

Threading Your Way Through the Ins and Outs of Outsourcing to Build an Effective HR Solution

By Michael Eck

Part 1

Although HR professionals have been using outsourcing in one way or another for many years, the trend continues to gather steam. A growing number of organizations are outsourcing at least some of their HR functions (see "[Outsourcing Defined](#)"). Some point to increasing cost pressures or the need to relieve staff of their administrative burden. Others say they are looking to improve their focus, access first-rate capabilities, share risks and rewards, keep up with rapidly evolving technology, deal with increasing regulatory and compliance requirements and/or to better manage continuous change.

This article looks at the current state of outsourcing — what HR is outsourcing now and why. A follow-up article in the next issue of *Perspectives* will discuss the segmentation of the outsourcing market, provide some tools to help in decision-making and discuss how to make the right choices when outsourcing.

Why Organizations Outsource: The Fact and the Fiction

Most HR departments have many common expectations and perceptions about outsourcing — not all of which are true.

When viewed objectively, Sibson has observed that outsourcing actually does:

- **Increase Efficiency** It allows organizations to take advantage of what others have learned. They already have found ways to improve efficiency and have solved many of the problems that other companies are now experiencing.
- **Free Internal Resources and Allow HR Practitioners to Be More Strategic** Instead of entering data, crunching numbers and pushing paper, HR can focus on core/non-administrative functions. Offloading the administrative work maximizes the organization's resources.
- **Offer Access to Expertise** Organizations that outsource gain access to know-how they probably do not possess. They tap into a broad network of experienced people and best practices.

There are, however, some common misconceptions about outsourcing, including the belief that it can and will in every situation:

- **Cut Costs** Although outsourcing will provide cost savings for some organizations (mostly those that are very large and extremely inefficient), in most cases, it is dollar-for-dollar cost neutral. Take an organization with hundreds of people in HR: If it can save just 5 percent of the \$100 million dollars it spends on HR, it will save \$5 million. But a company with only 10 people in HR is not going to pay for the service by shifting the work off one or two employees. What will happen is that the department will gain an increase in benefits or services — more bang for the buck.

- **Keep Up with the Latest Technology** Many HR departments are stuck with old technology and find it difficult and expensive to upgrade. Outsourcers, however, are expected to keep up with technology and provide the service at a reasonable cost. This is true for some vendors, but not all. It is up to the organization to check and manage the relationship correctly.
- **Provide Improved and Additional Services** As with technology, this is true to some extent. While the organization can get improved services, it will have to negotiate for them and they will come at a cost.
- **Share Risk** Although it is somewhat true that risk is shared between the HR department and the outsourcer, this is typically mitigated by the contract, and that is what determines where risk stops and starts, particularly around compliance efforts. In almost all cases, the risk stays with the organization.

Why Some Organizations Choose Not to Outsource

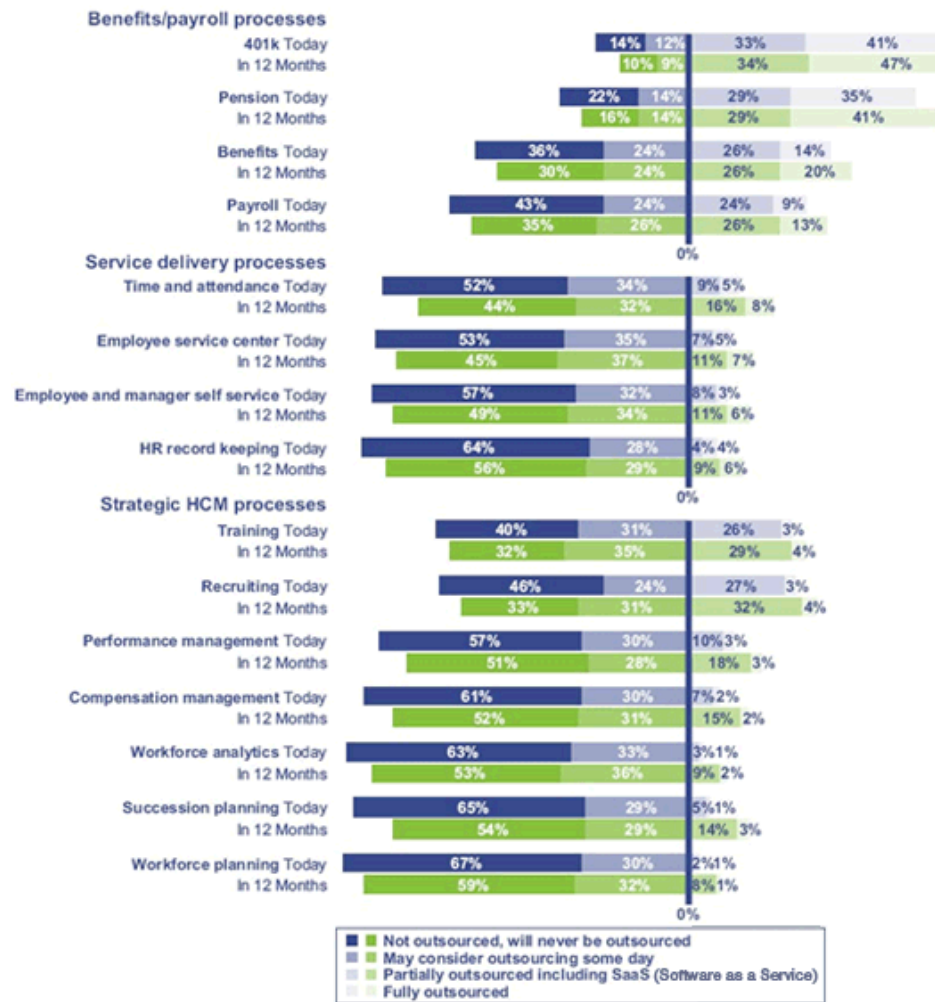
In our experience, some HR departments prefer not to outsource because they:

- **Cannot Justify the Outsourcing Fees** Outsourcing may cost more, but the organization will get more. The question is, what does the organization need, and can it afford more?
- **Have a Competitive or Strategic Advantage in a Particular Function** If an organization does something particularly well, it has little to gain and much to lose by outsourcing it.
- **Fear Losing Control** While it is true that some control must be surrendered in any outsourcing relationship, processes can be established to ensure the organization has all the control it needs. Nevertheless, some HR departments prefer to play their cards close to the vest.
- **Already Have the Investment, Infrastructure and Expertise in Place to Perform These Duties** The organization may have already made a large capital expenditure in people, process and/or technology and has costs to recover.
- **Believe their Internal Staff and Systems Are Not Ready** This is often a cultural issue. Some HR departments are not prepared for this kind of change.
- **Do Not Have the Resources and Skills They Need to Manage External Vendors** They have HR practitioners, but outsourcing calls for relationship managers — a different skill set.
- **Think Outsourcing would Be Culturally Unacceptable** In many cases, organizations have never outsourced because it conflicts with their practiced business policies.
- **Cannot Find “Suitable” Outsourcers** Although in some cases this is just an excuse, some organizations are looking for something that does not exist. For instance, they may want to outsource the distribution of electronic files for data exchange and nothing else, which is not possible.
- **Have Unusually High Security Requirements** This is largely a matter of perception. Most outsourcers have very high standards in place and pass multiple audits. Yet HR information is very sensitive and some organizations still believe they have stronger firewalls than anybody else. In short, they do not want anyone else managing their data.

What Are Organizations Outsourcing?

HR departments can outsource their technology, their people and/or their processes. The most common approach for mid-sized organizations is to outsource their technology and a part of their processes. As Figure 1 shows, the most popular process to outsource is 401(k) plan management, followed by pensions and benefits.

FIGURE 1: IN-HOUSE VERSUS OUTSOURCED CHOICES — PROCESSES



Source: CedarCrestone 2007-2008 HCM Survey

What the Data Shows

How do organizations like insourcing vs. outsourcing? Some of the findings are surprising. As Figure 2 demonstrates, when it comes to HR solutions (technology, people and process), HR departments that outsource say it has allowed them to avoid new information technology/capital expenditures and reduce software implementation times. Those that use in-house solutions say it has improved employee productivity and made it easy to integrate new services.

FIGURE 2: COMPARING THE KEY ACCOMPLISHMENTS OF ORGANIZATIONS WITH IN-HOUSE SOLUTIONS TO THOSE WITH OUTSOURCED SOLUTIONS

Accomplishment	Percent of Organizations that have Achieved this Accomplishment ...	
	... With In-house Solutions	... With Outsourced Solutions
Enabled HR to serve in a more strategic capacity.	80%	69%
Reduced administrative services expenses.	70%	69%
Improved employee productivity.	68%	48%
Achieved a return on investment.	64%	62%
Eased the integration of new services.	54%	38%
Affected internal staffing levels.	46%	48%
Enabled workforce performance measurement.	38%	28%
Achieved an executive mandate.	35%	30%
Avoided new IT/capital expenditures.	27%	54%
Reduced software implementation times.	27%	46%
Had an impact on shareholder value.	26%	26%

The arrows indicate accomplishments for which there is a major difference (16 percentage points or more) between organizations that outsource and those that handle solutions in house.

Source: CedarCrestone 2006 HCM Survey

The employee productivity example in Figure 2 is particularly interesting because it is contrary to what most HR professionals think: that outsourcing will improve productivity. In this instance, the portion of organizations with in-house solutions that say productivity has improved is actually 20 percentage points higher than those that have outsourced.

Conclusion


HR has evolved a great deal in recent years, moving away from administrative work to become a respected professional and a partner in the organization's business. Now, it is becoming a business leader that is ROI-focused and technology savvy. Outsourcing is one of the levers HR has used to move along this path. Although the reasons to insource or outsource HR processes, technology or people continue to vary from organization to organization, outsourcing remains a popular approach for delivering HR services.

Organizations need to identify their critical roles and the performance of individuals in those positions to determine whether and why they are losing top talent. They then need to quantify the effects and take steps to make any necessary corrections. While this is not an easy process, the returns can be significant, especially in today's tightening labor market.

Coming in the next issue of Perspectives: "Threading Your Way Through the Ins and Outs of Outsourcing to Build an Effective HR Solution; Part 2: How to Make the Right Choices When Outsourcing."

About the author:

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Outsourcing Defined

Within the world of HR, outsourcing is the performance of functions/services outside of the organization by a third party, utilizing the third party's staff and system technology. It can be domestic, near-shore (Canada and Mexico) or off-shore (including India, the Philippines and Central Europe). This is opposed to insourcing, which means the performance of functions/services is done within the organization with internal staff, utilizing in-house systems or technology. The in-house staff can be located on-shore, near-shore or off-shore. Standing somewhere between outsourcing and insourcing is co-sourcing, under which an organization shares responsibilities between itself and an outsourcer.

An HR organization can outsource its technology services (such as software), its people (by using contract labor, consultants, co-employment or temporary workers) and/or the entire business process.

Typically, HR will outsource technology services first and then, as they gain experience and confidence, move on to people and business processes.

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