosting centralized training sessions • Implement formal professional development protocols
Formalized playbooks/ best practice sharing	• Amount of feedback shared • Playbook adherence/adoption rates for best practice recommendations • Execution consistency metrics	• Download best practices from new acquisitions and incorporate them into playbooks that are shared with the broader organization • Host monthly/quarterly best practice meetings with branch level leadership

Note: KPIs=key performance indicators
Source: L.E.K. research and analysis

Figure 6
Scaling common success factors (2/2)

Key success factors to enabling an effective operating model

	Key assessment criteria highlighted	Scaling considerations
Rigorous KPI tracking system	• Branch-level buy-in on KPI monitoring and data quality • Actionability of KPIs • Branch-level adherence to KPIs	• Prioritize IT integration to track branch-level KPIs • Develop dashboards to increase ease of digestion and actionability of KPIs for branch-level leadership • Ensure effective transfer of trainings via on-the-job coaching and KPI tracking
Empowering and capable leadership	• Financial performance • Employee satisfaction scores • Executive level retention	• Consider how best to retain branch-level leaders following acquisitions via incentives and cultural preservation (e.g., formal management training programs) • Align executive-level incentives with key strategic priorities
Effective recruiting/ labor management	• Recruitment rates • Employee retention rates • Employee satisfaction scores • Number of open positions	• Allocate labor across newly added branches depending on demand • Evaluate the potential benefits of centralized recruiting to attract top talent if local recruiters cannot maintain adequate staffing levels

Note: KPI=key performance indicator; IT=information technology
Source: L.E.K. research and analysis

How operating model changes are timed

As service companies transition from operating on a local to a regional to a national level, they face a number of critical decisions. Some key factors are more pertinent during particular growth stages than others; for example, it's important to develop strong relationships with labor early in the growth cycle. Service organizations that strive to include these factors at the right stage and adjust their consideration priorities as they grow are often well-positioned for success (see Figure 7).

Figure 7

Success factors across growth stages

Key success factors during stage and rationale

Note: IT=information technology
Source: L.E.K. research and analysis

For service organizations growing through M&A, making the right changes at the right time is critical. As they grow and/or acquire smaller companies, specific functions and processes are frequently targeted for quick change, such as assets like IT systems or processes like KPI tracking. Changes to other areas, namely those that impact service delivery and execution, such as existing distributor relationships, might be adopted gradually (see Figure 8).

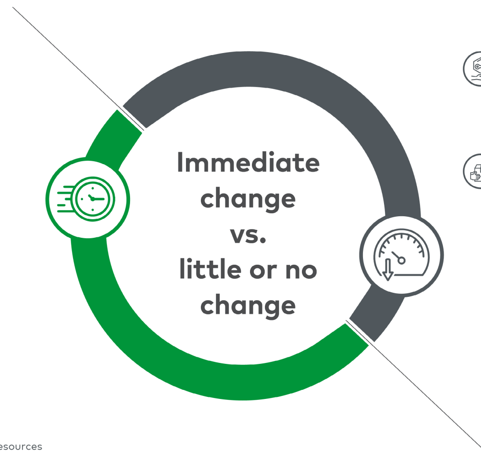
Figure 8
Approach to change

Areas often considered for immediate change

IT systems
Companies that pursue integration of IT systems often find that expediting the process can allow for more seamless overall integration and the ability to flag issues before they cascade

Other back-office functions
Back-office functions (e.g., payroll, HR compliance) that present minimal risk of service disruption are often cited as key areas to integrate quickly

KPI tracking
Smaller companies often lack sophisticated KPI tracking systems, whereas larger organizations derive substantial benefits from monitoring KPIs and look to establish tracking processes quickly



Slow/no change

Distributor/vendor relationships
Distributor/vendor relationships are often preserved for a time following an acquisition to avoid operational/service disruptions

Legacy ownership
Leadership may be a major factor in M&A decisions, and independent owners often hold key relationships/cultural initiatives and are thus encouraged to remain for as long as possible

Customer delivery
Effective customer delivery is typically a critical M&A criteria; acquiring companies do not typically prioritize customer delivery for immediate overhaul

Note: IT=information technology; KPI=key performance indicator; HR=human resources
Source: L.E.K. research and analysis

A unique operating model for every service organization

When it comes to deciding on an operating model, there are myriad factors that branch-based service organizations must take into consideration. And there is no one-size-fits-all solution. But there are common themes and pain points, as well as common decisions and trade-offs that need to be made. Indeed, studying the steps taken by service organizations that have walked this path before yields invaluable lessons, including the various pitfalls to avoid along the way.

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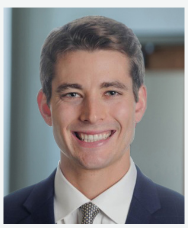

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