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Towards a new trading model for the Stahl European business?

Final Thesis for the Postgraduate Program
Chartered Controller, TIAS - Tilburg

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PREFACE

This report has been written as the final thesis for the Postgraduate Program Chartered Controller. Several fields of this study have been used in this thesis, which was challenging on one hand because it is about a new concept, the trading model, but difficult on the other hand, since the available literature does not provide the combination in the way it is done in this thesis. The biggest hurdle therefore was finding the right framework.

I would like to express my gratitude to Prof. Dr. F.W. Vlotman, Prof. Dr. F.D.J. van Schaik RA FB RI and Drs. S.B. Oudkerk RC for their various suggestions and recommendations.

Furthermore, I would like to thank my employer, Stahl International B.V., for enabling me to participate to this Program and my fellow students for the many interesting discussions.

And last but not least I would like to thank my wife Yvonne for her support and encouragements during the last two years of my study and my children, Mariska, Marcel, Stefan and Sander, for their patience when I wasn’t there at the times they needed me.

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MANAGEMENT SUMMARY

This thesis describes the options for Stahl to structure its European business. A new terminology, trading models, is introduced to reflect integration of several areas, which form part of this structure: business process, management control, information technology, information management and tax. Based of the developments in the European Community on one hand and in the IT area on the other hand, a new trading model for Stahl Europe's business has now surfaced: the Single Business Entity trading model. It provides similar benefits as a shared service center would, but on top of this it virtually eliminates intercompany transactions and reduces complexity in business processes due to the change of functions of legal entities.

The Single Business Entity trading model provides Stahl Europe with a lot of benefits, but the change to this new model is quite complex and needs top management support and leadership to make it work. It should be regarded as a large change project, visibly led by Stahl Europe's business management.

In summary the major benefits are:

- Elimination of intercompany invoicing, resulting in management information on "roll-through" profitability for customers and products in Europe;
- Lower operating costs, mainly in the finance area;
- Increased focus on the (external) business;
- Increased central control of processes, which are needed to run a true European business;
- Future changes in business processes and systems can be implemented more easily and quickly.

Because of the various fields, which need to be taken into account as mentioned above, the Controller is the person best placed in the organisation to identify and initiate a review on whether a new trading model would be worthwhile. Since more and more companies have transformed their disparate businesses in Europe to a true European business, these companies should be reviewing this option for the merit of their own benefit. And these benefits can be significant!

1 Introduction

The aspects that gave rise to this thesis will be discussed in this chapter. In section 1.1 the changes in Europe over the last decade will be highlighted and in section 1.2 the response of Stahl to these changes, while the issues that remained after the initial actions from Stahl Europe's management are discussed in 1.3. In section 1.4 the problem statement and its sub questions of this thesis will be described and section 1.5 will outline the scope and structure of this thesis. The methodological approach is discussed in section 1.6.

1.1 Developments in Europe over the last ten years

Enormous political, legal and economic changes have occurred in Europe during the last two decades as the integration of the European Community (EC) has really taken off. The European Commission has implemented during 1987 and 1993 over 300 legislative measures, based on the White Paper of June 1985, to remove discriminatory regimes, anti-competitive practices and other non-tariff barriers. The overall objective was to promote free trade and fair competition in the "level playing field": the internal market, in which there would be free movement of goods, persons, services and capital (Brown, 1993). Examples of non-tariff barriers have been the unnecessary paperwork at borders, different systems and levels of taxation and different technical standards. Physical barriers like custom posts have been removed. The immediate impact has been clear: access to wider markets and greater competition at home. Secondary impacts include the ability to enter into joint ventures, compatibility with ancillary industries, and longevity of product design. Additionally entrance costs to new markets have been lowered and at lower risks. The latest major change was the introduction of the Euro as currency in 1999 and the elimination of the national currencies for the countries in the Euro-zone during the first half of 2002.

On top of that there have been huge changes in the information technology worldwide, like ERP systems, the development of the world-wide-web and the development of internet-based applications to name just a few.

The changes in the areas above have prompted enterprises to review and adapt their strategies and to change their organisation structure in Europe. During the 1990's large companies have restructured to reposition themselves on a European-wide basis via acquisitions and formation of joint ventures between companies from different European countries, as companies seek to establish a market presence right across the European Community and simultaneously to rationalise production capacity. Internally companies have restructured their operations to create a unified management structure at a European level able to integrate production, distribution and marketing across Europe. The result was that in many companies the primary axis of management decision making and control has shifted from national subsidiaries, responsible for all business activities in a particular territory, to transnational business divisions at the European level, responsible for the production, distribution and marketing of products or services across territories (Marginson a.o., 1993). Furthermore, the growth of European-scale companies increased the trend to a further centralisation of management organisation in large enterprises.

1.2 Stahl's response to these European developments

Until 1997 the Stahl subsidiaries in Europe were responsible for their own local supply chain activities, like purchasing, inventory management and sales, as well as its financial performance on profit and cash delivery. But due to the progress made within the European Community to eliminate more and more obstacles in favour of free trade between the member states, Stahl decided in 1997 that the time was right to manage its business from a European point of view instead of local subsidiaries. The first action it took was the formation of a European Management Board (EMB) in 1997 to manage Stahl's European business and to implement the necessary changes in the European units to realise its strategic goals and specifically the need to:

- Be able to deal with customer groups across Europe
- Roll out our technology and marketing plans through the European markets
- Use the people resources more flexibly and efficiently
- Manufacture Stahl's products in the most rational and efficient way
- Increase velocity and simplify the logistical network
- Manage change in a constantly changing environment

From 1997 to 2002 the EMB has taken the following steps to implement the new European strategy:

- Implementation of MRP-II based processes for all European operations, which has led to Class "A" certification for all subsidiaries in Europe by Oliver Wight, a leading consultant in this area;
- Change the focus of the various production units to a more narrow product range, which is sold throughout Europe; before each subsidiary produced most of the products for their own local market;
- Implementation of SAP throughout Europe as the standard ERP system, based on one process- and financial model which was jointly developed and agreed to by all subsidiaries;
- Development of standard key performance indicators for the European business, like on-time in-full order delivery (customer service), production planning performance and First-Time-Right quality measures;
- Improvement of communication and exchange of technical know-how to ensure customers throughout Europe are serviced from the optimal location, like product availability.

1.3 The remaining issues of Stahl Europe

As discussed in the previous section, the EMB has taken several steps to change the organisation in Europe from locally led units to a European business. Although this has been done reasonably successfully there are a number of issues, which block further developments in the goal of creating a "true European business". The European Management has identified the following issues:

- Although all financial results are consolidated and reviewed at a European level, the local subsidiaries still report and discuss to a large extent all financial information as they did before 1997. All budget data was also available at the subsidiary level. It has proved to be difficult to have the local organisation only focus their new targets, while they still have to report all financial information as before.
- Making changes in business processes and the supporting integrated ERP system is complex, since all trading subsidiaries have all functionality. Therefore the people in these subsidiaries need to be involved, trained and supported in all aspects of changes to current business processes and system upgrades. This has proven to be a timely and costly necessity.
- There is a lack of proper information on product and customer profitability. Although all entities in Europe are integrated into one SAP system, this system does not give the "roll-through" profitability, i.e. the system only provides the margin that is recorded by the legal entity that sells to the direct customer based on purchase cost of this legal entity for products that are produced by another legal entity. In spite of considerable effort that was spent to write additional programs to retrieve this information, this has not been achieved. Since a big part of the current sales are sales within Europe between Stahl legal entities (around 25%), this is seen as a major issue.

The conclusion is that the current way of doing business in Europe reflects the "old" autonomy of legal entities for the sales of the markets they are responsible for and this does not match with the a European approach, in fact the entity structure creates internal blocks and distracting factors, which leads more to an internal focus in stead of an external focus.

1.4 Problem formulation

The problem in this thesis is stated as follows:

In which way can Stahl change its trading model for its European operations best to ensure that it will meet its strategic objectives and how can the implementation issues of this change be addressed?

To find an answer to this problem the following sub-questions are stated:

- *What is a trading model?*
- *Which trading models are available for the Stahl Europe business?*
- *What are the criteria to be used to decide on the future trading model?*
- *What trading model fits best with Stahl's strategy and objectives for Europe?*
- *What are the issues around the implementation of the proposed trading model and how can these be tackled?*

1.5 The scope of the study and chapter arrangement

1.5.1 The scope of the study

The scope has been limited to the legal entities of Stahl in Europe, which are controlled by the European Management Board. Furthermore the problem will be tackled in an integrated way from three different viewpoints: business process, IT, and the fiscal structure. The issues of implementing the proposed trading model will only be discussed at a high level.

1.5.2 Chapter arrangement

Chapter 2 deals with a brief view of the various ways the structure of organisations can be looked at, the definition of "trading model" and its different variants, including a general description of the elements of the definition for every variant. Chapter 3 provides an overview of the way the Stahl business is currently organised, its strategy, objectives, culture and its IT- and legal set up. The criteria for evaluation of these alternatives are laid down in Chapter 4. Based on the previous chapters, the analysis of the various trading models for Stahl Europe versus the criteria is presented in Chapter 5 while the implementation issues of the chosen trading model is reviewed in Chapter 6. The overall conclusions will be discussed in Chapter 7.

1.6 Methodological approach

The purpose of this thesis is to recommend a trading model to the Stahl management for its European business that fits best its strategy and eliminates the remaining issues as described by its management. Methodologically, it is about forming a normative theory, which is based on empirical research. Therefore, one of the limitations of this study is its explorative character. The conclusions and recommendations are related only the Stahl European business and should as such not be used for other organisations without further investigation.

2 Trading model: the framework

2.1 Structure follows strategy

The issue of structuring organisations has been discussed in literature at length from several perspectives: legal, tax, financial, people, management control, IT etc. Various ways to look at organisations have emerged from an information management perspective such as the 7-S model, the Minzberg configurations and Porters value chain model. It is now commonly accepted that the structure of organisations is dependent on its goals and strategies: structure follows strategy! (Chandler, 1966). The structure is not only determined by strategy, but also by the style of management (Goold, Campbell, 1987) In management accounting literature several themes have emerged over time in these discussions: centralisation versus decentralisation, functional, business unit or holding company, profit, cost or investment center etc. Also here there is no doubt that different strategies have implications for the organisational structure as well as for its management control system (Anthony, Govindarajan, 1998).

Still, most of these discuss the issue of structuring organisations from the view of one or more particular disciplines. Given the issues of Stahl Europe as described in paragraph 1.3, I will combine the disciplines of legal, tax, management control and IT/Information management into one approach which is called "a trading model". This term was first used in this way by Voorne Partners, a Dutch management consultancy firm (www.voornepartners.com) (3 Nov 2002).

In the next chapters the term "legal entities" is used to identify organisations. However, in reality there are various other ways to set up a local organisation in a specific country.

2.2 Definition of trading model

The definition of a trading model in this thesis is:

"The total relationships of an international company with respect to:

- *Business processes*
- *IT-model*
- *Fiscal structure"*

In principle two different trading models can be distinguished:

1. <u>The "Multi business entities" model (MBE-model).</u>

In this model each sales organisation of a legal entity will invoice to customers and will record receipts from customers, will be invoiced by suppliers and pay to suppliers and will, if applicable, produce for their own account (all of these processes determine "business"). This "full trading" scenario is known as "Multi Business Entity" and has basically three variations:

a. The "Multi-business single market" entity model: in this model more than one legal entity is buying and selling to customers. Every customer is invoiced by one legal entity only.

b. The "Multi-business multi-market" entity model: in this model each entity will invoice a customer directly irrespective of the customers' location. Every legal entity has buying and selling processes.

c. The "Multi-business re-invoicing" entity model: All invoicing to end-customers is done by the "the center" legal entity. The other legal entities can buy and produce but they will only invoice "the center" legal entity.

2. The "Single business entity" model (SBE-model)

In this model only the "center" legal entity will invoice to customers, will be invoiced by suppliers and will, if applicable, produce for her own account. All other local legal entities will either act as "agents" for sales activities, as "toll converters" for production activities, or a combination of the two.

From now on the "center" legal entity in the SBE-model will referred to as the "Single Business Entity" or SBE and the one described in the "Single-business re-invoicing" model will be referred to as the "Central Entity" or CE.
The basic differences between the various models are displayed in Figure 1 and described in more detail below.

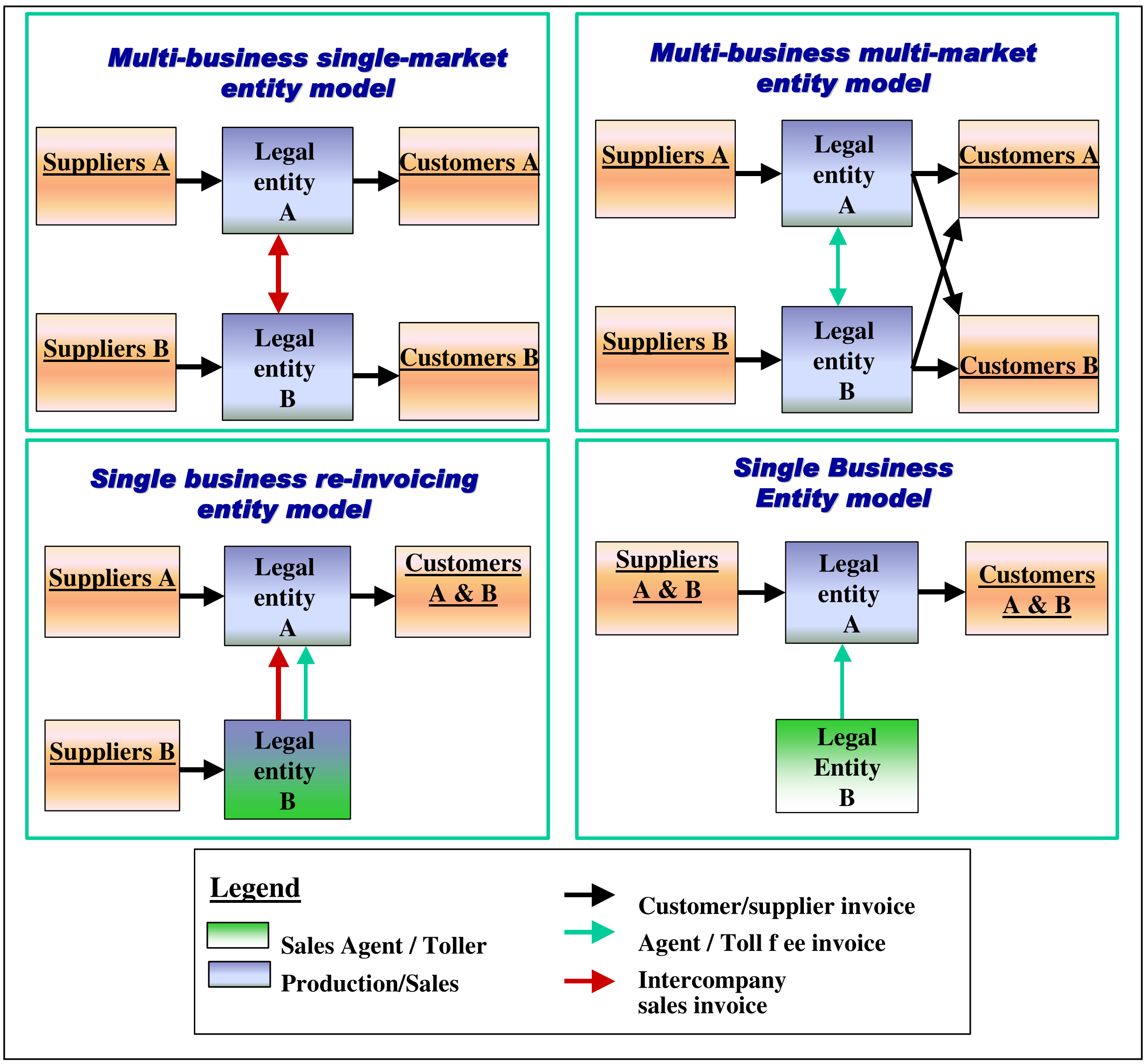

Figure 1: Overview of fiscal structure and relationships by trading model

2.2.1 Multi-business single market entity trading model

The main characteristics of this trading model are:

- A market is only sold into by one legal entity;
- Intercompany sales are necessary if the legal entity does not produce the product itself;
- Every producing legal entity buys its own raw materials and pays the related creditors;
- The legal entities that act as a sales agent in a particular market have only one principal.

2.2.2 Multi-business multi-market entity trading model

One option is to switch to a multi-business multi market trading model of legal entities. The main characteristics of this trading model are:

- Each legal entity that produces a product sells it directly to the customer in Europe wherever it is located;
- No intercompany sales are therefore necessary in this trading model;
- Every producing legal entity buys its own raw materials and pays the related creditors;
- All legal entities that produce products are principals of the legal entities that act as a sales agent in a particular market.

2.2.3 Multi business re-invoicing entity trading model

The next option is to switch to a trading model whereby one legal entity will act as a re-invoicing centre for all external sales. The main characteristics of this trading model are:

- Only one legal entity sells directly to the customer in Europe wherever it is located;
- The other producing legal entities sell all product as intercompany sales to this legal entity;
- Every producing legal entity buys its own raw materials and pays the related creditors;
- The legal entities that act as a sales agent in a particular market have only one principal, the company that sells to all external customers.

2.2.4 Single business entity trading model

This is a relatively new way to structure a business organisation on a European scale. This was introduced successfully for the first time by a European multinational in 1997, which was facilitated by developments of ERP systems (Willcocks & Sykes, 2000).

This trading model can be characterised by:

- Only one legal entity (the SBE) owns all finished product in Europe and sells directly to all customers in Europe wherever they are located and receives money from these debtors;
- The centre also buys all raw materials and pays the related creditors.
- The other producing legal entities act as a toll manufacturer for the centre;
- The legal entities that act as a sales agent in a particular market have only one principal, the SBE.

These characteristics of this model are displayed in more details in the following table:

SBE ownership	*Local ownership*
• ***Sales (order confirmation, invoicing credit management, pricing, contracts and terms)***	• ***Customer Service (order taking and advising of terms & pricing, technical service activity)***
• ***Sourcing and planning strategy***	• ***Production as a toll manufacturer and the quality of the manufacturing process***
• ***Customers (terms, debt, risk, rebates, commissions, discounts)***	• ***Local consumables and engineering***
• ***Finished goods & raw material stocks and related creditors***	• ***Sales force activities (agency)***
• ***Management reporting and central company fiscal reporting***	• ***Custody of local stock***
• ***Treasury / Cash management***	• ***Fixed assets***

Table 1: SBE trading model characteristics

2.2.5 A Euro-company: 'Societes Europea' (SE)

A new legal and tax structure for companies in the EC will become available in the near future. The European Commission has agreed to establish a new type of legal entity, which is described in the European Company Statute. This is important as it will allow companies to operate throughout the European Union as a single legal entity, the 'Societas Europeae' (SE) while it will be governed by Community law directly applicable in all member states.

The main features are:

- A European Company is set up by the creation of a holding, joint subsidiary or by merger of companies located in at least two Member States or by conversion of a national company;
- The information, consultation and participation procedures of a European Company are laid down by negotiations between a special negotiating body representing employees and the management of the founding companies;
- In the absence of an agreement a set of standard rules shall apply

The European Company would have to be registered in the Member State where it has its administrative head office (which would be Holland in the case of Stahl). The SE will, for tax purposes, be treated as any other multinational company according to the national fiscal legislation applicable at company level or branch level. Employment contracts and pensions are not covered by the regulation. They would be subject national law in the member states where the headquarters and branches operated.

However, this option of a European company will only be available after the legislation is due to enter into force, which is currently planned 8 October 2004. This fact, together with the changes that are needed in the area of workers participation (which may not be in line with Stahl's requirements), the uncertainty in the areas of tax, pension law and several other areas, leads me to conclude not to pursue this option in more in detail now, especially because from a process and systems point of view the SBE trading model would have a similar outcome.

2.3 The elements of the trading model in more detail

2.3.1 Business Processes

The first element of the trading model is business processes. Business processes will restricted here as supporting administrative processes that are directly related to the value-chain (Porter, 1985). The main issue is to devise business process in the most effective and efficient way to support the organisation's strategy and objectives.

The issue of optimising administrative business processes and in relation hereto the issue of executing these processes centrally or locally has been under review since the beginning of the 1990's. The process approach enables all control issues of this process to be viewed integrally and to devise all control measures as effectively and efficiently as possible, under the headings such as "Business Process Redesign", "Workflow-management" and "Kwaliteit Administratieve Dienstverlening (KAD)" (Molenkamp a.o., 1998).

The issue of whether these administrative processes are better executed centrally or locally has been discussed widely over the last years with the emergence of shared service centers (SSC). Shared service operations combine the efficiency and leverage of centralization with the superior customer-service usually associated with decentralization. Companies try to achieve this balance by drawing together activities performed similarly in various locations across the business, standardizing on a common process design that emphasizes high quality and customer responsiveness, and putting in place measurement tools to monitor performance and guide improvements efforts (Triplett a.o.; VanDenburgh a.o. 2000).

A SSC might be described as a consolidated back-office for a multinational company that is intended to perform transaction-oriented work at a favourable cost. Although the reasons for establishing this type of facility are primarily to minimize headcount and reduce cost, companies also benefit through access to skilled multi-lingual work forces at a central location, service level improvements, better information, and greater control (Miller, 1999).

An analysis of the various business processes by trading model is presented in Table *2*, as well as the indication of whether processes are or can be dealt with only centrally (C), only locally (L) or that both are possible (L/C).

L = Local ; C = Central	Multi-business Entity			Single Business Entity
	Single Market	Multi Market	Re-invoicing	
PTO processes (Prospect to Order)				
Marketing & Pre-sales process	L / C	L / C	C	C
Define strategy & develop target customers	L / C	L / C	L / C	L / C
Promote products & services	L / C	L / C	L / C	L / C
Develop sales plans	L / C	L / C	L / C	L / C
Manage sales and technical service force	L / C	L / C	C	C
Manage strategic partnerships	L / C	L / C	C	C
OTC processes (Order to Cash)				
Order Fulfilment process	L	L	L / C	L / C
Credit control Process	L	L / C	C	C
Distribution	L	L	L	L
Billing/invoicing	L	L / C	C	C
Intercompany invoicing	L	L	L	N/A
Accounts receivable	L	L	C	C
Receipts processing	L / C	L / C	C	C
MTS processes (Manufacturing to Stock)				
Product costing	L	L	L	L / C
Inventory Management	L	L	L	L / C
Asset Accounting	L	L	L	L
PTP processes (Procurement to Pay)				
Define sourcing strategy	L / C	L / C	L / C	C
Develop vendor relations	L / C	L / C	L / C	C
Set up buying contracts	L	L	L	C
Call-off from buying contracts	L	L	L	L
Purchase invoice processing (external)	L	L	L	C
Purchase invoice processing intercompany	L	L	L	N/A
Goods receipts processing	L	L	L	L
Accounts Payable	L	L	L	C
Payments processing / treasury	L	L	L	C
Overall processes				
Management (Business) Reporting	L / C	L / C	L / C	C
Regulatory reporting	L / C	L / C	L / C	C
General Ledger Accounting	L	L	L	C

Table 2: Overview of business processes by trading model: local or central

Several conclusions can be drawn from this overview:

- The Order-to-Cash-processes (OTC) show the most differences among the various trading models;
- The SBE model requires that most administrative processes are performed by the SBE;
- The SBE model is the only model that virtually eliminates intercompany invoicing for products and services within a group of companies;
- The SBE model is the only model in which the processes result in the fact that only one company, the SBE, has relationships with the external environment (customers, suppliers, bank).

The commonalities between the SBE model and an SSC approach are obvious, but there are also differences to be noted:

- Implementing an SSC does not require a change in function of the legal entity, while the trading models do;
- The consequence of this is that some processes are no longer required in e.g. the SBE model (like intramerger invoicing, which becomes a change in warehouse location) and that other processes can be done automatically for Europe (like Purchasing).
- It is therefore more easy in the SBE model to gain additional benefits, like “roll-through profitability” and purchasing power benefits;
- SSC’s require a relatively large minimum size to capture the cost benefits;
- In the SBE model, local processes (like asset accounting, cost center accounting and general ledger) are being dealt with locally. It is due to the change is function of its legal that the complexity of these activities are far less, than in a full trading scenario.

2.3.2 IT-model

The differences in the administrative value-chain business processes of the various trading models have implications for the IT model used. Since a decade it is customary for international organisations to implement one IT model in ERP systems for all or most legal entities. Modern ERP systems, like SAP R/3, normally consist various modules for the various business processes but these modules form an integrated system from a system architectural point of view. The differences within the various “Multi-business entity” models are negligible from an IT systems viewpoint.

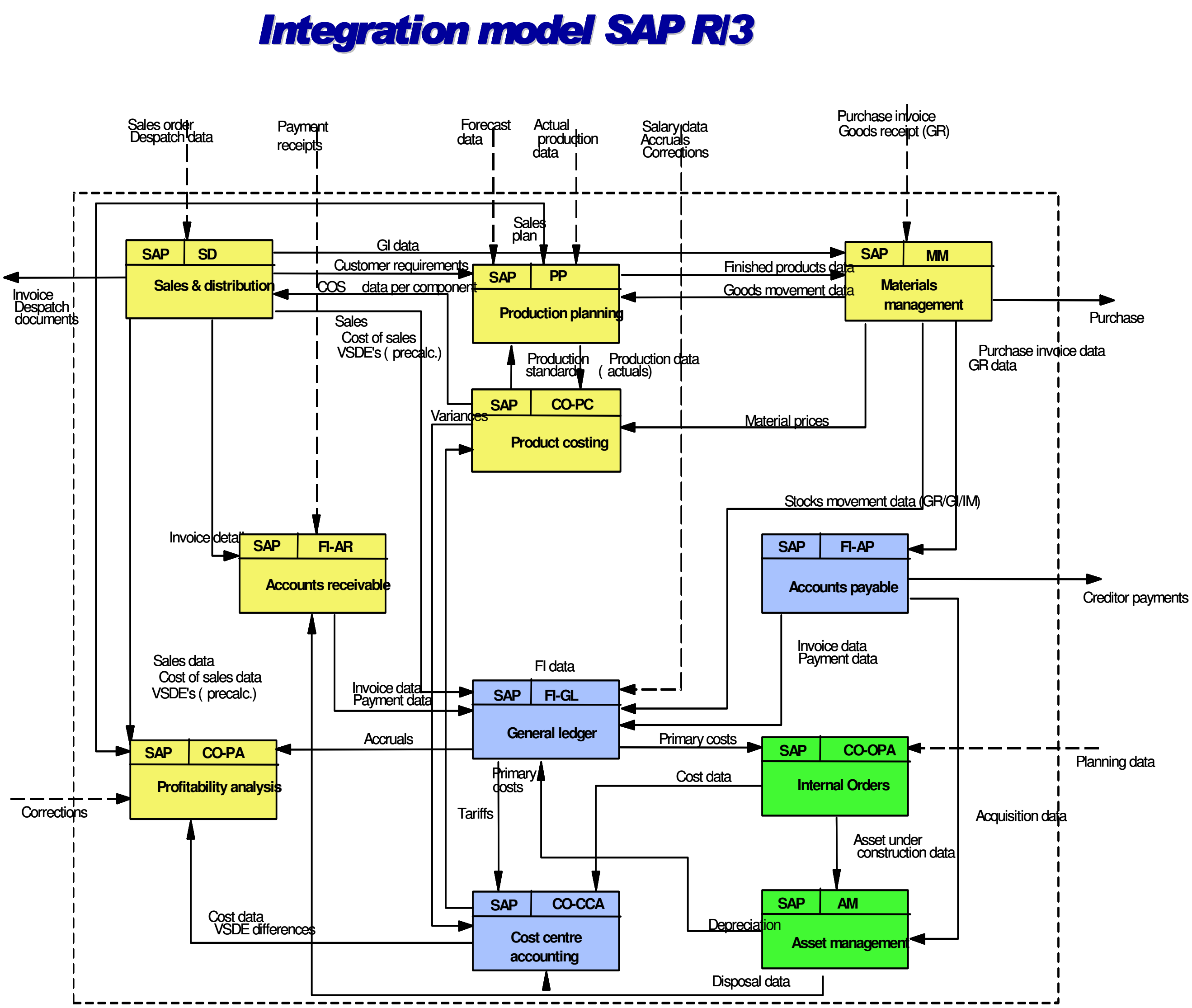

Figure 2: SAP R/3 modules and integration

Figure 2 displays the various SAP modules in boxes with the lines between the boxes indicating the integration of the various modules.

How the MBE- and SBE model differ can be seen from the colour of the modules: in the MBE-model all legal entities (if production is part of their process) need all modules, irrespective of their colour. In the SBE-model however, only the SBE itself needs all modules, while the other legal entities only need the modules marked blue and green.

It should be noted that changing from one trading model to another could cause severe changes in the way the ERP is set up, which should be taken into consideration in the decision making process of choosing the optimal trading model.

2.3.3 Fiscal structure

a. Corporate income tax

Legal entities in all countries in Europe are being taxed for corporate income taxes, which is based on their profit before taxes as determined by the tax laws in each country. One of the factors which determines the profitability of a legal entity is its function: within a given business, a legal entity that is performing selling and distribution activities normally receives a higher compensation and carries a higher risk, than a legal entity which is only an agent. One of the basic rules in international tax is to set the compensation between related legal entities (‘transfer pricing’) within a group “at arms length”.

Within the various trading models the transfer pricing issues vary, because the functions of the legal entities are different, which can clearly be seen in Figure 1.

The transfer pricing issues from a tax point of view vary per model from:

a. setting a product transfer pricing in place for intercompany sales invoicing (red lines);
b. setting at arm’s length sales agent and/or toll fee in place (green lines);
c. both of the above.

Apart from the transfer pricing issues, issues around permanent establishment need to be taken into account. Given the specific nature of this issue, this will not be discussed here further.

It also should be noted that changing from one trading model to another has consequences for the corporate income tax as well. For profitable business, goodwill payments may be high, although there are some options to reduce or eliminate this. In fact, in some cases it may bring about some opportunities as well. In any, case expert tax advice needs to be obtained before changing towards another trading model.

b. Value Added Tax (VAT)

Another tax issue that needs to be considered is VAT. Especially the SBE model increases the complexity around the VAT dramatically:

- the SBE should apply for a VAT number in every country where it the legal en economic owner of raw materials and/ore finished goods;
- the SBE has to take account of quite complicated VAT declarations, Intrastat and EC sales listings;
- the SBE has to nominate fiscal representatives in every country where it owns raw materials or finished goods.

3 Stahl Organisation: business, strategy and structure

3.1 Stahl Worldwide

3.1.1 Stahl history and positioning

Stahl is a key player in the leather industry worldwide and is engaged in the development, manufacturing, sales and distribution of specialty chemical products mainly used in the leather, footwear and textile industries. Headquartered in the Netherlands, the company produces worldwide over 4000 products at 13 production sites.

Stahl has operations throughout Europe, North and Latin America and Asia. Stahl employs over 1400 people worldwide of which ca 650 in Europe. Approximately 20% are technical experts based at application laboratories offering high-level services to customers wherever leather is being processed.

Until the end of 2001 the Stahl Group was a division of various multinationals (Avecia, Zeneca, ICI), but it is a standalone company after a levered buy-out from Avecia in the beginning of 2002.

3.1.2 Stahl's Characteristics

The business characteristics of Stahl can be summarised as:

- Primarily a Leather Finish business
- A portfolio of Business units sharing common technology, manufacturing assets and infrastructure
- A global business with regional manufacturing and sales / distribution facilities
- A service business
  - Expert application know how
  - Customised formulation skills
  - Technical lead customer service
- A people's business

Stahl has a specific culture which contains the following elements:

- High entrepreneurial instinct
- "Hands-on" mentality
- Action oriented
- Small family business mentality
- Managing Directors with a strong focus on the bottom line
- Controlled autonomy
- Strong identity and loyalty to the local company

Stahl is pursuing a differentiation strategy, the elements of which are summarised in Table 3 below:

Element	***Characteristic***	***Remark***
Product differentiation	High	Approx. 4,000 products
Market segmentation	Relatively high	15 segments
Distinctive competencies	Technical service, R&D	20% of manpower

Table 3: Characteristics of Stahl's differentiation strategy

Stahl is achieving sustained competitive advantage by this differentiation strategy, which is based on its distinctive competencies of resources and capabilities, which are summarised in Table 4.

Resources	***Capabilities***
Local presence near leather markets	***Innovation***
The Stahl trade name	***Formulating skills***
Stahl's organisational culture	***Technological know-how Leather Application***
	MRP-II Class "A"

Table 4: Stahl's distinctive competencies

3.1.3 Stahl Organisation

The Stahl organisation is structured by way of largely independent regions, which to a large extent have full P&L and balance sheet responsibility and are viewed as profit centres. On the other hand Stahl has three business units, which all regions report on and are responsible for. Each business unit has a Product Management Team (PMT), represented by people of all regions, which is responsible for setting the global strategy for each business unit, the coordination of the worldwide product portfolio, the demand for new products, and the exchange of knowledge and experience between regions. Stahl has a small head office in Waalwijk, The Netherlands, which coordinates and controls the overall strategy of the Stahl group, strategic capital investments, R&T, financial reporting, treasury, intellectual property and IT strategy.

The organisation of the regions and business units of the Stahl group are displayed in Figure 3.

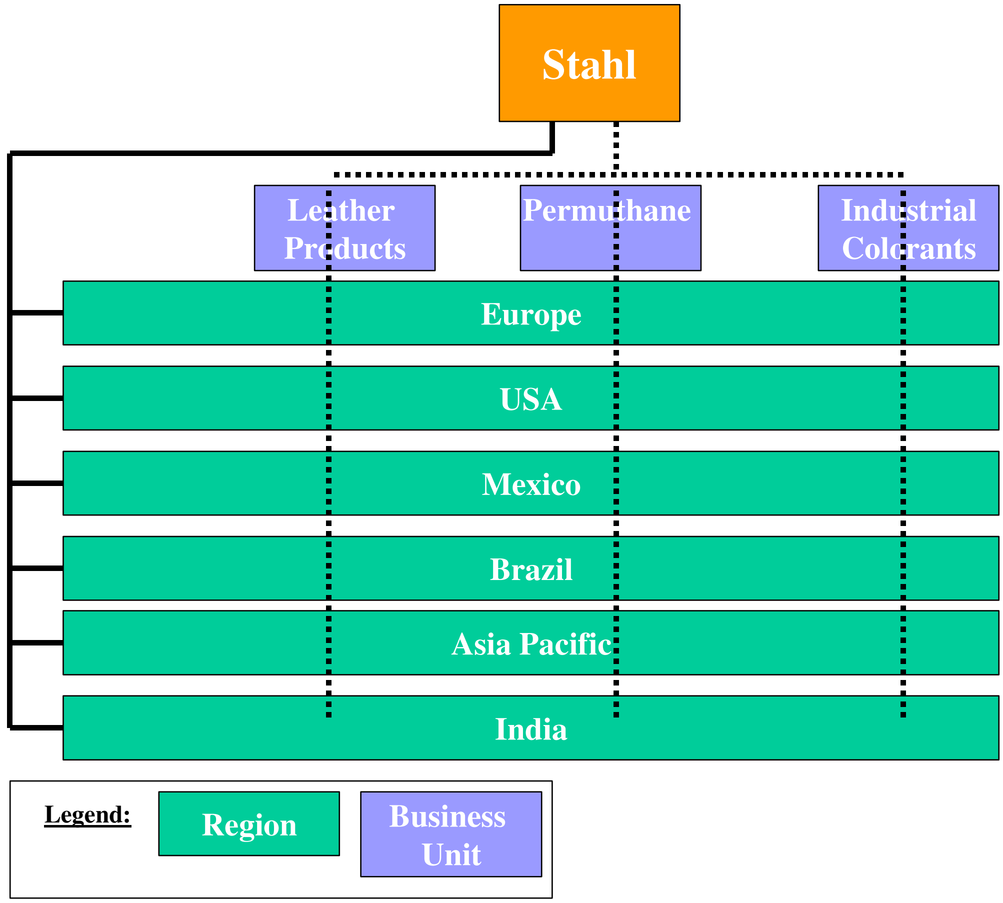

Figure 3: Organisation of Stahl

3.2 Stahl Europe

Stahl's European business represents about 50% of the Stahl global business. Next are described its vision statement, organisational principles, business drivers, objectives and its current trading model and IT model.

3.2.1 Stahl Europe vision statement

The European Management Board (EMB) has presented their vision to the European organisation in May 2002, which consisted of a declaration of the vision and the Stahl values:

Vision:

- We want to be nr. 1 in our Industry
- This means staying ahead of the game by:
  - Leading by innovation
  - Adapting and moving with agility and flexibility
  - Leading by the best people for the industry, focused on targeted financial results
  - Anticipating changes in market needs
  - Operating efficiently as a fully integrated Europe

Organisational principles: Based on this vision, the EMB has set out the following organisational principles for its European business:

- "There will be two business units (Leather Products and Permuthane) consisting of:
  - Centralised sales and marketing management and centralised R&D
  - Co-ordinated, decentralised sales force, technical service, customer service, warehousing, enabling each business to provide fast-response and local service to customers"
- "Business support will be via shared services viz. Manufacturing, Finance, IT, Human Resources, SHE, Transportation/distribution, Legal and Communications"
- "Centralisation (plus rationalisation) will be done for the sake of synergy and cost benefit provided that there is no negative effect on key business objectives"
- "The whole organisation will have a European mind-set. The priority will be to support the European customer-base as opposed to the local customer base. Local units will resolve any conflicts, maintaining customer satisfaction both locally and at the European level"
- "All the separate European plants will be regarded as one plant. As a consequence, product, no matter where it is located, is owned by the European business, represented by their respective Demand Managers".

3.2.2 Stahl Europe business drivers: country, region, global

The EMB has evaluated whether the drivers for their European business are determined on a country, region or global basis, which is presented in the following table:

Driver	***Country***	***Europe***	***Global***
Consumers / End users	√		
Customers	√		
Competitors	√	√	
Strategic direction of the business		√	√
Financial management		√	
Marketing - strategic		√	
Marketing – tactical	√		
Research & Development	√	√	√
Product line extension		√	√
Sales organisation		√	
Product availability		√	
Supply Chain management & planning		√	
Supply points – plants		√	
Supply points – warehouses	√	√	

Table 5: Stahl Europe drivers (source: Stahl Europe analysis)

The conclusions from this table are that:

- Almost all direct customer contact activities are driven by local circumstances,
- The business is managed mostly on a European scale (sales, supply chain and financial),
- Which is put into a global context with regard to strategy and R&D.

3.2.3 Stahl Europe objectives

The following objectives are developed by the EMB for the future organisation structure and the processes it is operating:

- Reduce the organisational complexity
- Achieve a truly European business
- Achieve a more European mindset for employees in stead of the local mindset only
- Achieve single European business processes
- Improve the quality of management information
- Reduce fixed costs.

3.2.4 Stahl Europe's current trading model

Until 1997 each legal entity in Europe selling products into the market was viewed as a profit centre. Each legal entity has its own markets (countries), which they sell into. This together with the fact that all plants had a limited range of products, which was even increased by focusing production in each plant further, has resulted into a substantial level of intercompany sales volumes (approx. 25% of the total). From a selling and service perspective this gives a very good focus on the customers they should be servicing and developing, but the focus within production is more based on building expertise for specific product lines and there is only a limited relation between the products produced locally and local sales.

Figure 4 displays the legal entities in Europe, which are "controlled" by the European Management Board, their function (production and/or sales organisation, sales agent) as per September 2002 in a similar way as the generic trading models are displayed in Figure 1. Stahl Europe's current trading model is characterized as a multi-business single market entity model as described in section 2.2.1.

There are four legal entities in four countries that act as a sales agent of Stahl Holland. In each of these entities technical service representatives are on the local payroll (between 4 and 8 people per legal entity). These entities receive a commission from Stahl Holland on the sales in the markets they are servicing, from which they can pay the salaries, travel costs and administrative costs. The same applies to Stahl Portugal, which is an agent of Stahl Iberica.

There are a lot of intercompany shipments and -invoicing (approx. 25% of the total), with the main stream being between Stahl Holland and Stahl Italy.

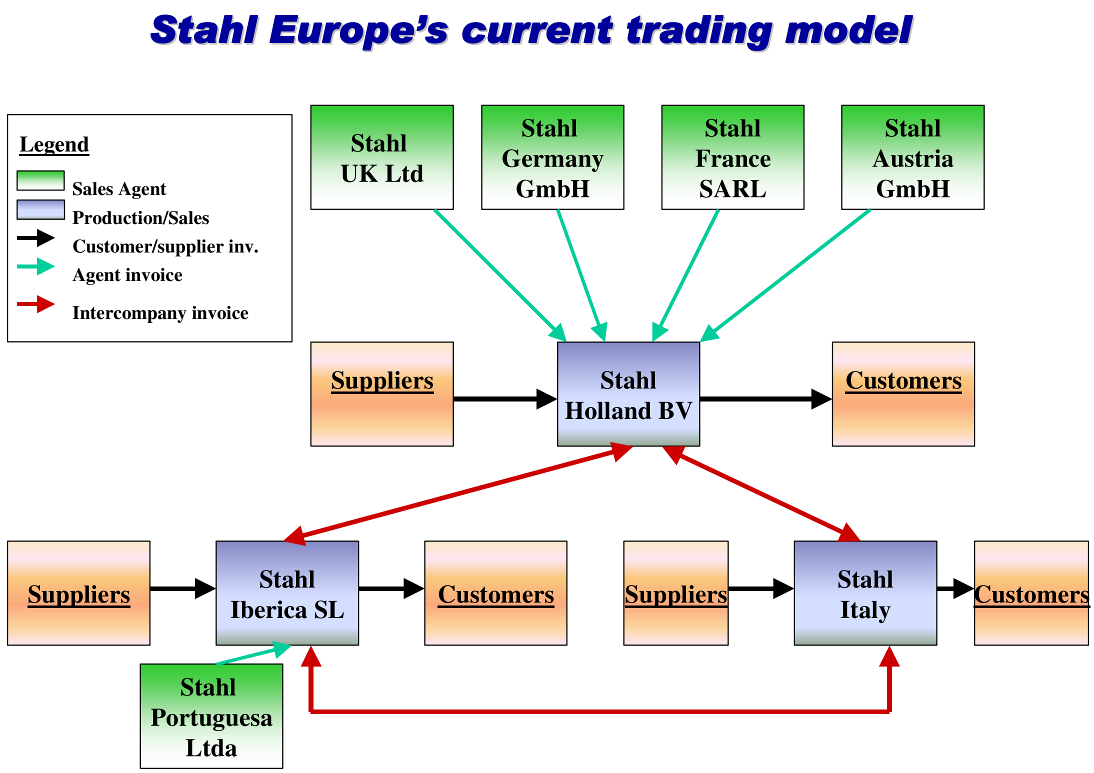

Figure 4: Overview of Europe's current trading model

3.2.5 Stahl Europe current IT model

One of the first actions that Stahl's EMB has taken was the implementation of a European wide ERP system (SAP) in 1997/1998. Up to that time almost every legal entity in Europe operated with different systems and it was only at a high level of reporting when information on the European business made sense.

The implementation to a common ERP platform and common processes throughout the European organisation was done via a kernel, which entailed the agreed way of working in all legal entities. The system was changed for each legal entity only where these changes were enforced by local laws or regulations.

The structure of the current SAP R/3 model for Stahl Europe is given in Figure 5.

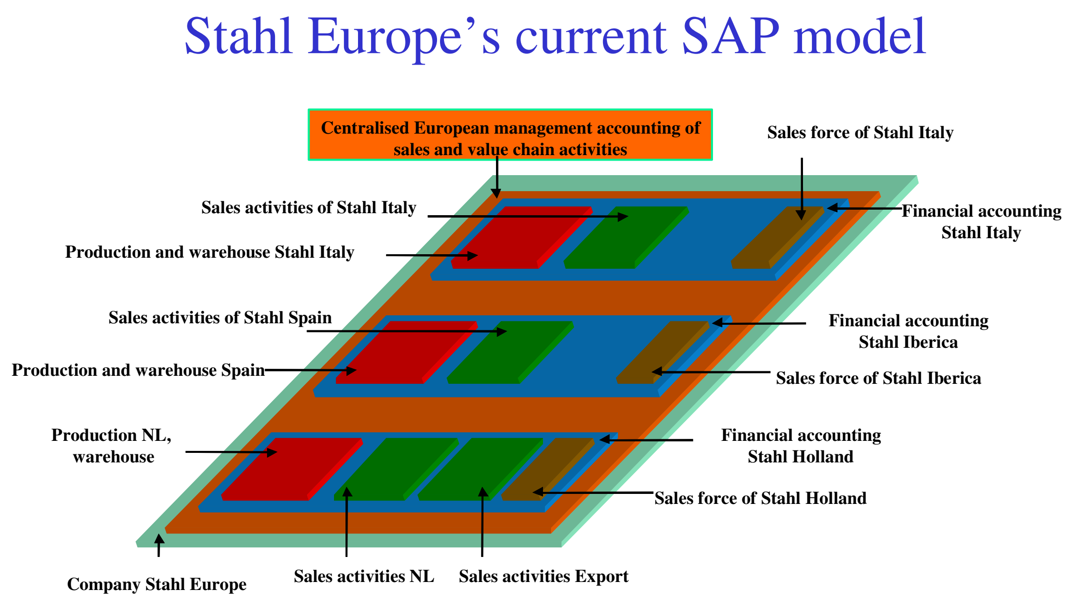

Figure 5: Stahl Europe current SAP system overview

This figure clearly shows that, from an IT-systems point of view, the sales-, purchasing-, manufacturing- and warehousing processes (in the red, green and brown coloured modules) are performed in each legal entity, which are integrated in the financial modules in each legal entity, while it provides management information on a European scale.

4 Criteria for evaluating the alternatives

The criteria for evaluating the alternatives are derived from the EMB vision statement and its organisational principles:

Any new structure for Stahl Europe should:

- Facilitate the Europe based processes with minimum of administrative activities;
- Reduce operational complexity in business processes and systems;
- Reduce fixed costs;
- Not hinder the current legal entity ownership structures and their developments over time;
- Fully be able to comply with European fiscal rules;
- Be able to support the current and future SAP systems;
- Be easy to extend if further activities of Stahl in Europe do crystallize;
- Not create large fiscal negative consequences other than the current existing ones;
- Improve the information on product and customer profitability on a European basis.

The criteria above will be evaluated for every alternative as mentioned in chapter 3 and broken down into the following sections (the bold and italics abbreviations between brackets will be used in the next chapter for the analysis):

<u>*Fit with business objectives:*</u>

1. Direct customer contact activities should be executed at the local legal entity (see section 3.2.2); ***(local customer activities)***
2. Management of the business should be supported on a European basis for sales, supply chain and financial management (see section 3.2.2); ***(European business management)***
3. Improve product and customer profitability information on a European basis, the so called “roll-through” profitability (see section 1.3); ***(roll-through profitability)***
4. Reduce complexity (see section 1.3 and 3.2.3)
    a. Business processes ***(process complexity reduction)***
    b. ERP systems set up ***(systems complexity reduction)***
5. Reduce fixed costs (see section 3.2.3); ***(fixed costs reduction)***
6. Changes to business processes in future should be facilitated in an easy way (see section 1.3 and 3.2.3); ***(facilitate future changes)***

<u>*Implementation effort and costs:*</u>

Includes the extra time and effort in changing from the current trading model to a new one (***Implementation effort & costs).***

5 Analysis of the various trading models for Stahl Europe

In this chapter the various trading models are analysed whether they "fit" with the criteria derived from Stahl Europe's strategy and objectives as mentioned in the previous chapter. Table 6 gives an overview of Stahl Europe's current and desired business processes, indicating whether these are or should be managed locally or centrally. From a centralisation/decentralisation of processes point of view, the SBE-model provides the best fit with Stahl Europe's strategic direction.

L = Local ; C = Central	**Stahl European business now**	**Stahl European business strategy**	**Multi-business Entity**			**Single Business Entity**
			Single Market	**Multi Market**	**Re-invoicing**	
PTO processes (Prospect to Order)						
Marketing & Pre-sales process	C	C	L / C	L / C	C	C
Define strategy & develop target customers	L / C	L / C	L / C	L / C	L / C	L / C
Promote products & services	L / C	L / C	L / C	L / C	L / C	L / C
Develop sales plans	L / C	L / C	L / C	L / C	L / C	L / C
Manage sales and technical service force	C	C	L / C	L / C	C	C
Manage strategic partnerships	C	C	L / C	L / C	C	C
OTC processes (Order to Cash)						
Order Fulfilment process	L	L / C	L	L	L / C	L / C
Credit control Process	L	L / C	L	L / C	C	C
Distribution	L	L	L	L	L	L
Billing/invoicing	L	C	L	L / C	C	C
Intercompany invoicing	L	N/A	L	L	C	N/A
Accounts receivable	L	C	L	L	C	C
Receipts processing	L / C	C	L / C	L / C	C	C
MTS processes (Manufacturing to Stock)						
Product costing	L	L / C	L	L	L	L / C
Inventory Management	L	L / C	L	L	L	L / C
Asset Accounting	L	L	L	L	L	L
PTP processes (Procurement to Pay)						
Define sourcing strategy	L / C	C	L / C	L / C	L / C	C
Develop vendor relations	L / C	C	L / C	L / C	L / C	C
Set up buying contracts	L	C	L	L	L	C
Call-off from buying contracts	L	L	L	L	L	L
Purchase invoice processing (external)	L	C	L	L	L	C
Purchase invoice processing intercompany	L	N/A	L	L	L	N/A
Goods receipts processing	L	L	L	L	L	L
Accounts Payable	L	C	L	L	L	C
Payable processing / treasury	L	C	L	L	L	C
Overall processes						
Management (Business) Reporting	L / C	C	L / C	L / C	L / C	C
Regulatory reporting	L / C	C	L / C	L / C	L / C	C
General Ledger Accounting	L	C	L	L	L	C

Table 6: Stahl Europe's current and desired business processes: locally or centrally managed

The next sections will give an analysis of the various trading models. Each model will be displayed graphically and any impact versus the current IT model will be discussed. The "fit" with Stahl Europe's strategy and objectives will be presented in table form. The markings under the column "Fit" have the following meaning:

+ + highly positive
+ positive
O medium
– negative
– – highly negative

5.1 Analysis of the multi-business single market entity trading model

This trading model is Stahl Europe's current trading model and is displayed in Figure 1 of section 3.2.4 and the current IT model is already discussed in section 3.2.5.

Criteria	*Fit*	*Comments*
Local customer activities	+ +	All activities are carried out and managed locally
European business management	–	A strong local entity presence makes it difficult to operate in a truly European way
Roll-through profitability	– –	No roll-through profitability directly available; all information is intended to be used on a local level
Process complexity reduction	O	Processes are likely to be more standardised on a local level in stead of a European level; more differentiation is therefore likely within Europe
System complexity reduction	O	The current system fully supports this trading model
Fixed costs reduction	O	No changes since this model is the current position
Facilitate future changes	–	Changes in business processes or SAP affect all units; all units and the people operating the processes / systems in these units need to be (re-) trained in proposed changes
Implementation effort & costs	+ +	No implementation effort and costs, since it is the current model

Table 7: Analysis of multi-business single market entity trading model

From the analysis it is clear that this trading model is not really geared up to running a true European business and does not take away any of the current issues of section 1.3. The model reflects the "old" Stahl way of doing business in Europe with legal entities in each country having large autonomy for their local processes.

5.2 Analysis of the multi-business multi-market entity trading model

The analysis of the second trading model is presented in Table 8. This model is characterized by the fact that a product is shipped and invoiced to any customer in Europe from the place it is available, which would normally be the legal entity that produces the product.

This would not work for Stahl: the most important non-financial measure, which Stahl has implemented as part of the MRP-II Class 'A'-processes, is customer service (see section 1.2). This is defined and measured as delivery of products to customer against promise for all orderliness in one order. The fact that a full customer order needs to be delivered at the same time to the customer is critical to Stahl's customers, since they only cannot progress their production processes in full if they miss only one item. This requirement is only for customers in the Leather Products business unit, which is the most important business unit. A Leather Products customer order typically has 5 to 7 orderlines in one order. When these products are manufactured in more than one legal entity, which is highly likely, this trading model by its nature does not fulfil this requirement.

Criteria	*Fit*	*Comments*
Local customer activities	-	Local sales people are partly restricted in their decision making powers to agree prices, conditions etc. (to prevent Permanent Establishment tax issues) which could jeopardise the local business; since the local service team is almost fully technical service oriented and not as sales representatives, this issue becomes manageable
Local customer activities	+ +	All activities are carried out and managed locally
European business management	–	A strong local entity presence makes it difficult to operate in a truly European way
Roll-through profitability	+ +	Roll through profitability is not an issue here, because the production legal entity invoices the customer directly, wherever located in Europe
Process complexity reduction	– –	This set-up would create one critical issue from an operational point of view: the typical customer is ordering 6 orderlines on one order and he needs to get all products at the same time to work properly which is measured by Stahl's customers level (On-Time In-Full). This would be almost impossible to achieve; order entry, credit control and administering customer receipts would become more complex
System complexity reduction	O	The current system fully supports this structure
Fixed costs reduction	O	No changes versus current position
Facilitate future changes	O	No change versus current situation
Implementation effort & costs	O	No implementation effort and costs

Table 8: Analysis of multi-business multi-market entity trading model

This trading model for Stahl Europe is visualised in Figure 6: Stahl Iberica, Stahl Italy and Stahl Holland would continue to buy raw materials, produce and sell these to any customer in Europe. The fact that various Stahl agents will have more principals may seem to be complicated, but this can be dealt with quite easily. Setting an arm's length agency fee may present more issues, since there are differences in the value of products which are produced at every manufacturing location.

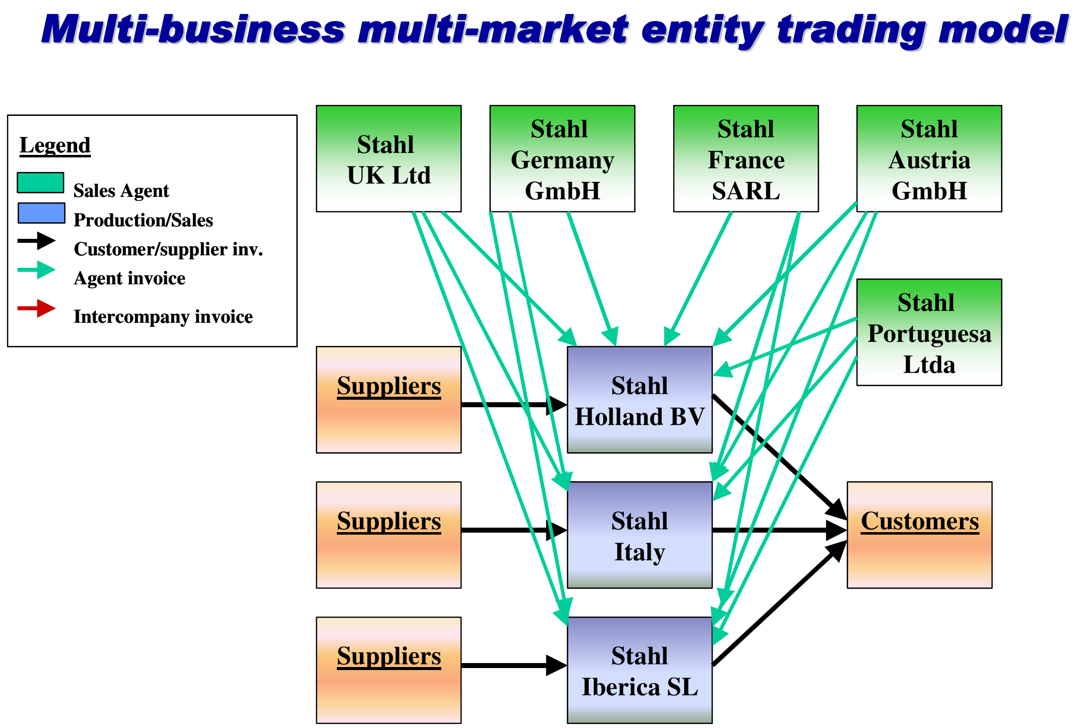

Figure 6: Legal entities and their function in a multi-business multi-market entity trading model

This trading does not change the current IT model for Stahl Europe as described in section 3.2.5. Every legal entity continues to use all SAP R/3 modules. Only some processes within are getting more complex as described above.

5.3 Analysis of the multi business re-invoicing entity trading model

The analysis of the third trading model is presented in Table 9. In this model (see Figure 7) Stahl Holland is seen as the Central Entity (CE), because it is the largest legal entity from a production, sales and headcount point of view, employs most members from the business management, members of the EMB, and it has an extensive R&T Department for Europe. This model is characterized by the fact that Stahl Iberica and Stahl Italy do not have their own customers any more and have therefore become sales agents from Stahl Holland and that all their production is invoiced to Stahl Holland.

Criteria	*Fit*	*Comments*
Local customer activities	-	Local sales people are restricted in their decision making powers to agree prices, conditions etc. (to prevent Permanent Establishment tax issues) which could jeopardise the local business; since the local service team is almost fully technical service oriented and not as sales representatives, this issue becomes manageable
European business management	+	Supports a European business management from a sales point of view; other processes are being dealt with locally
Roll-through profitability	– –	The roll through profitability issue is increased in this trading model since all producing units would sell their production to the central legal entity.
Process complexity reduction	–	All activities would remain locally apart from invoicing and credit control; transfer pricing issues would increase especially for units who produce part of their production for customer in the countries they are now responsible for; increased complexity around VAT processes and reporting
System complexity reduction	O	No changes in system complexity
Fixed costs reduction	O	No changes are foreseen
Facilitate future changes	O	The impact is restricted to changes in invoicing and credit control
Implementation effort & costs	–	Implementation effort and cost is limited to changes in invoicing and credit control; corporate income tax consequences for implementing this trading model would need a specific tax review and advise.

Table 9: Analysis of multi business re-invoicing entity trading model

The analysis shows that only the sales processes are different from the previous trading model, which gives good support to the European sales business, but which also increases the roll-through profitability even further (to about 50% of the total external sales).

With regard to the IT model, this trading model requires no change versus the current model, because Stahl Iberica and Stahl Italy keep on invoicing from a systems point of view. The fact that they now only have one customer they invoice, Stahl Holland, does not make a difference.

Multi business re-invoicing entity trading model

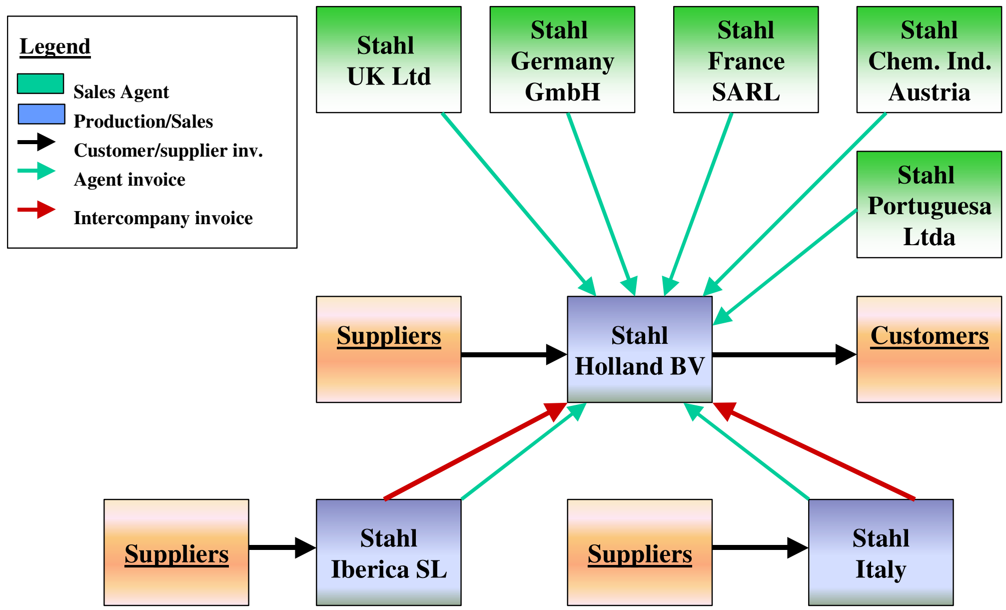

Figure 7: Legal entities and their function in a multi business re-invoicing entity trading model

5.4 Analysis of the single business entity trading model

The analysis of the third trading model is presented in Table 10. In this model (see Figure 8) Stahl Holland is seen as the SBE, due to the same reasons as give in the previous section. This model is characterized by the fact that Stahl Iberica and Stahl Italy have no involvement in the business from an administrative point of view, other than as agents or as toll manufacturer. All business processes are being carried out in name of the SBE.

Criteria	*Fit*	*Comments*
Local customer activities	–	Local sales people are restricted in their decision making powers to agree prices, conditions etc. (to prevent Permanent Establishment tax issues) which could jeopardise the local business; since the local service team is almost fully technical service oriented and not as sales representatives, this issue becomes manageable
European business management	+ +	Fully supports a true European business management: financial information, supply chain and sales
Roll-through profitability	+ +	No issues with roll-through profitability, since no sales from one legal to another is performed in the system
Process complexity reduction	O	Several processes are simplified and are being carried out centrally; transfer pricing issues for products is replaced by transfer pricing issues for agents & toll fees which are easier to handle from a process point of view; on the other hand several processes are more complex since more people from one legal entity are involved; VAT set up is more complex
System complexity reduction	+	The IT system set-up is simplified since several key modules are only needed for the central legal entity
Fixed costs reduction	+ +	Fixed costs reductions can be obtained in Finance, Purchasing, Distribution
Facilitate future changes	+	The trading model is simpler from a design and execution point of view; new legal entities can be integrated with less people and time
Implementation effort & costs	– –	High implementation effort and costs from a business, tax and IT point of view

Table 10: Analysis of a SBE trading model

The IT model will need to be changed to reflect the changes of the functions of Stahl Iberica and Stahl Italy. This is displayed in Figure 9. Reference is also made to Figure 2, which shows which modules are no longer used by the Stahl Iberica and Stahl Italy (all modules coloured yellow). All financial data, apart from local costs in Spain and Italy, like salaries, engineering, maintenance, are now centrally under control of the SBE, Stahl Holland. Since there is no need to invoice other legal entities within Europe, all intercompany invoicing is automatically eliminated, and so is the issue of roll-through margin reporting.

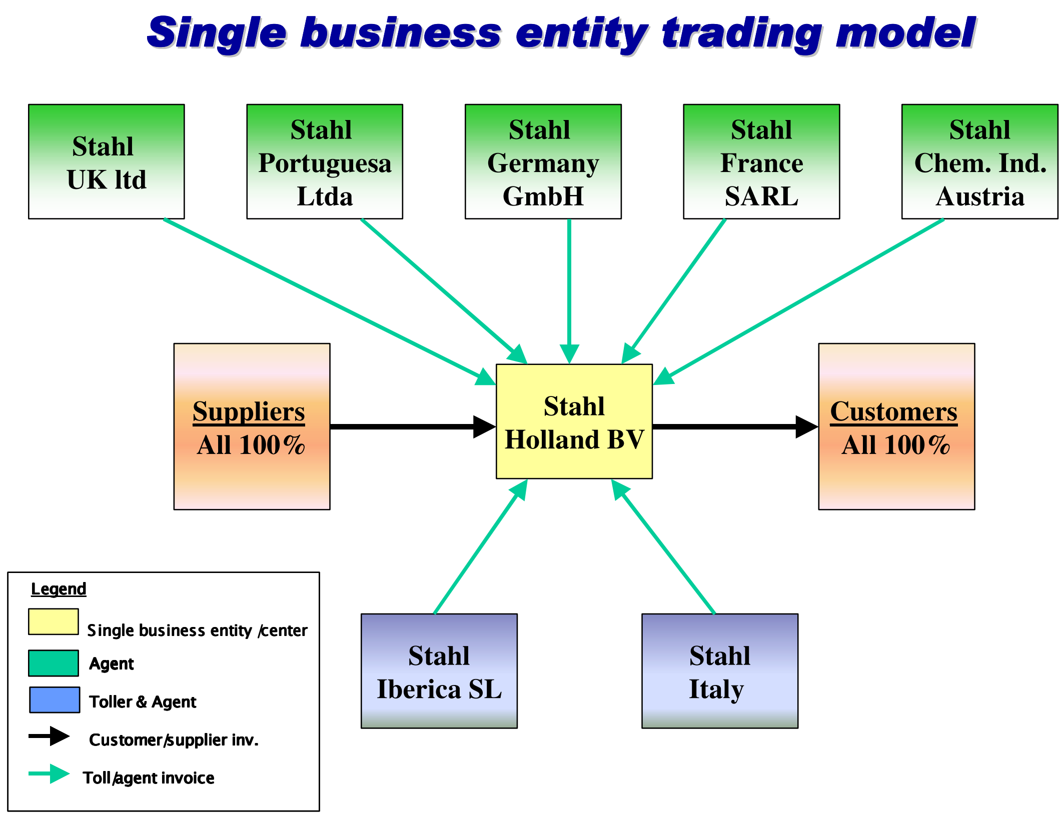

Figure 8: Legal entities and their function in a SBE trading model

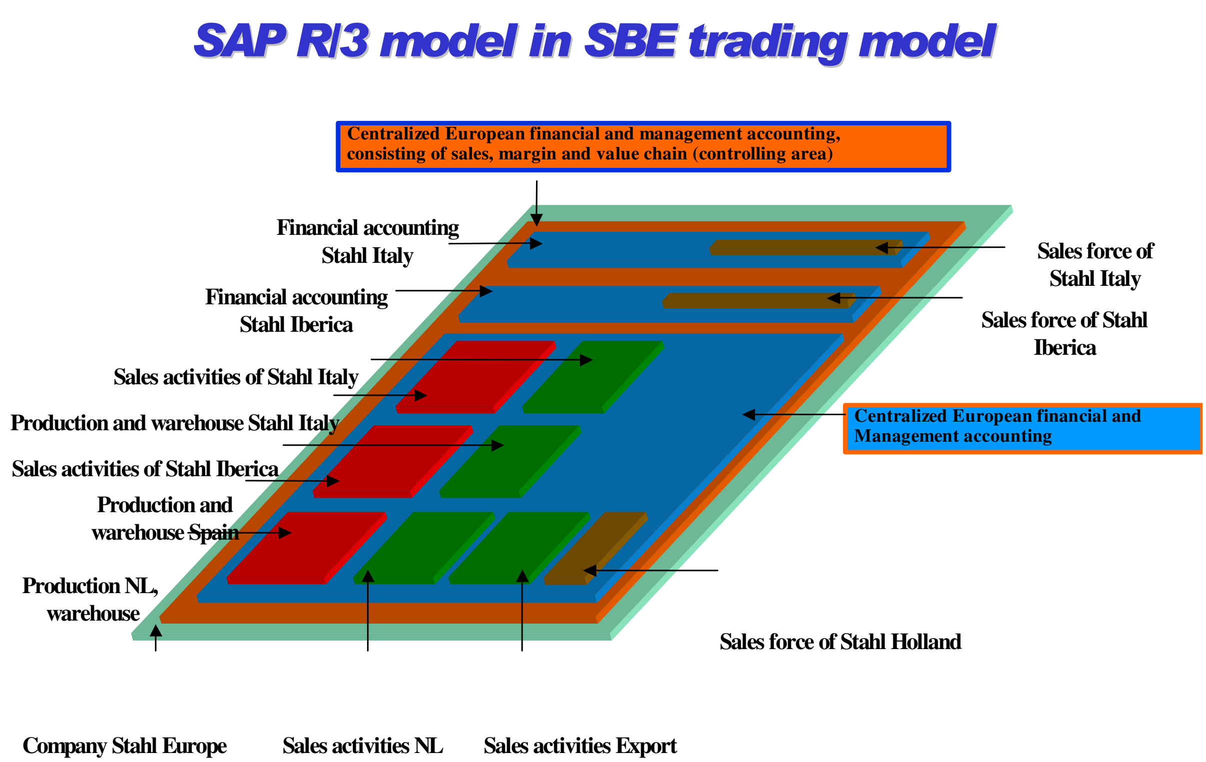

Figure 9: The IT model in the SBE trading model

5.5 Conclusions from the analysis

The conclusions from the analyses can now be made. From the four given options the SBE trading model is the one that supports the objectives for most criteria and takes away most of the issues management has with the current trading model, as can be seen from the business process analysis in Table 6 and the overview of the fit with the strategy in Table 11. The SBE trading model however increases complexity mainly in the order handling process and the VAT related processes and is the most complex one to implement.

The option of the multi-unit multi-market trading model forces processes which are in fact completely in contrast with Stahl's customer service objective and measures, so this option is definitely ruled out.

The option of the multi business re-invoicing trading model increases the roll-through profitability issue and would add some complexity in the order to cash business processes. The implementation is however less complex and costly than the SBE option.

The initial conclusion is therefore that the SBE trading model should be pursued if the savings in fixed costs and the advantages it provides to truly supporting the European Stahl business outweighs the complex and costly implementation. This will be discussed in the next section.

	Multi-business Entity			**Single Business Entity**
Criteria	**Single Market**	**Multi Market**	**Re-invoicing**	
Local customer activities	+ +	–	–	–
European business management	–	–	+	+ +
Roll-through profitability	– –	+ +	– –	+ +
Process complexity reduction	O	– –	–	O
System complexity reduction	O	O	O	+
Fixed costs reduction	O	O	O	+ +
Facilitate future changes	–	O	O	+
Implementation effort & costs	+ +	O	–	– –

Table 11: Overview of fit between Stahl Europe's strategy and trading models

5.6 Costs and benefits

The high level costs and benefits are listed in Table 12 and explained more in detail below (in EUR 1,000). The project has a payback of approx. 2 years.

Cost / Benefit element	***One off***	***Ongoing***
Benefits:		
Manpower net savings in Finance, Supply Chain and Purchasing (7,5 FTE)		+ 300
Reduction in stocks	+ 200	
Reduction of freight costs		+ 100
Reduction of purchasing cost of material		+ 200
TOTAL BENEFITS	***+ 200***	***+ 600***
Costs:		
Legal/fiscal consultancy fees	- 75	
IT costs	- 500	
Project costs (incl. redundancy cost)	- 800	
TOTAL COSTS	***- 1,375***	***0***
NET COSTS/BENEFITS	***- 1,175***	***+ 600***

Table 12: Cost and benefits overview SBE trading model

The background and reasoning of the costs and benefits will be discussed now:

Benefits:

Reduction in Finance manpower is the largest and this is due to the fact in the local entity hardly only local costs will need to be administered: all activities around sales, inventory, purchases, margin analysis, pricing, payments to suppliers and from customers etc. will transfer to the central company.

Reduction in stocks is due to increased visibility of product availability in the system for the users, and to some extent the increased central control.

Reduction of freight costs is a result of increased purchasing power and better use of European distribution techniques by central control and coordination.

The reduction in Purchasing manpower is due to the fact that in future only one Purchasing department will agree and put contracts in place on which the local units can place their local demand. Furthermore it is estimated that increased purchasing power on a European basis will result in lower purchasing cost of raw materials and packing materials.

Costs

The IT costs relate to a required upgrade, which is needed to take care of the VAT issues in the SBE model. The current version of SAP which Stahl Europe uses does not offer this functionality and training of users in the new setup.

Project cost contains mostly redundancy cost and cost of the project team, communication costs and contingency costs.

6 Implementation issues single business entity trading model

Changing towards a SBE trading model is in fact a major change in the current way of working and should therefore be treated as a very important business change project. It should not be regarded as an IT project although it would mean a big change in the way the IT model is set up. People from all legal entities in Stahl Europe would need to be involved to some degree on the foreseen changes and their cooperation and commitment is needed in making such a change.

The issues with implementing a SBE trading model for Stahl Europe can be broken down into the following categories:

- Impact on the business
- Fiscal
- IT model

These will be discussed in the sections below.

6.1 Issues with business impact

The following issues with business impact are identified:

1. Changes in business processes:
   a. Functions and activities which need to be performed from the "centre" in future are:
      - setting sales prices, payment terms and conditions
      - setting up purchase contracts for all raw materials and packing materials
      - payment of all raw material purchases and management of all customer receipts
      - management reporting of sales and contribution analysis

   b. Changes in local activities:
      - stop with all activities as listed above
      - involve local customer service in credit control: chasing

   c. Changes of the relations between the local entity and the "centre":
      The order-to-cash and purchase-to-pay processes will involve both local and central activities. This requires excellent execution of processes to prevent errors and difficulties in communication to resolve these.

2. Changes in responsibilities of local sales managers: at this moment local sales managers are responsible for setting prices, discounts, rebates, payment terms and conditions although these are currently in fact overviewed and controlled by the centre to a large extent. In the SBE trading model these activities should be performed by the centre to prevent permanent establishment issues. This change needs to be dealt with carefully to ensure sales managers are kept motivated.

6.2 Fiscal issues

The following issues that are related to tax need to be taken into account and require expert tax advise from:

1. Transferring business from one legal entity to another legal entity in another country would normally trigger payment of goodwill, which would be taxed in the country which transfers the business and which will be tax deductible in 5 years if transferred to Holland. This could be beneficial if there would be tax losses in the country that transfers the business (there are no losses in Holland). Otherwise this issue of paying goodwill could be prevented by setting the agency- and toll-fee to an arm's length level that this would be in line with than if the company would have continued selling products to customers itself. Also from a Dutch tax perspective this would be an acceptable solution, but it is advised that the final solution would be signed off from the tax advisors in every country. A transfer pricing report should be written to support the arm's length basis of the toll- and agency fees.

2. The issues around VAT would become much more complex, due to the fact that a Dutch company would be the owner of the inventory in various countries and would need to pay toll- and agency fees:
   - The central company would need to register for VAT in all applicable countries, with appointment of fiscal representatives where needed and it needs to file VAT returns in accordance with the VAT legislation in each country
   - VAT treatment of consignment stocks, changes in transfer of stock from one country to another, agency fees and toll fees needs to be done properly and implemented in systems correctly
   - More complicated intrastat reporting

3. If a permanent establishment (PE) is not wanted by the company (as is with Stahl) changes in the order handling process are required to be able to show to tax authorities that only the SBE is controlling prices, sales conditions and terms and the company should be able to prove this is done consistently over time.

   Overall it should be noted that implementing a SBE trading model brings with it some increased tax risks. There will be a fundamental change in the nature of the business activities carried out by the Stahl legal entities, and this in itself is likely to lead to questions from the tax authorities in these countries. The importance of documentation to support the approach taken is paramount.

6.3 Issues with the IT model

1. Changes to current incoming and outgoing interfaces
2. The changes in the VAT area are not supported by the current 3.i version of SAP. It is therefore advised to go to version 4.6, which does support these aspects. The SAP support for the current version runs out by end 2003, so there is anyhow a need to upgrade to a later version. Furthermore a decision should be taken to convert to the new version to make a fresh instalment.
3. Changing the legal structure results into a transfer of master files for customers, vendors, materials, plants, work centres and cost centres.
4. Due to the large impact on the SAP system and the time and resources, which it takes for application consultants, users and key-users, it needs to be planned properly in line with other initiatives undertaken by the business.

7 Overall conclusions

The main question of this thesis is:

In which way can Stahl change its trading model for its European operations best to ensure that it will meet its strategic objectives and how can the implementation issues of this change be addressed?

And the related sub-questions are:

- *What is a trading model?*
- *Which trading models are available for the Stahl Europe business?*
- *What are the criteria to be used to decide on the future trading model?*
- *What trading model fits best with Stahl's strategy and objectives for Europe?*
- *What are the issues around the implementation of the proposed trading model and how can these be tackled?*

How far have we come in answering these questions?

The trading model was defined as "the total relationships of an international company with respect to business processes, IT-model and its fiscal structure".

Four trading models have been identified:

- The multi-business single-market entity model,
- The multi-business multi-market entity model,
- The single-business re-invoicing entity model, and
- The single business entity-trading model.

The characteristics by trading model have been discussed in general with regard to its business processes, its supporting IT-model and its fiscal structure.

The strategy and objectives of Stahl's European business was discussed and it is used, as a basis to select the criteria to evaluate which trading model is the most appropriate one for Stahl Europe. The four trading models have been evaluated against these criteria in detail and it has been concluded that the Single Business Entity (SBE) trading model was the trading model that supported best Stahl Europe's strategy and objectives, because:

- It eliminates intercompany invoicing, resulting in management information on "roll-through" gross margin for customers and products in Europe without any additional steps;
- It results in lower operating costs, mainly in the finance area;
- It increases the focus on the external business;
- Increased control of processes, which are needed to run a true European business;
- Future changes in business processes and systems can be implemented more easily and quickly.

Apart from these benefits, the SBE model forces some changes in the local customer contacts since it requires that several important decisions need to be made by the SBE. However, since most direct customer contact is by leather technicians and customer service people, who are not directly responsible setting sales prices and conditions, it is believed this risk is minimal when managed properly.

The other disadvantage is that implementing the SBE model is difficult, expensive and time consuming. Therefore a financial evaluation of costs and benefits was prepared, which showed that the implementation costs has a 2-year pay-back.

The overall conclusion is therefore that Stahl should change its trading model to an Single Business Entity trading model, since it supports Stahl Europe's strategy and objectives in the best way and because the benefits outweigh its implementation costs.

Finally the implementation issues were discussed, highlighting the fact that the change to the SBE trading model should be regarded and executed as an important business change project and not as an IT-project with a leading and visible role of Stahl Europe's business management. The implementation issues which are broken down into business impact, fiscal and IT were identified and discussed and should be used as building blocks of the implementation.

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