

HR OUTSOURCING – ISSUES & IMPERATIVES

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Abstract: Human Resource Outsourcing (HRO) has finally come to stay. With that, few of the eye brows have raised with questions – what will be the future of HR? Is it doomed to fade away? OR will it emerge a winner all the way? Will Indian HR break new grounds and embrace outsourcing unconditionally? What is the magnetic attraction of outsourcing? What are the risks involved and what is the secret to success? Is this the beginning of a revolution, where HR transcends traditional boundaries and emerges as a powerful business function? Some of these and various other relevant issues concerning HR outsourcing (HRO) need to be deliberated and arrive at imperative organizational dimensions to reap the fruits of new paradigm of HR outsourcing that has come to stay. In a liberalized economy wherein change, competition and competence are the major drivers of business efficiency the need will be to optimize each link in its value chain. Rapid pace of technological development coupled with intense market competition are threatening organizations to maintain optimality of all their business processes only through their internal resources particularly when they have to continuously focus their internal resources towards core processes to accomplish their strategic intents and maintain the competitive edge in the market. This has led to the growth of the outsourcing paradigm by which an organization enters into a contract with an external agency [partnering organization] to operate and manage one or more of its business processes, which usually are the support processes in the value chain. This paper deals with various issues concerning HR outsourcing, contours and concerns of HRO, trends and insights into effective functioning of HRO and certain imperative organizational dimensions for making the concept successful in an organizational context.

Keywords: Outsourcing, Optimality, Contours, Value chain

1.0 Introduction:

Human Resource Outsourcing (HRO) has finally come to stay. With that, few of the eye brows have raised with questions – what will be the future of HR? Is it doomed to fade away? OR will it emerge a winner all the way? Will Indian HR break new grounds and embrace outsourcing unconditionally? What is the magnetic attraction of outsourcing? What are the risks involved and what is the secret to success? Is this the beginning of a revolution, where HR transcends traditional boundaries and emerges as a powerful business function?

Some of these and various other relevant issues concerning HR outsourcing (HRO) need to be deliberated and arrive at imperative organizational dimensions to reap the fruits of new paradigm of HR outsourcing that has come to stay.

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2.0 What is HR outsourcing?

Due to significant strategic business advantages that a business unit can fetch by assigning the management of some or all functions related to human resources needs to a third party provider who specializes in the management of human resources, companies have started outsourcing these functions to specialized third parties. HR outsourcing is typically viewed as a cost effective method of managing all OR a portion of the human resources related operations of a particular business, on payment of predetermined fees for their services. Those who provide outsourcing services are subcontracted, not employees of the company to which they provide their services.

While a large number of smaller businesses that experience rapid growth will consider HR outsourcing as a viable alternative to hiring internal staff to accomplish the tasks associated with the human resources needs of the business, bigger business units may consider HR outsourcing as a strategic tool to gain cost advantages as well as relief from the operation of routine transactions and instead effectively utilize the internal human resources for strategic intended purposes.

3.0 What drives HR outsourcing?

3.1 HR service delivery is a non-core business area for most organizations. Hewitt Associates surveys show that as much as 30-35% cost saving can be achieved by outsourcing HR service delivery

3.2 Companies are looking for ways to manage growth without adding infrastructure, head count and cost. As such it is a definite business sense to outsource non core HR service delivery transactions and gain cost advantage

3.3 Emerging technologies are drastically aiding such service deliveries and reach, thus fetching dramatic and radical improvements in operations at lesser costs.

3.4 Now-a-days the concept is for developing lean and clean organizations which will increase agility and speed in the market place. Thus the rise of the fast growth, broad based organizations has encouraged organizations has encouraged organization designers to find ways of staffing only the critical functions and evolving cost effective partnerships for others.

3.5 Companies are focusing on 'virtual' organizations-seamless technology based transactions.

3.6 The tightening talent market with rising wage costs will naturally force companies to place scarce resources in doing better things.

3.7 HR service delivery directly impacts employee productivity and having massive internal HR resources for providing such deliverables which are basically non-core activities for any organization does not sound a good business sense.

3.8 In the changing economic and business environment companies are compelled to keep the permanent head count at a low level.

3.9 Three most important drivers for HRO are (i) financial gains (ii) lesser administrative hassle (iii) focus on core areas

3.10 Converging technologies of telecommunications, information technology and media have redefined the way we do business, with electronic commerce and enterprise systems becoming a way of life. Correspondingly there has been a sharp increase in the need for qualified software professionals to manage various functions and HR function is not an exception. Hence managing all HR functions in-house may not make business sense when outsourcing provides a neat solution to several business problems.

4.0 The benefits of HR outsourcing:

The need for Human Resources function to be able to scale up and play the role of a strategic business partner is being fast recognized and appreciated by HR professionals. Thus they also started freeing themselves from the routine time-consuming transactional tasks and have started directing their focus to key strategic human capital issues. HR outsourcing has definitely come to their rescue here. By outsourcing all such HR processes which does not add significant value to the requisite strategic intents of the business, the HR functionaries are also deriving several other benefits such as:

- * The opportunity for HR to focus on strategic and core competencies
- * Sharing of risks and increase in mobility
- * Option to convert fixed cost to variable cost
- * HRO transfers various risks involved in compliance, financials, and technology, legislative and corporate restructuring issues to the vendor.
- * Companies need not invest capital to maintain and upgrade high quality, prohibitively expensive HR systems and infrastructure.
- * HRO ensures world class processes, competitive advantage and increased share holder value.

The benefits arising out of HR outsourcing can be classified as primary benefits (8) which afford major benefits providing strategic advantages and secondary benefits (12) which afford operational and cost advantages. They are depicted below in figure – 1

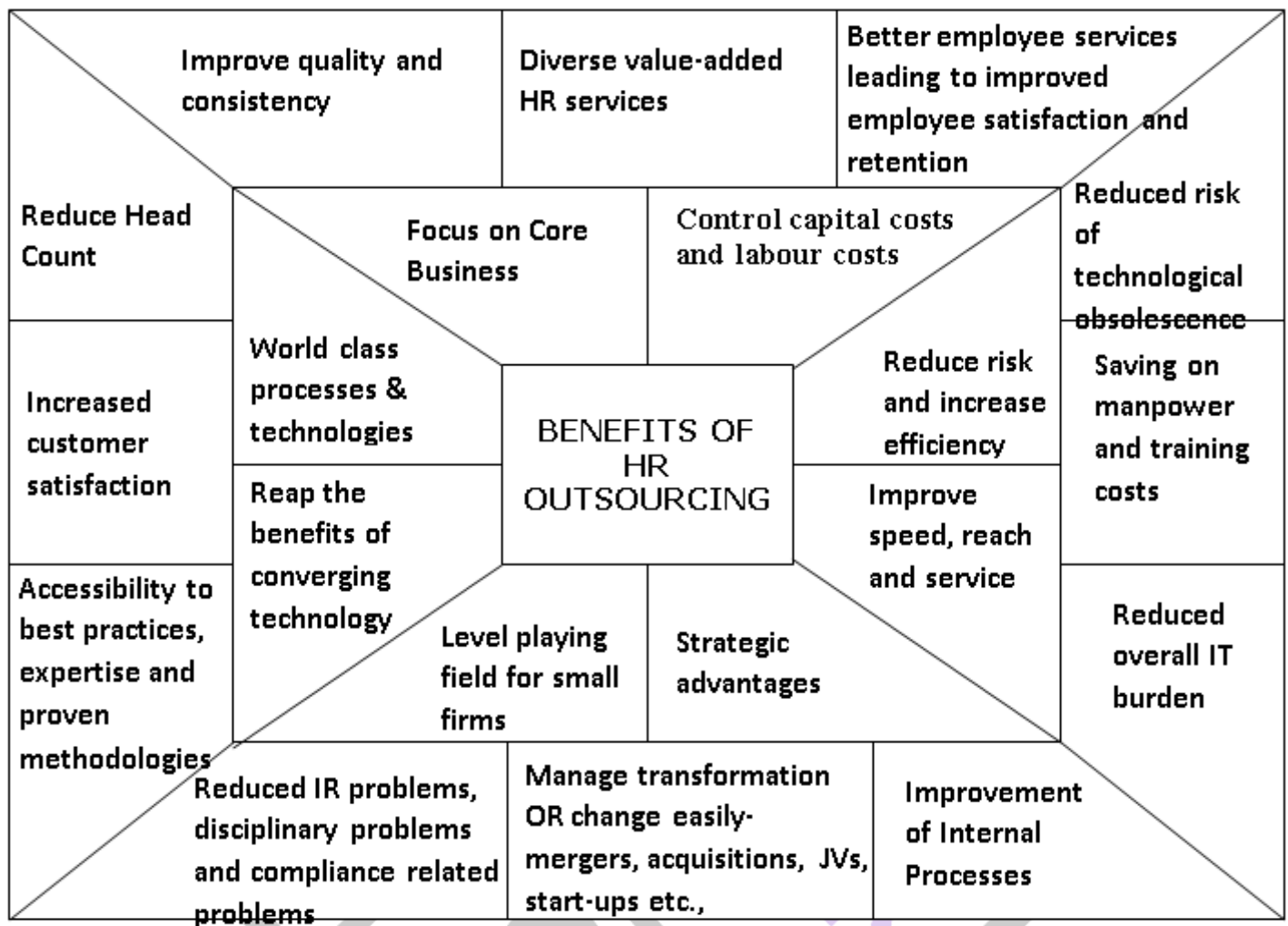


Figure - 1

5.0 HR outsourcing – Contours and Concerns ...!

5.1 HR outsourcing is becoming business strategy among

- Those with seasonal products and services
- Those seeking to restrict their overheads
- Those who are proactive and open to change
- Those who are thinking lean, acting smart and concentrating on core competencies
- Those who do not have full fledged HR department and thus the required competency and resources to deal HR matters

5.2 Typically, a larger corporate with several legal entities and locations, vast and varied employee clusters, decentralized non-harmonized processes and an army of HR looking after the entire operations would find outsourcing HR administrative functions of payroll and personnel benefits administration, beneficial on all these factors.

5.3 Third party outsourcing agencies can offer leading edge technologies, highly developed programmes and software to manage employee data along with specialized expertise, minus the accompanying cost of hiring and retaining the best HR professionals. This in fact is the specific strategic advantage that can be effectively utilized to leverage the talented internal HR resources with core strategic intents of the business to derive competitive edge in the market.

5.4 Interim staffing OR temps deployment is another major HR outsourcing product that can be effectively used:

- By businesses that have seasonal or time based shifts
- By businesses when flexibility of manpower deployment is required
- By businesses needing speedy adjustment
- By businesses operating fixed cost projects
- By businesses in all of their non-core areas of business
- By businesses operating in highly competitive environments calling for constant increments in quality

- g) In post downsizing period, when recruiting permanent staff may be awkward.
- h) To establish new benchmarks for skills and competencies in use
- i) To establish new norms for superior pay commensurate with performance
- j) During undertaking start-up operations
- k) Post mergers, acquisitions, JV's, collaborations, expansions, technology upgradations

5.5 A recent Forrester research study found that, on an average, HR managers spend nearly 80% of everyday administering employee benefits and answering routine questions. IDC (International Data Corporation) reports that 60% of the standard HR processes is administration, customer service accounts for 30% and strategic planning only 10%. With outsourcing, most of the administrative, labor intensive paper work can be taken care of, leaving staff with more time to concentrate on the company's core competencies.

5.6 With the increased acceptance that HRO is enjoying today, outsourced functions are fast moving beyond administrative and transactional duties. Online recruiting and online assessment tools and personality tests are gaining ground as accepted means of selecting the right human capital for organizations.

5.7 An HR outsourcing firm can save small to midsize companies money by allowing the business owners the time to concentrate on the daily operations and strategic goals of the core business as opposed to using that precious time to manage transactional and routine activities concerning human resources

5.8 Professional HR outsourcing firms are often intimately familiar with the most cost effective employee benefit programmes, varied experience of providing such services to different organizations, legal and other compliances and reducing risk associated with the performance of these functions.

5.9 Concerns:

5.9.1 HR staff may be hesitant to embrace HRO because they fear it will eliminate their role within the company. This issue needs to be addressed and intervened to educate them about the benefits of HRO that would outweigh some of the challenges in transitioning to outsourcing mode.

5.9.2 HRO entails making available all such important information about the human resources, company's culture, company information relating to staff, structure, system and strategies and hence speculations of loss of information that is sensitive could act as deterrent for HRO to be welcomed by the organizations

5.9.3 Most of the times the complexities involved in computing the cost-benefit equations and no clarity being there in understanding clearly the advantages may also act as deterrent for HRO.

5.9.4 Lack of psychological acceptance on the part of employees in general and HR staff in particular could pose problems of assimilating outsourcing with the companies operations and structure.

5.9.5 Ethics and quality of outsourcing vendors coupled with professionalism displayed by such vendors is another major variant of successful launching of HRO.

5.9.6 Outsourcing could limit the development of distinctive competencies and may create inefficiencies because contractors lack firm-specific knowledge and may engage in opportunistic behavior.

5.9.7 Outsourcing cannot be seen as a panacea for all the troubles of an organization. What works for one organization may not work the same way for another. Hence it is essential to make HR outsourcing through the processes of HRO, activities chosen for outsourcing, culture-fit required for successful implementation so as to make HRO compatible with the organization.

5.9.8 Several other concerns relating to outsourcing are:

- a. Security of critical data, employee privacy and of transactions
- b. Resistance from within the organization
- c. Lack of knowledge on vendor's end
- d. Lack of availability of professional vendors
- e. Issues with cultural mis-match
- f. Difficult relationships with vendors
- g. Regulatory and legal constraints
- h. Opportunism that could be displayed by vendors

5.9.9 Middle-aged people who often loose jobs due to downsizing or outsourcing of HR function are often put to mid-career crisis if not handled properly.

5.9.10 Trade unions too are directly affected by the concept of outsourcing as their membership as well as comradory suffers a dip every time jobs are axed.

6.0 The arena of HR outsourcing:

6.1 A survey by an HR association showed that 72% of Indian companies have outsourced atleast one HR activity and 50% of these are operational in nature. Traditionally Indian HR outsourcing market has been in the unorganized sector. But now with several professional multinational players like India Life, Hewitt, Exult, etc arriving on the Indian scene, it has added a new dimension to the complexion of the business. According to a survey by Gartner Inc., 89% of midsize companies outsource atleast one HR function. Corporate India does not lag behind too.

6.2 An illustrative, not a comprehensive list of HR activities that could be outsourced to derive strategic advantages are:

1. Overseeing organizational structure and staffing requirements
2. Recruiting, training and development
3. Personnel benefits administration – pay roll, leave and attendance monitoring, taxation etc,
4. Employee orientation programmes
5. Implementing a human resource information system (HRIS)
6. Create or update employee handbooks and policy manuals
7. Develop and implement a compensation program
8. Create or review a performance appraisal system and performance management system
9. House keeping
10. PF, Gratuity, ESI administration
11. Training for pre-hiring skills (Finishing school)
12. Superannuation benefits administration
13. Employee welfare schemes
14. Transportation, fleet management
15. Cafeteria
16. Security services
17. Safety services
18. Nursing assistance and basic health services
19. Educational services for employee's children
20. Estate administration
21. Relocation services for expatriates coming into the country or Indian nationals being relocated overseas
22. Disciplinary and legal services
23. ESOP administration
24. OD, CM, TQM initiatives
25. Regulatory and compliance services

7.0 HR outsourcing: Trends and Insights:

7.1 The National Association of Software and Services Companies [NAASCOM] which represents the country's information technology (IT) and IT-related firms, estimates that the Indian outsourcing sector will be a \$15 by industry by 2008, up by a staggering \$12bn

compared to current earnings of \$3bn. It also estimates that the banking and financial services sector in the US made savings of \$8bn in the last four years by outsourcing to India.

Due to the Indian talent, re-engineered systems, and world class delivery standards, the US companies enjoy about 50-70% savings in cost per transaction. Sizeable portion of this outsourcing business could be tagged on to HR outsourcing also.

7.2 HRO has grown more prudent and prevalent during the past 5 years, and the trend is continuing. Industry forecasts had projected HR and benefits outsourcing to generate about \$60bn in 2005. According to HR outsourcing trends – a survey conducted by the conference.

Board involving HR Vice-Presidents, CFO's, and CEO's from 165 companies – the two most commonly outsourced activities were transactional and administrative HR functions. Ranking below those processes were – employee communications, HRIS, assessment and recruitment.

7.3 According to an estimate by market research firm AMI (Access Markets International) U.S. companies spend \$17.6 by on HR outsourcing. As many as 400,000 small businesses outsourced HR functions in the preceding year, AMI estimates.

7.4 Survey highlights of Hewitt's research study: "HR Outsourcing: Trends and Insights" has very interesting revelations about HR outsourcing universally.

- * Out of 125 companies who responded to the survey, 121 companies were found to outsource atleast one HR function.
- * By 2008, study participants expect to expand HR outsourcing across the board, with significant increases in the following areas: leave management, learning and development, payroll, recruiting, health and welfare, defined benefit plans and global mobility
- * Organizations are driven to outsource HR activities for a variety of reasons. The most commonly cited reasons are: gaining access to outside expertise, improving service quality, a desire to focus on the core business and the opportunity to realize cost savings

At the same time, just over half of respondents indicated that there are barriers to outsourcing HR functions in their organizations: concerns about loosing control of key processes, employee reactions and building a business case are the most commonly cited barriers.

- * Overall, 89% of participants indicated that they are satisfied or very satisfied with their current HR outsourcing arrangement. A substantial majority of respondents (85%) felt that they realized expected benefits from HRO. They feel 'cost savings' was not the primary objective but more than 80% of the times cost savings have been achieved by HRO.
- * One-fifth of companies also reported of realizing unexpected outcomes from HRO which include:
 - a. A substantial increase in process efficiency in non-HR areas
 - b. Greater discipline in demand prioritization, cost control and planning
 - c. More cost savings than expected. As much as 30-35% cost savings reported.
 - d. Greater employee awareness of the outsourced benefit plan
 - e. Higher levels of employee savings in the outsourced plan

7.5 Success Rate of HRO:

However, the flip side of HRO also cannot be undermined. Dun and Brad street reports that 20-25% of all outsourcing relationships fails within 2 years and that 50% fail within 5 years. Nearly 70% of the companies responding to Dun and Brad street survey asserted that suppliers did not understand what they were supposed to do and that the 'cost' was too high and they provided poor service.

7.6 In general HRO brings 60% increase in productivity, 30% reduction in costs and eradicates labour union problems to a great extent.

8.0 Imperatives for HRO to be most effective to fetch business advantages:

8.1 Outsourcing will never lead to the complete elimination of the internal HR function. Instead HR will have to play a lead role in terms of supervising, implementing, and successfully carrying on the process of HRO. Internal HR will have to see the larger picture and has to constantly work towards employee retention especially at key levels, succession planning, fine tuning the available human resources, ensuring people-to-productivity ratio and such other strategic functions. HRO under any case cannot be a substitute for the HR department.

8.2 It is important to define vendor conduct, conduct regular reviews, and define parameters for quantitative measurements and matrices for success. HR department must involve itself in providing value additions according to changing business needs and process evaluations to analyze the observable benefits out of the outsourcing.

8.3 It is essential to determine and specify various HRO vendor qualifications very clearly at the time of vrending out and ensure that the vendor invariably possesses those qualities for the HRO to be effective.

- * Requisite domain skills
- * Expertise
- * Consultative selling
- * Project management
- * Technology skills
- * Process and industry expertise
- * Ethics and quality

8.4 HRO can be successful when outsourcing could be used to achieve an enterprise wide strategic impact. Extensive planning and intricate detailing of the outsourcing processes and partnership between the company and the vendor built and nurtured with open communication, flexibility and trust will only lead to successful implementation of outsourcing plans.

- 8.5 Companies need to transfer understanding of the business protocols and procedures to the vendor. Vendor needs to be trained on how business is actually done in the company.
- 8.6 Vendor needs to be clearly made known of the service expectations through evolving of norms and evaluating the service performance periodically for bringing about improvements through process updations and penalties, opting-out clause, if required.
- 8.7 Handling the transition period is very vital for the success of implementing HRO. Pilot projects and building trust, confidence and credibility through intervention by a select expert team could provide solution. Communication campaigns, training for managers and employees are required.
- 8.8 With outsourcing, there is a danger of physical connect between the company and employees breaking-up. Interventions should be in place for the relationship between and HR to graduate from a mere transaction level to an involvement level, where in they connect more interms of higher level issues related to potential assessments, career development, growth, succession planning, work-life balance etc
- 8.9 Vendor should be able to assimilate himself with the culture of the organization and meet the expectations of the internal customer. This requires proper interfacing between the client and the vendor and execution of full contract only after piloting and remedying for 'culture-shock' that could be inevitable in the process.
- 8.10 An outsourcing arrangement should be perceived as a partnership between the vendor and the HR department, but a close monitoring and periodical audit is required at each stage to ensure high quality service standards.
- 8.11 There is critical strategic HR issue of potential loss of expertise in certain areas, which may be difficult to recover – danger of “Hallowing – out” of the organization.
- 8.12 It is important to assess what the vulnerability of the vendor is to attrition of key people and the ability of the vendor to sustain in business. It is also important to understand the passion and commitment of the key people to the business and clients.
- 8.13 More number of companies believes in integrated design and delivery of outsourced HR functions through very few vendors. Organizations embracing an integrated approach indicate that they gain main advantages including:
- * More efficient delivery processes
 - * Greater consistency and a comprehensive perspective
 - * Easier communication and coordination between the company and the vendor.
 - * A vendor with greater knowledge of the company's needs goals, business strategy and culture.
 - * Fewer errors due to seamless data sharing
 - * A to Z ownership of and accountability for processes and content.
 - * Better cost savings and Better support for complex initiatives
- 8.14 Companies need to have more time for due diligence and reference checking of vendors. They need to be more diligent during the decision – making and contract negotiation process.
It is necessary to involve all stakeholders including end users, early in the outsourcing process and engaging them not only in planning but also in communication.
- 8.15 Some of the major aspects of HR outsourcing firms to be considered when evaluating a firm include:
- * The range of outsourcing services it offers
 - * The expertise it has in industry which is considering outsourcing its HR processes.
 - * Its general HR experience
 - * Its available resources
 - * The flexibility of its contracts
- 8.16 Before deciding to outsource there are several soul-searching questions that need to be answered:
- * Examine the corporate culture – is the organization comfortable with relinquishing some control to a trusted vendor for the overall good of the business?
 - * Evaluate current HR processes – determine the effectiveness of your processes and decide whether they can be handed over to a third-party to manage
 - * Performance measurements – ensure metrics are in place to measure the vendor's performance and determine whether they are improving workflow and processes.

- * Are you mature enough to utilize a strategic business partner or is a service provider good enough for you?
- * Are you cooperative enough to share information? Can you resist the basic human tendency to hoard information?
- * Are you ready to change the structure and system post-outsourcing so that it dovetails with the outsourcing company?

8.17 Some of the most important questions that you must ask your prospective service provider before outsourcing your work are:

- i. How reliable is the vendor?
- ii. Does the vendor provide quality products/services?
- iii. What is the life cycle cost of the products/services provided?
- iv. Will the vendor be able to meet delivery deadlines?
- v. How safe is my data?
- vi. What kind of risk am I taking on with this vendor?
- vii. What are the effects of the vendor's employee attrition on me?
- viii. Will the vendor be fair and transparent in his financial dealings with my organization?
- ix. Does the vendor comply with statutory laws and regulations?
- x. Does this vendor's culture match that of our organization?

Answers to all these questions need to be obtained before finally choosing an outsourcing partner to you.

8.18 Consulting unions and employees and other major stakeholders and taking them into confidence is a must for successful implementation of an HR outsourcing plan.

9.0 Conclusion:

The outsourcing institute finds, "outsourcing is rapidly becoming an accepted management tool for redefining and re-engineering the corporation. It challenges today's executives to rethink the traditional, vertically integrated firm in favour of a more flexible organization structured around core competencies and long-term, outside relationships". Experience now shows that the benefits of outsourcing outweigh some of the challenges. It is important to take the time and evaluate company's requirements and outsource the services that will allow the organization to focus on the core business competencies that will give the company the requisite competitive edge in the market.

HR outsourcing thus has come to stay and is revolutionising the very anatomy of the HR function to metamorphose from traditional transaction oriented, reutilized non-core function to highly intensive and dynamic strategy business partner in the modern businesses.

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