



# OUTSOURCING IS {IN}

*Shift attention from routine tactical operations to critical strategic business issues by handing over noncore functions to third-party specialists.*

BY JAN NIEHAUS

**V**ertical integration as a business model had its heyday. Years ago, for example, auto manufacturers completely controlled the supply of their primary raw material: steel. But modern-day auto manufacturers don't own iron mines and steel mills. Rather, steel is a commodity, sourced from suppliers with quality material, a reliable supply, and good pricing.

Today, vertical disintegration is the trend, with companies outsourcing ancillary functions so they can focus on their core competencies. Financial institutions outsource call center operations; telecommunication companies outsource help desk functions; and companies in every industry are outsourcing facilities and vehicle maintenance, security, IT, some finance and accounting functions, and many HR tasks.

“Every firm has a set of business objectives it needs to accomplish,” explained Rakesh Kishan, president and CEO of UMS Advisory ([umsadvisory.com](http://umsadvisory.com)), an international management consulting firm that specializes in outsourcing. By outsourcing the more tactical considerations that can best be handled by others, a firm not only gets higher service levels and reduced cost, but also—and more importantly—frees up a lot of resources, allowing it to pivot its organizations and shift its attention to strategic business issues.”

When advising clients on whether or not to outsource, Kishan guides them through three determining criteria: “First, we look at whether or not the function they are considering outsourcing creates a competitive advantage for them. For example, smaller companies cannot match the resources of larger companies. Therefore, bringing in customized, specialized services is an option.

“The second criterion: Can the service be easily obtained? Are there mature suppliers available? If there are, then there is a higher likelihood of securing a qualified supplier,” he noted. “And the third: Can the service be easily specified so performance can be measured?”

According to a case study published by CDM Electronics in Turnersville, N.J., and ThomasNet ([thomasnet.com](http://thomasnet.com)), CDM offers a textbook illustration of the process. CDM set a goal of doubling annual revenue in five years by landing key international aerospace and military accounts.

In order to compete in this sophisticated market, CDM needed a robust, dynamic website with a comprehensive database and interactive catalog. And while not resident within CDM, the IT and engineering talent required to construct such a website was readily available from third-party Internet commerce specialists. Using performance metrics such as search engine rankings, site visits, first-time visits, unique user sessions, requests for information, and conversions, this new website enabled CDM to reach 150% of its revenue goal a year ahead of schedule.

## **OUTSOURCING OPTIONS**

Website development is just one of the technology services that companies are farming out in order to elevate service, reduce expenses, increase energy efficiency, limit carbon emissions, and remain agile in an ever-changing technological environment.

Cloud computing—which enables email, social media, online gaming, and many mobile applications—is large-scale, shared IT infrastructure that’s available over the Internet. A company can vastly expand its IT capacity through cloud computing without investing in equipment that will be obsolete

before it's fully amortized, specialized facilities to house it, the expense of operating and cooling it, and skilled staff to keep it going.

Software-as-a-Service (SaaS) gives companies access to sophisticated IT applications that they could never afford to develop or purchase. Again, IT staffing levels remain modest, and system maintenance is the SaaS vendor's responsibility.

Virtual events, such as meetings, trade shows, and training, which are typically accomplished through video conferencing, eliminate attendee transportation and lodging costs and the associated greenhouse gas emissions. According to *Media Business* magazine, the virtual events industry will grow by 56% a year to \$18.6 billion by 2015.

According to Kishan, "Other functions that are commonly outsourced are HR, parts of finance and accounting, and real estate—in general, the SG&A [Sales General & Administrative] functions where technology and scale can offer an advantage. Most firms don't need to have highly specialized insurance and accounting expertise in-house."

Case in point: Faced with a 42% increase in health insurance costs, Samson Electrical in South Plainfield, N.J., went shopping for a different carrier and coverage that would offset rising costs while maintaining quality employee benefits.

"One of the things that we were looking for was a provider that offered a variety of benefit analyses and how we could be strategic with our benefits. We wanted a well-rounded plan that was good for both the company and employees," said Brian Dubey, controller and CFO. The company also wanted to integrate payroll and benefits administration.

According to Patrick Carragher, director of benefits for CheckPoint HR (checkpointhr.com), "We helped Samson Electrical analyze its options not only with its current carrier, but also with competitors. We discussed the advantages and disadvantages in a variety of funding strategies. At the end of our evaluation and due diligence process, our HRA and specific funding recommendation was clear and concise and one that would be the best fit for Samson Electrical." The solution integrates benefits administration, payroll processing, reporting, and other HR functions.

"The other thing that we have seen since making the switch to CheckPoint HR is that all of our HR processes run a lot smoother—from an administration standpoint, it is less of a headache," Dubey explained. "Using our previous solution, we received multiple notifications each month. But with CheckPoint HR, the system is able to gather and report on information seamlessly—plus it is very easy to use. In addition, with many of the new healthcare laws coming out, CheckPoint HR has provided us with a comprehensive over-

view and analysis of the law changes and has allowed us to stay compliant."

### IS IT COST-EFFECTIVE?

Another HR function that companies often outsource is staff training and development. According to a 2009 survey by *Chief Learning Officer* magazine, 46% of companies outsource training, development, assessment, and simulations.

Barbara Carnes, founder of Carnes & Associates (carnesandassociates.com) in St. Louis, provides leadership development and assessment tools, coaches, and trains learning and development staff in a range of industries, including electrical distribution.

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**—Mike Anderson, Granite City Electric Supply**

In Carnes' experience, "When a company gets to about 50 employees, it's time to hire an internal person devoted to HR. Still, this is just one person, usually a generalist, and he or she may not have the specialized expertise that's needed for some projects. For example, the compensation system might require an overhaul, and a specialist is needed to implement it.

"Companies within the 50-to-250-employee range are usually in need of a certain amount of learning and development, such as supervisory skills, harassment, and leadership training for all managers. The expertise may not be available internally," Carnes explained.

Technology-driven transactions are strong candidates for outsourcing, Kishan pointed out. Carnes agreed: "In the case of payroll, it may be more cost-effective for the company to hire an HR firm that offers a wide range of services, such as payroll, employee benefits management, worker compensation, training and development, and compensation metrics analysis," she said.

Billtrust and Transcepta both offer Internet-based invoicing services, which get clients' invoices out faster, eliminate paper, reduce carbon emissions, and feed the accounting data into common accounting systems such as QuickBooks.

Granite City Electric Supply in Quincy, Mass., relies on Billtrust for accounts receivable. "Our company has always placed an emphasis on identifying productivity opportunities across our organization," said CFO Mike Anderson. "Early on we recognized that Billtrust could help us achieve cost savings on postage, material, labor, and IT." Granite City achieved immediate savings above 25%, Billtrust reported.

"A key part of our strategy is to continue to reduce our

costs by leveraging Billtrust's products and expertise to migrate more of our customers to eBilling," Anderson continued. "So far, more than 50% of our customers have adopted eBilling."

## **MANAGING 3PL SUPPLIERS**

"It's hard in this day and age to not outsource," Kishan remarked. He warned, though, against incomplete research and hasty decisions. "These are not transactional contracts. They are longer-term relationships with sophisticated contracts. Many clients haven't previously dealt with the question of whether or not to outsource. Because we are neutral, we can look at their operations without bias and help them determine the business case for outsourcing.

"We ask what they will spend in the next five years on the function if it's kept in-house and how it impacts their P&L," he continued. "If the NPV [net present value] under an outsourcing scenario is positive, then they should consider removing it from their vertically integrated operation."

When a client determines that the particular function is not really core and that someone else may be doing better, UMS helps them put the specifications together and build the RFQ. Clear specifications are critical, as Kishan explained: "With your own people, they will do anything you ask them to do. With a third-party supplier, they will do what is specified, what they are going to be measured on."

UMS also helps clients identify prospective suppliers, evaluate their proposals, and negotiate the contract.

Kishan offered another warning: "One doesn't go into autopilot after outsourcing a function. Mastering the management of these third-party suppliers is a lot of hard work, but a different kind of work. You need much higher levels of internal management competencies. And if current management lacks the requisite competencies, this skill development challenge may require further outsourcing."

One final thing to be aware of: Bringing in consultants or specialists almost always causes a ripple, if not a permanent change, in the cultural fabric of an organization. Employees may fear that their jobs could be eliminated, and when an entire function—such as billing or benefits administration—is outsourced, layoffs usually do occur. When a customer-facing function is outsourced, customers may worry about a possible decline in service quality.

Prevent problems by talking with your employees and customers in advance of any outsourcing decision. In addition to calming fears, you may find employees with talents not previously revealed—because their current jobs don't require them. As for customers, explain the reasons for the service change and the positive results they can expect—and then keep close tabs on the competitive advantage your strategic business decision to outsource is creating. ■

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