

Shaping up
Evolving the
HR function for
the 21st century

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Executive summary

HR is at a turning point. For a decade now it has been undergoing a process of transformation. But for many, it has been a process that has increasingly failed to produce the results expected of it. During these times of rapidly changing economics, we believe HR is faced with a stark choice. It can either evolve and make a significant contribution, or be diminished and dispersed into the business.

Many companies have made efforts to transform their HR function in recent years. A survey in 2007 by the Chartered Institute of Personnel and Development (CIPD), the UK's leading HR professional association, found that more than half of those responding had restructured their HR function in the previous year, and four out of five had done so in the previous five years (see "*The Changing HR Function*").

Yet despite having spent tens of millions on the transformation process, many organisations were not happy with the results. In Deloitte's *Aligned at the Top*² report, only 4% of senior business executives described their company's HR capability as "world class". Nearly half of them said it needed to improve, while over 30% said it needed "significant improvement".

It is not that these transformation programmes have been insignificant. On average, probably 25-30% of HR staff have lost their jobs as a result of them. Costs have undoubtedly been cut. Indeed, there has been a tendency to equate the word 'transformation' with 'cost reduction', as if that were all it involved.

But, given that HR operating expenses typically represent less than 1% of a company's total revenues, even massive improvements in efficiency can have only small effects on the bottom line.

We believe that HR Transformation has to be about much more than the efficiency of the function if it is going to have a significant impact on results. Several studies indicate that by far the most common objective of HR Transformation was to enable HR to become "a more strategic contributor" to the organisation. This has never been more true than in the current economic environment. However it is here that the process has most blatantly failed to deliver. With only 23% of companies in the *Aligned at the Top* report stating that HR currently plays a crucial role in strategy formulation and operational results, it is apparent that HR has not yet transformed to the point where it is involved in strategic thinking at the highest level.

Getting the basics right is a prerequisite. Due to reduced growth in the market and an increased number of redundancy programmes, now more than ever HR must work strategically with business leaders on re-sizing and restructuring their organisations whilst retaining key talent.

So, HR is now at a crossroads. HR has to make the same journey as Finance and IT did before it. The HR Director has to transform into a CHRO in the same way that the Finance Director became the CFO and the IT Director the CIO.

1 Survey report September 2007, © Chartered Institute of Personnel and Development 2007

2 'Aligned at the Top' survey report, (Deloitte and Economist Intelligence unit, 2007)

During the 1990s, both the CFO and the CIO undertook similar journeys and in most cases successfully transformed their functions. Both developed shared services, utilised new technologies, implemented offshore delivery models and established strategic partnerships which led to greater efficiencies within their own function and higher quality delivery for the business. This creation of value through their willingness to embrace transformation, has helped cement their position at the leadership table.

What's more, Finance and IT have faced recurring crises where they have shown boards their mettle and their value. For IT there was the Y2K problem at the end of the 1990s, and then the internet and the threat from online sales; for Finance there have been various regulatory and compliance challenges that have put it to the test and more recently, a global financial slowdown. HR is now facing its biggest business challenge, needing to drive improved productivity and performance whilst retaining talent during a time of hard hitting cost reductions.

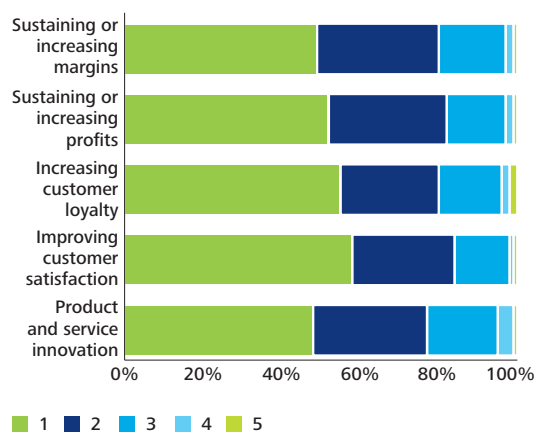
During times of significant organisational change, the HR function should come into its own. As a function it is but a small part of a company's direct costs, and as such can only contribute a little in direct headcount savings, however it does hold sway over some of the company's biggest cost budgets, in areas such as Learning, Recruitment and Compensation. When these budgets come under pressure HR will be in the front line and will be called on to make decisions on spend, which will not only impact a company in the short term but, if executed poorly, will adversely impact areas such as Talent Management and Employer Brand for much longer.

Last but not least, HR should be at the heart of helping the business navigate through organisational change, by carefully managing consultation, communication and selection processes, all of which carry great risk to a company if delivered incorrectly.

The opportunity is truly there for HR to show its worth. Companies are only too well aware that HR is critical to their future success. Eighty five per cent of the Aligned at the Top respondents said that people were vital to every aspect of their company's performance, from increasing profits to product innovation.

"Show me a company that undervalues its people," said the CFO of one leading pharmaceuticals company, "and you'll find someone who's underperforming relative to others in their industry."

Figure 1. How vital are people in terms of your organisation's performance?



(Rate on a scale of 1 to 5, where 1 = Extremely and 5 = Not vital)
Results based on all participants.

Source: *Aligned at the Top* survey report
(Deloitte and Economist Intelligence Unit, 2007)

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So where is it all going wrong?

The driving force behind the early restructuring of HR departments came from a combination of technology, a desire to cut costs and some influential management ideas. Most companies that have restructured their HR operations have done so along similar lines by dividing the HR function into three – into what are generally called: Shared Service Centres (SSCs), Centres of Expertise (CoEs), and Business Partners (BPs).

Transformation of HR is not new, it has been underway in one form or another since the mid 1990s. During this time the main focus of the transformation efforts was on the implementation of service delivery models and in particular the deployment of service centres. Many of these initial forays into HR Transformation have failed to deliver the value and savings originally anticipated. Their failings were due in part to:

- **Reduced client satisfaction**, as a one size fits all approach to service delivery was applied, which did not recognise the diversity of employees.
- **Insufficient market insight** and innovation in HR policies.

- **Low morale in HR**, with no clear career path or longer term development program for HR professionals.
- **Overly expensive running costs** and poor quality outsourcing contracts.
- **Ineffective HR Business Partners** who were unable and ill-equipped to deliver the level of business advice expected.
- **Continued erosion of data quality**, and therefore HR credibility, as a result of poorly constructed processes.
- **Dissatisfaction with self-service** technologies due to low quality implementation and education of line managers.

These failings lead the business to question whether HR is best placed to fix the issues or if the business should take control and address them.



Taking a closer look

Remote Service Centres

Initial attempts to implement Shared Service Centres (SSC) in the marketplace have been met with mixed success. Deploying a SSC is just the start of the transformation. Lessons learnt in deploying this model in Finance during the 90s highlight that full transformation takes time and needs room to evolve. Yet for many HR functions their initial attempts have left them some way off from achieving their aspirations of:

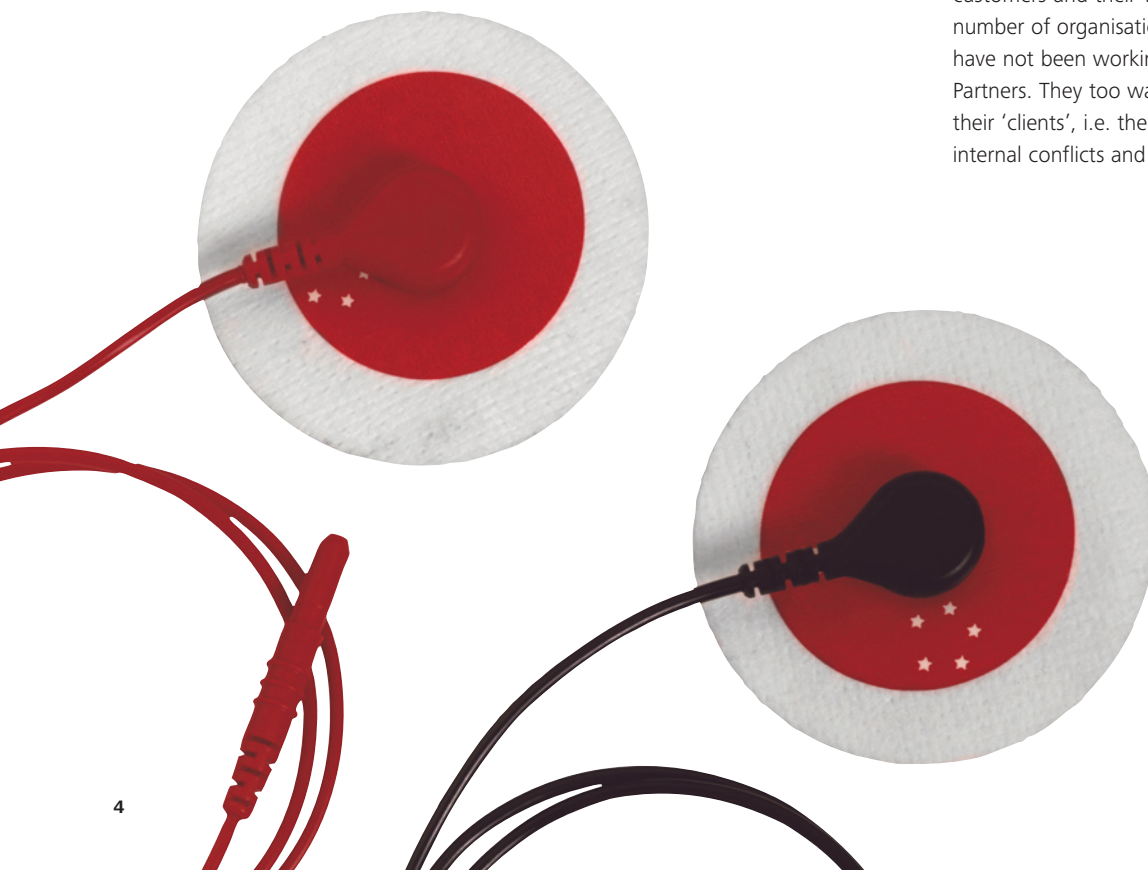
- An embedded service culture.
- Technology enabled specialist HR skills.
- Collaborative technologies and integrated self-service.
- Segmented service delivery and processes.
- A data ownership culture.
- Integrated outsource provision with flexible transactional pricing.

These shortcomings in the core activities of the HR department fundamentally damage the reputation of HR and its ability to deliver value-added services. It is impossible to discuss the strategic people agenda when service delivery is inconsistent or poor. HR needs to embrace the learnings from Finance and IT around operational excellence and Six Sigma disciplines in order to raise the standard of their core services.

Silos of expertise

As with Shared Service Centres, the concept of the Centres of Expertise is not a new one. However, they too experienced teething problems with early implementations and many have not been as successful as anticipated. They face challenges around integration, lack of innovation and business applicability. In a number of cases, Centres of Expertise have fallen into a trap of developing generic products on an ad-hoc and reactive basis. This, coupled with a lack of alignment to business objectives, has pushed the Centres of Expertise further and further away from where they need to be focused and, as a consequence, further from the business.

Critics have already accused some CoEs of being too like ivory towers, far removed from the front line of customers and their varied demands. It also seems in a number of organisations that the Centres of Expertise have not been working well with their HR Business Partners. They too want to have a relationship with their 'clients', i.e. the line managers, which causes internal conflicts and confusion to the customer.



Business Partners, or parts of the business?

In many transformation programmes, both HR and Finance, it is the Business Partners who still require the most assistance to transform. Instead of becoming leaders in the business, strategic players and developers of business aligned solutions, many Business Partner organisations find themselves:

- Pre-occupied by operational issues.
- Unable to diagnose and develop strategic HR solutions.
- Operating as a Customer Relationship Manager and a 'broker' of specialist HR services.

One message to have come over loud and clear from HR Transformation so far is that Business Partners cannot allow themselves to become bogged down in the detail. They cannot deliver both operational support and strategic direction.

Business Partners should be contributing to strategic planning at the highest level. However with a focus still on some functional, execution elements, they are dedicating less of their time to where it is needed most.

For reasons of control and trust, these more transactional elements have not always been migrated over to the Shared Service Centres for delivery.

Additionally we have found that the role has been interpreted very differently by different organisations. In some organisations the number of Business Partners is still too high, not all of whom can be contributing to high-level strategic planning; others have appointed just a few. One company with 60,000 employees has 350; another, with some 50,000 employees, has just two.

People working in HR have to believe that they are not only partnering with the business, but that in a very important way they *are* the business.

It is a combination of HR to manager ratios, organisational alignment (i.e. business or country), capability and culture (high or low levels of interaction), which should determine the number of Business Partners.

Just as many Centres of Expertise have not been working well with their Business Partners, the reverse has also been true. Business Partners don't want to be mere brokers to their organisation's Line Managers for the services of the Centres of Expertise. So if they find themselves waiting for a CoE to come up with a solution to a problem, they begin to design their own. Hence they start to duplicate the capabilities of the specialists.

It appears that part of the problem lies in the language of HR Transformation. Being a Business Partner to other parts of the business suggests that HR somehow lies outside the business rather than being an integral part of it. As Dave Ulrich himself wrote in his 2005 book *The HR Value Proposition*³: "Think of the key wealth creator in your business. In an investment bank that would probably be an investment banker. In a software company it could be a systems architect. In the upstream portions of an oil company it's probably the petroleum geologists who search the world for oil ... All of these three [job categories] would think (assuming they could perceive the issue): 'We do not need to aspire to be Partners in the Business. We are the Business.' "

All of these challenges continue to erode the business' faith that HR will 'get its house in order' and add fuel to the argument to bring critical HR activities closer to the business.

Where should HR go now?

If HR does not continue its transformation process, it risks becoming redundant. In the end, it could find that virtually all HR administration is outsourced, the centres of excellence are handed over to individual businesses to manage for themselves and strategy continues to be determined without any significant input from HR. If it does not evolve, HR is likely to devolve or, at best, to shrink into little more than a vendor manager and employee relations organisation.

Those who decide to take HR to the next level will undoubtedly have the competitive advantage. So where exactly should HR go now? And what does the next generation of HR Transformation look like?

A good example of taking HR Shared Services to the next level is Deutsche Bank where the HR Shared Services organisation "HR Solutions" is now a part of their Global Technology and Operations organisation (GTO), which is responsible for not only HR but also other back office activities such as IT and procurement.

Deutsche Bank's strategy has been to consolidate the transactional and administrative functions, therefore moving as many back office functions to the GTO as possible.

This has not come without challenges however. Securing buy-in to the initial shared services concept was difficult and the HR Business Partner organisation was also initially hesitant in giving up its transactional activities.

The task ahead for HR is demanding and yet it is not unachievable. So what can you do to evolve your HR function? How can your HR function progress to the next level?

Enhancing your HR function to be fit for purpose requires a number of key organisational and cultural changes to come together:

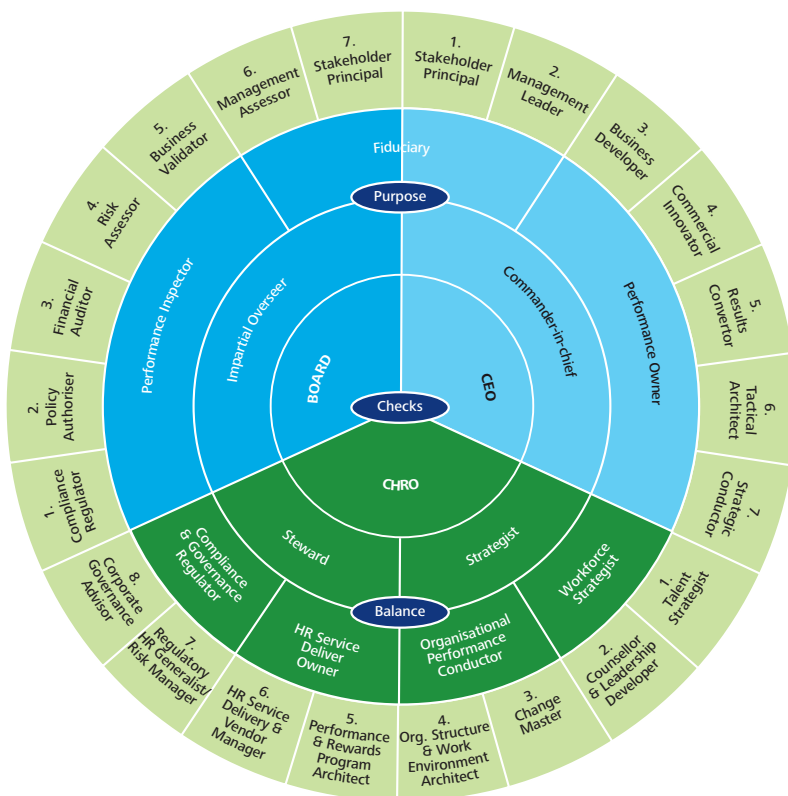
1. Establish the role of the CHRO.
2. Segment your customers.
3. Free the Business Partners.
4. Align the CoEs.
5. Optimise Shared Service Centres.
6. Measure success.

1. Establish the role of the CHRO

A CHRO does not need to carry around intimate details of employment legislation or health and safety rules. CHROs need a rather different set of skills. In a recent Deloitte publication, these skills were defined under two headings: Strategist and Steward.

As a Strategist, the CHRO will have to help the CEO craft their plans in light of global labour market trends and the availability of talent. This means moving from strategy implementation to strategy development.

At the same time, as the Steward the CHRO will have to be a custodian of the organisation's performance, judging which methods and rewards optimise its employees' behaviour. With a bewildering array of options to choose from, from telecommuting to job sharing, to flexible hours and workforce diversity, this is no easy task in today's working world.



Source: CHRO Strategist and Steward Series, Book 1: The Evolving role of the Chief Human Resources Officer (Deloitte, 2006)

The CHRO will continue to have overall responsibility for delivering the day-to-day HR services, where the pressure to cut costs and to outsource operations will intensify significantly. Finally, they will need to play a leading role in regulatory compliance. Sarbanes-Oxley legislation has put pressure on organisations across the board, but it is their CEOs and CFOs who have borne most of the burden. CHROs need to be more involved in compliance and in business ethics generally. After all, every corporate scandal ultimately has its roots in the workforce.

2. Segment your customers

HR cannot be all things to all people so it will need to segment its customer base. Different segments of its market will have different needs. By providing a service that meets the needs of critical workforce segments, not only will it be rewarding for most, but HR will find itself ahead of its competitors in the war for talent.

The nature of the Business Partners' involvement will inevitably depend to some extent on the business they are in. In the pharmaceuticals industry, for instance, which is driven these days by the length of a firm's patent pipeline for drugs to cure or alleviate medical ailments, the HR function needs to be tuned in to its top performing talent.

It needs to know who are the people internally that are most likely to come up with such patents, and make sure that they have a package that is highly competitive. And then it needs to recognise where (and how) it can recruit others like them.

A large international oil company has a very diverse set of working environments, where managers and employees (customers) have varying levels of access to communication channels. When they carried out an exercise to segment their employees for HR purposes, they identified 13 distinct customer-types.

These varied from what it called nomads, people who travelled the world in search of oil, to the office-bound professionals who backed them up. The categories wanted different things from their HR service provider and required a different method of access to services.

HR also needs to prioritise its work in line with the priorities for their industry. These priorities vary by industry and by country but in our experience the business priorities for say the telecoms industry are:

- New market entry.
- Move to low-cost countries.
- Workforce reconfiguration.
- M&A and divestitures support.
- Talent and culture.

Stephen Dando, CHRO of Thomson Reuters

"My role as Reuters Group HR director changed following the acquisition by Thomson. The top level roles of the combined organisation were established early on and I was given the role as the future Thomson Reuters CHRO and member of the Executive Committee.

"My relationships with the legacy Reuters Board and Executive Committee, combined with my new role, played an integral part in enabling the HR function to be at the forefront of the integration. HR played a key role throughout, working closely with senior executives to lead initiatives such as organisation design, the appointments process, benefits harmonisation, talent management and synergy planning and preparation. HR's active involvement during the integration meant that important issues such as global talent and culture are now on top of senior executives' agendas.

"Today, I spend much of my time with the executive committee, defining the strategic people agenda and priorities with the aim to create one Thomson Reuters as quickly as we possibly can. Since Day 1, I have mainly spent my time on:

- Getting to know the CEOs, senior leadership and key talent of our businesses to understand their future plans, priorities and challenges.
- Defining and embedding the future vision and values.
- Working with Tom Glocer, our Chief Executive on key people and organisation priorities.
- Working with the HR committee on our executive compensation and talent agenda."

The Business Partners' greatest failing has been their inability to convince senior managers that they have the necessary business acumen to contribute to the strategic debate.

3. Free the Business Partners

The role of the Business Partner can deliver a number of benefits for an organisation, in particular by raising the perceived standards of the HR function. Next generation Business Partners still face a number of key challenges and it seems the most effective way to get the function to work properly is to split their role in two, similar to those of the CHRO: the strategic contributor and custodian of HR operations. In doing so, the strategist will be free to do what HR has always aspired to do – analyse and propose HR action in support of the company's strategic business goals – while the custodian will revert to delivering HR Operations through self-service and Service Centres.

So far Business Partners have too often been appointed from amongst the organisation's HR personnel, from HR generalists. As a consequence, they have frequently been either too timid and failed to engage in the debate on strategy, or they have 'gone native' and ignored policy in order to curry favour among senior managers.

Business Partners have tried to shift their mindset from that of a compliance officer to that of a Business Partner. Now they need to take one step further. They need to think like a strategic business player. And then they need to act like one. They need to understand and deliver solutions to the people implications of moving into China, for instance, or in seeking to serve emerging new markets.

For the future of HR, in many cases, there is a need for the role of the Business Partner to work on more of a project basis. Responding to changing business strategies requires flexibility and demands that HR now operates in two dimensions: functional and project-based. For HR, this means a whole new set of skills and capabilities, such as strong programme management and delivery skills, and requires a flexible mindset.

In summary, successful completion of the transformation of HR depends on the success of the Business Partner transformation; especially in developing business acumen, consultancy skills and the ability to build people strategies for their organisations. Without this vital part of the equation, the business will question the relevance of their HR support and push to gain control of this function.

4. Align the CoEs

If HR is to meet the needs of the business, it needs to move away from traditional functionally-aligned CoEs to business-aligned CoEs that reflect the projects and programmes that the business is focused on. With alignment on solutions for business challenges like M&A, Talent Management, Absenteeism, Organisational Change, etc. the CoEs will engage more with the business by having a naturally common ground around which to forge relationships.

This realignment requires a different way of working for CoEs. It requires flexibility to grow and shrink as the business' needs evolve. It requires project management skills as teams come together to develop and deliver solutions and then disperse. It requires different styles of leadership and career management models to cope with the change from the traditional, time served model.

This does not mean the end of traditional 'Reward, Benefit and Learning' CoEs. But it does require HR organisations to rethink the way in which they provide support to the other solution-focused CoEs, whilst still delivering their other commitments.

One retail bank has taken a unique approach. To avoid building a costly fixed headcount, the bank has partnered with external consultants to meet their peak demand for HR specialist resources. Through this model, HR can continue to deliver on their day-to-day commitments and, as and when the business needs additional specialist skills, they parachute in external support to help on a project by project basis.

With this example in mind, it seems that, like the Business Partners, the role of the CoEs will evolve and require a stronger business acumen. Translating their specialist knowledge into this new, more business-focused environment requires different skills from those valued by CoEs today.



5. Optimise Shared Service Centres

'Get the basics right' – we have all heard those words before in relation to HR Transformation. Unfortunately in a lot of HR organisations this has yet to be achieved with any degree of consistency. It takes time to embed true service delivery and an operational excellence culture into an organisation, but this is exactly what HR needs to do.

It is time for Shared Service Centres to embrace techniques adopted by Finance and IT before them, in order to improve services, quality and process delivery. Techniques such as Six Sigma and Operational Excellence will facilitate this, but will also allow for the rest of the Shared Services Centre to free itself from operational burden and concentrate on delivering the HR strategic agenda.

HR can also learn from other businesses on achieving effective and operationally proficient service delivery. For example, mobile phone companies and utilities companies already make significant use of call centres, to help accelerate their own level of service delivery and provide their customers with a higher quality service.

However you choose to improve services, 'getting the basics right' for Shared Service Centres means:

- An embedded service and continuous improvement culture.
- Technology enabled specialist HR skills.
- Collaborative technologies and integrated self-service.
- A data ownership culture.

To achieve this level of fundamental change to HR delivery requires significant and ongoing investment in training, performance management and leadership development. When successful, these core capabilities will have significant impact on HR operations and HR performance.

Some organisations have come to realise that the step change required is so significant that they embrace outsourcing as a way of bringing these capabilities and approaches into their service delivery functions. Whilst there are undoubtedly positive lessons to be learnt from how outsource providers run their businesses, not all HR functions will wish to embrace an outsourced model.

Without consistent service delivery and clear accountability for results, the business will resist the change to shared services or will push for outsourcing in order to achieve the step change in service delivery.

6. Measure success

For HR to become more fully integrated with the rest of the business, it has to 'know and show'. It has to know the business, and it has to show to the business that it can translate its requirements into realistic and achievable initiatives. But measuring HR effectiveness and its benefits to the business is not easy – suitable yardsticks are hard to find.

Conrad Venter from Deutsche Bank comments:

"We have started to move away from 'traditional' measures to instead use what we call 'Value Creation Metrics'. This includes employee surveys, customer satisfaction measures and HR culture assessments. Our Germany based service centre has also implemented 'quality circles' to get feedback from the business itself on how well the call centre is performing. We also have a plan to introduce 'continuous improvement measures' outside of our service centres which we hope to implement in the short-term future."

Shared Service Centres will have accumulated, in most cases, data that could be used for such metrics. For example, it should be possible to find out whether recruits from expensive employment agencies are retained longer than those obtained by other means. They may show that it is more effective to promote schemes such as the popular Silicon Valley practice of encouraging workers to invite friends with valuable skills to their corporate canteen for a free lunch.

Measuring and reporting the impact and effectiveness of HR to the business is critical in winning confidence in the quality of service delivery and in tangibly demonstrating the worth of HR. Should this be absent, the business is more likely to work on perception, undervaluing and hence questioning the role of the HR function.

The *Aligned at the Top* report, which questioned more people from outside the profession than from within it, concluded that “the strategic people agenda is not being addressed by HR”.

Conclusion

Evolve as a function or see its role dissolved back into the business? That is the question HR departments now have to consider. In a significant number the transformation so far has been partial. HR must continue to transform themselves into a function fit for purpose – the purpose of getting the best out of their organisation's people.

For that, first and foremost HR will need to have more business and financial acumen, plus a deeper understanding of the levers that can affect their business. They need to be capable of joining in with board-level strategic discussions and need to be proactive and take entrepreneurial risks. Their transactional HR skills must become secondary to their strategic understanding of the business.

It is a demanding agenda, but it is not unachievable. However, HR should not delude itself about the progress it is making. Respondents to the CIPD study⁴ reckoned that strategic issues took up 12% of HR's time three years ago and 23% today, a figure that will rise to 35% in three years' time. More than half of them also reckoned that their CEOs would today rate their performance highly.

But they would tend to say that wouldn't they? For they were all members of the HR profession. The *Aligned at the Top* report, which questioned more people from outside the profession than from within it, concluded that "the strategic people agenda is not being addressed by HR". Senior Business executives still do not involve HR in major strategic decisions. For instance, over 60% of respondents said that they "rarely or never" consult HR about mergers or acquisitions.

If HR continues to fail to address these fundamental challenges, who could blame the business for wanting to wrestle back control in driving the people agenda.



⁴ Survey report September 2007, © Chartered Institute of Personnel and Development 2007

Contacts

For more information on HR Transformation, please contact:

Aaron Alburey

UK HR Transformation lead

Deloitte MCS Limited
+44 20 7007 4942
aalburey@deloitte.co.uk

Margot Thom

Global HR Transformation lead

Deloitte Inc.
+1 416 874 3198
mathom@deloitte.ca

David Parry

UK Organisation & Change lead

Deloitte MCS Limited
+44 20 7007 2988
davidparry@deloitte.co.uk

Beth Thiebault

US HR Service Delivery lead

Deloitte Consulting LLP
+1 612 397 4062
bthiebault@deloitte.com

Global Human Capital contacts

Global Human Capital

Dr. Sabri Challah
Global Practice Leader, Human Capital
+44 (0) 20 7303 6286
schallah@deloitte.co.uk

Jeff Schwartz
Global Practice Leader, Organization
and Change
+1 703 251 1501
jeffschwartz@deloitte.com

Tim Phoenix
Global Practice Leader,
Total Rewards
+1 512 226 4272
tphoenix@deloitte.com

Margot Thom
Global Practice Leader, HR
Transformation
+1 416 874 3198
mathom@deloitte.ca

Human Capital – Americas

Michael Fucci
National Practice Leader
Human Capital
Deloitte Consulting LLP,
Americas and United States
+1 212 618 4708
mfucci@deloitte.com

Margot Thom
National Practice Leader
Human Capital
Deloitte Inc., Canada
+1 416 874 3198
mathom@deloitte.ca

Vicente Picarelli
Regional Practice Leader
Human Capital
Deloitte Consulting
Latin America and Caribbean
+55 11 5186 1043
vpicarelli@deloitte.com

Human Capital – Asia Pacific

Richard Kleinert
Regional Practice Leader
Human Capital
Deloitte Consulting LLP, United States
+1 213 688 3368
rkleinert@deloitte.com

Lisa Barry
National Practice Leader
Human Capital
Deloitte Consulting, Australia
+61 3 9208 7248
lisabarry@deloitte.com.au

Kenji Hamada
National Practice Leader
Human Capital
Tohmatsu Consulting Co., Ltd., Japan
+81 3 4218 7504
kehamada@tohatsu.com.jp

Byung Jeon Kim
National Practice Leader
Human Capital
Deloitte Consulting Korea, Korea
+82 2 6676 3830
bjkim@deloitte.com

P. Thiruvengadam
National Practice Leader
Human Capital
Deloitte Touche Tohmatsu
India Pvt. Ltd., India
+91 80 6627 6108
pthiruvengadam@deloitte.com

Hugo Walkinshaw
Practice Leader,
Human Capital
Deloitte Consulting Singapore
Pte. Ltd.,
Singapore and South East Asia
+65 6232 7112
hwalkinshaw@deloitte.com

Jungle Wong
National Practice Leader
Human Capital
Deloitte Touche Tohmatsu
CPA Ltd., China
+86 10 8520 7807
junglewong@deloitte.com.cn

Human Capital – EMEA

Brett C. Walsh
Regional Practice Leader
Human Capital
Deloitte MCS Limited
United Kingdom
+ 44 (0) 20 7007 2985
bcwalsh@deloitte.co.uk

Dr. Udo Bohdal
National Practice Leader
Human Capital
Deloitte Consulting GmbH, Germany
+49 69 97137 350
ubohdal@deloitte.com

Gert De Beer
National Practice Leader
Human Capital
Deloitte Consulting,
South Africa
+27 11 806 5995
gedebeer@deloitte.co.za

Enrique de la Villa
National Practice Leader
Human Capital
Deloitte S.L., Spain
+34 9151 45000
edelavilla@deloitte.es

Rolf Driesen
National Practice Leader
Human Capital
Deloitte Consulting, Belgium
+32 2 749 57 21
rodriesen@deloitte.com

Christian Havranek
National Practice Leader
Human Capital
Deloitte Consulting, Austria
+43 1 537 00 2600
chavranek@deloitte.com

Feergus Mitchell
National Practice Leader
Human Capital
Deloitte MCS Limited
United Kingdom
+44 20 7007 3698
fmitchell@deloitte.co.uk

Petr Kymlicka
National Practice Leader
Human Capital
Deloitte Advisory s.r.o.
Central Europe
+ 420 2 246042260
pkymlicka@deloitte.com

Gilbert Renel
National Practice Leader
Human Capital
Deloitte S.A., Luxembourg
+35 24 5145 2544
grenel@deloitte.lu

Ardie van Berkel
National Practice Leader
Human Capital
Deloitte Consulting B.V.
The Netherlands
+31653733271
AvanBerkel@deloitte.nl

David Yana
National Practice Leader
Human Capital
Deloitte Consulting, France
+33 1 58 37 96 04
dyana@deloitte.fr

Alexander Zabuzov
National Practice Leader
Human Capital
Deloitte CIS, Russia
+7 495 787 0600
azabuzov@deloitte.ru

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