

# Accelerate Growth with an Employer Services Organization

# Table of Contents

Introduction.....3

Costs and Benefits of Human Resources.....4

Pursuing Strategic HR.....6

Conclusion.....10

Appendix A: Cost Savings through ESOs.....11

Appendix B: ESO/Strategic HR Opportunities and Obligations.....12

## Introduction

High-growth businesses constantly seek an edge. Anything that could help bring in a new client, deliver an innovative service, or streamline the organization becomes vitally important – offering a chance to widen margins, capture market share, or feed the top line. Internal efficiencies, especially, constitute a way to reduce operating costs and redeploy capital to initiatives that support rapid growth. Employer services organization (ESO) companies empower high-performing small and medium-sized businesses (SMBs) to improve human resources operations while reducing costs and enabling the company to focus on revenue-generating opportunities.

ESOs can assist companies using several service models, including Professional Employer Organizations (PEO), Administrative Service Organizations (ASO), and Human Resource Organizations (HRO) in one or more of the following areas:

- Payroll and tax administration
- Human resources
- Risk management
- Benefits plan design and administration
- Employee training and development

The PEO is a co-employment model where employment-related responsibilities and liabilities are shared between the service provider and the client company. The ASO model operates in a similar manner but without shared employer-related liabilities, and it tends to lend itself better to larger companies than the PEO service offering. Finally, the HRO model can be implemented in many forms ranging from payroll only to such high-touch services as full recruiting and on-boarding. HROs generally are designed for companies who have efficient HR infrastructures already but need help in some specialized areas. An emerging high growth company might find itself using each one of these service models at some point as it matures through its ever-changing dynamic lifecycle.

Unique to high performing SMBs is the struggle to support sales and service staff sufficiently while keeping overhead as low as possible. Every company wants to keep costs down, but high-performing companies rely on every invested dollar to create as much value as possible. Investing a bare minimum in internal operations seems attractive at first, but mistakes, slow responses, and lost employee productivity quickly demonstrate the importance of allocating sufficient resources to support functions. An investment in HR operations can bolster response times and increase the accuracy of transactions, enabling employees to focus on their core responsibilities, ultimately fueling company growth.

The implementation of an ESO program leads to improved HR performance and a residual advantage to the rest of the company. An ESO does not replace your HR department entirely. Instead, the ESO shifts the burden of transactional tasks out of the company HR department to an outside organization that uses economies of scale to fulfill the nuts and bolts of HR service fulfillment – e.g. exit interviews, HRIS adds/deletes, and payroll – allowing a much smaller HR staff within the company to contribute to company growth on a strategic level.

The impact is twofold. A reduction in HR operating costs enables capital to be reallocated to business units that fuel growth. The cost savings that results from using an ESO can be applied to additional marketing campaigns, new employees, or even incentive-based compensation programs – among other options (see Professional Employee Outsourcing Primer: A Cost Comparison to Traditional Human Resources Departments for a detailed examination of the cost savings available through ESOs). The streamlined internal HR staff can focus on strategic initiatives around structuring the organization for growth, maintaining staff strength levels, and identifying innovative ways to motivate the employee population. With an ESO, the HR department costs less, delivers transactions more efficiently, and positions the internal HR staff to support accelerated top line growth.

ESOs reduce the cost and internal footprint of HR in smaller businesses. As a result, the implementation of an ESO program frees resources for redeployment to growth initiatives, and it keeps the company focused specifically on growth. Even the internal HR team can focus on supporting growth opportunities, rather than struggling to keep pace with a mounting pile of transactional obligations.

## Costs and Benefits of Human Resources

HR does not – in fact, cannot – contribute to top-line growth (i.e. net sales). This is the most salient myth surrounding the HR function in the contemporary business world, and it is accepted at face value in the SMB community. High-growth SMBs realize that this myth is wholly inaccurate. While the HR department’s contribution to top-line growth is not direct, there is a clear connection between effective HR management and increases to company revenues – and as a result to the company’s high-performing behavior.

Traditionally, the strategic posture assumed by HR has been one of efficiency. HR leaders pursue streamlined operations and performance improvement initiatives in order to reduce error rates, improve response time, and lower the cost of serving the employee population. The HR Director tends to perceive success qualitatively in terms of employee satisfaction or task completion and quantitatively by either reduced operating expenses or (more frequently) by employees served per HR staff member, and success is pursued through efficiency initiatives that limit expenditure. Pursuing strategic growth usually does not reach the HR Director’s agenda.

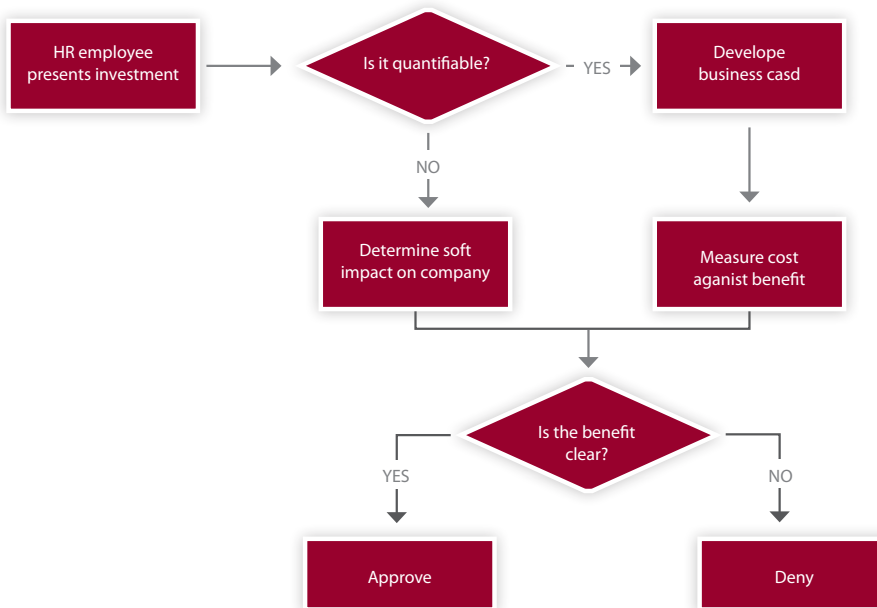
The HR department, consequently, strives to do more with less, balancing qualitative assessments of service providers with a quantitative analysis of the costs of doing so. Fundamentally, the challenge is to reduce the cost of HR without degrading service levels. In SMBs, this challenge is particularly noticeable. As expenditures must be allowed prudently, an investment in HR efficiency deprives the company of a growth opportunity.

The SMB, therefore, has to decide:

- Whether a new recruiting software system delivers more value than an additional marketing campaign
- How to allocate the annual compensation budget to reward support professionals sufficiently but not at the expense of revenue producers or client-facing professionals
- The effect of HR cost-cutting on employee-related service levels
- The value of developing HR professionals through formal, and at times expensive, employee development programs (e.g. seminars and conferences)

Company executives and HR leaders tend to evaluate such HR investment decisions first in terms of cost and next in terms of efficiency (which itself becomes evaluated by cost impact). Investments in HR consequently result from the assessment that an internal operational advantage could result from a particular improvement opportunity. The possibility of a growth-oriented impact typically does not receive any attention because of the persistent myth that HR is capable of rendering such a contribution. The company focuses on improving the areas that generate revenue rather than internal support functions.

### Exhibit 1 – The HR Investment Process



Cases where the benefit of a HR investment are quantifiable include:

- New systems (e.g. payroll, ERP, recruiting)
- Increased headcount
- Benefits plans

Qualitative investments tend to include:

- Training and conferences
- Disproportionate or off-cycle compensation increases
- Consulting and coaching services

As SMBs tend to run leaner HR operations than their larger counterparts, the investment decision is even more difficult. An investment in HR almost certainly entails deferring – or even sacrificing – another opportunity. Company executives consequently have to analyze the HR investment directly against other opportunities, instead of considering the HR business case on its own merits. For high-growth SMBs, this almost certainly leads to a minimal planned investment in HR, with HR initiatives delayed until resolution becomes unavoidable, often as an unplanned expense.

Unplanned expenses often can result from waiting too long to address aging systems, obsolete processes, and open positions that have remained unfilled for long periods of time. As HR tends to receive a lower priority, other business areas are addressed first. HR problems receive attention only when the need becomes urgent. When the problem finally is addressed, resolution becomes much more expensive, which has the effect of diverting even more funds from growth initiatives. This is why high-growth SMBs include support functions such as HR in strategic investment plans. The strategic benefits offered by support functions are supplemented by the lower cost of forward-looking investments in current HR capabilities.

High-growth SMBs evaluate expenditures based on their potential contribution to growth, i.e. the likelihood that an investment will lead to new business opportunities. Increasing the sales force size, developing new products or services, and ad buys thus trump pursuing operational or organizational enhancements to the HR department, where the benefit is measured at the bottom line instead of the top line.

Through this analysis process, SMBs overlook the fact that HR can contribute indirectly to top line revenue growth. Efficient HR operations facilitate company growth, and HR involvement in strategic planning is vital to capturing market share and winning new business in the marketplace. To realize this advantage requires a fundamental shift in thinking from tactical HR to strategic HR. For high-growth SMBs, engaging an ESO answers a number of questions around resource allocation, the positioning of HR to play a strategic role in the company, and how to off-load costly and low-value transactional processes to keep the organization lean and focused on the marketplace. An ESO allows even smaller businesses to take advantage of economies of scale for tactical activities at a reduced cost. The result is more efficient transactions and elevated employee service without the accompanying price tag. ESOs are both more efficient and cost-effective.

## Pursuing Strategic HR

Strategic HR looks beyond internal efficiency to activities that clearly, even if indirectly, facilitate company top line growth. As opposed to the core transactions for which most people know HR – e.g. adds/deletes, new employee orientations, exit interviews, and compensation and benefits – strategic HR examines opportunities that help the company win new business and deliver products or services. Strategic HR ensures that sales and customer-facing staff members are motivated and properly supported.

Unlike tactical activities, strategic efforts reshape the face of the business, affecting a fundamental change that enhances how the company operates either internally or in the market. Strategic HR, consequently, must yield an advantage that shifts substantially the way the company does business. Thinking conventionally, it is easy to dismiss strategic HR as impossible – or at least far-fetched. In reality, there are a number of ways that HR can make a strategic contribution to any enterprise. Examples of the initiatives that contribute to strategic

HR includes:

Strength Management – ensuring that business units remain fully staffed and that open positions are filled as quickly as possible

Organizational Design – planning a structure for the company that extracts the full value from each employee, conserves resources, and enables a swift and proactive market posture

Career Pathing – structuring the company for upward mobility and career growth to improve morale and improve employee retention

Competency Modeling – developing a framework to ensure that employees are properly matched to their positions and have the hard and soft skills required for success

These four examples indicate high-value HR activities that can reshape the business in a manner that delivers either a bottom line advantage or a contribution to top line revenue growth.

In general, the purpose of strategic HR is to position the company for growth. Unable to seek a direct revenue advantage, the role of the HR department in a high-growth SMB is to ensure that sales and service teams are poised to capitalize on growth opportunities. HR may not drive growth, but targeted HR actions can entail the difference between success in the market and a missed opportunity.

By pursuing competency models, developing job descriptions, and conducting compensation analyses, and other strategic HR initiatives, the HR department moves from the tactical to the strategic. In a high-performing SMB, this is where HR belongs. Tactical matters must be addressed, but not at the expense of HR's strategic obligations. Engaging an ESO allows high-performing SMBs to attain a balance between the strategic and tactical more easily. The ESO assumes responsibility for specific tactical roles, allowing the internal team to position HR strategically in the organization to facilitate continued high growth trends.

ESOs offer predefined services and HR business processes to their clients' employees in place of internal resources and processes, demonstrating immediate improvements through procedural rigor, predictable results to employee questions and transaction requests, and a subsequent efficiency that increases employee productivity and enhances the reputation of the HR department across the company. The ESO does the "grunt work" of HR, and the streamlined internal team focuses on strategic opportunities.

ESOs deliver a variety of HR services – either in part or in total – using economies of scale to serve smaller businesses for a fraction of the cost of fully in-sourced HR with an improvement in service levels. ESOs can handle payroll, benefits administration, and even address more people-intensive disciplines such as recruiting and candidate management, employee termination, and various forms of compliance. The ESO approach even to people-intensive activities is system-driven, applying economies of scale to the softer aspects of HR while containing costs and making the process more efficient.

ESOs can power the transactional aspects of HR or be used to provide employee-facing services through a systematic approach to HR. The flexibility of ESOs and their service offerings allows smaller companies to determine the scope of the ESO relationship and to change that scope over time as the needs of the company evolve.

Because of the flexible relationships enabled by ESOs that operate in the SMB space, most ESOs offer more sophisticated benefits packages than SMBs can implement on their own, for example, because they do not have the administrative burden of designing, implementing, and managing the programs themselves. Increased efficiency results, along with greater employee satisfaction because of more competitive benefits and compensation packages. ESOs increase efficiency, deliver benefits services, and offer more accurate services to support the employee population and improve the competitive positioning of the business.

Outsourcing entails the delivery of services to a company with an outside company rather than an internal staff. For a fee, ESOs handle traditional HR services on behalf of their client companies, using pooled resources while not compromising service levels or confidentiality. The ESO delivers these services through employee web portals, phone hotlines, and other interactive tools, bringing to bear the collective experience of serving a large portfolio of similar companies. HR is HR; the services are the same, though less expensive, scalable as the client's business grows, and do not require maintaining large internal headcount levels.

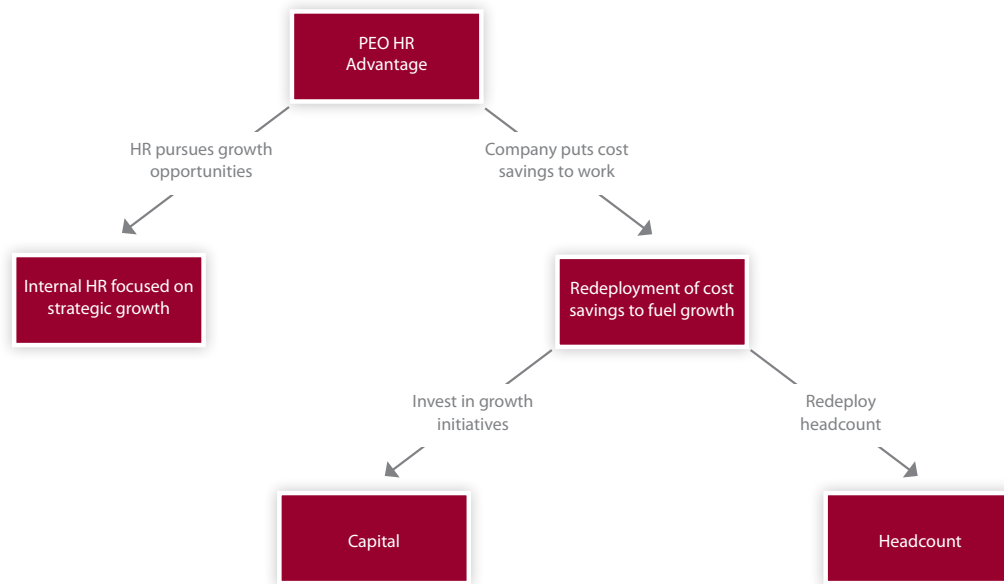
SMBs that use ESOs draw an implicit distinction between the strategic and the tactical. Tactical obligations are the domain of the ESO, which brings economies of scale to reduce response time to employee requests – and at a lower cost. The ESO ensures that HRIS records remain current and that payroll is run on time. Also, the ESO manages most compliance matters, again at a lower cost because the infrastructure supports a larger pool of companies rather than just one.

While the ESO completes the rote aspects of HR, the internal team improves the organization and enhances product or service delivery, which contributes to company revenue growth and demonstrates how HR can participate in the strong growth of high-performing SMBs. HR becomes a key growth driver rather than a mere cost center to be contained aggressively. The result is clear. ESOs turn HR into a strategically significant business unit by off-loading the tactical requirements of the department to an external entity whose purpose is to complete HR transactions quickly, accurately, and at a low cost.

High-growth SMBs can fuel growth by engaging an ESO to handle HR tasks that do not generate revenue-oriented advantages for the company. The advantages of an ESO extend beyond the strategic focus of the internal HR staff members. The cost savings that result from using a ESO also can fuel growth initiatives outside HR.



## Exhibit 2 – Deriving a Growth Benefit from ESO Cost Savings



Through the use of an ESO to handle tactical HR matters, cost savings come in the form of reduced financial expenditures and the ability to reallocate headcount to other business units that do contribute directly to financial growth. Financial resources can support marketing programs, new product development, and other capital-intensive initiatives that drive both near-term and long-term growth. Cash is the oil that fuels the company growth engine, and newly available funds from the ESO cost savings easily can find their way into the budgets of client-facing business units.

The redeployment of headcount is a bit more complex but is nonetheless attainable. Simply reassigning HR employees to other business units is not feasible. Their skills do not necessarily align with those of other areas of the company. But, the use of an ESO would seem to render transaction-oriented HR employees obsolete. At this point, growth-hungry SMBs face a decision. The company either can reduce the size of the HR department and apply the addition accost savings to other areas of the business or retain the HR staff members and mature their roles from tactical to strategic.

Applying existing HR employees to strategic initiatives constitutes an important investment in HR, as the resources applied to strategic HR are multiplied. This approach can succeed as long as the savings is treated like an investment rather than a continuation of pre-ESO operating models.

ESOs do not yield strategic HR. Instead, implementing an ESO program offers an opportunity. With transactional obligations outsourced, a streamlined HR department is free to focus on strategy and overall company growth, but HR leadership does need to develop and execute the strategic HR agenda. ESOs make resources available. The company then has to apply those newly available resources judiciously.

## Conclusion

HR does not have to be a cost center that drains resources from revenue-producing business units. Instead, HR can contribute to company growth; strategic HR enables a company to multiply the value of its HR department considerably, turning it into a contributor to rapid and consistent growth. This approach to HR requires a fundamental shift in thinking among the company's HR employees. Currently, HR is treated as a transactional operation which is encouraged to be cheap, fast, and accurate. The goal is to turn HR into a competitive advantage for the company.

High-growth SMBs continually seek an advantage in the market. Strategic HR constitutes a growth opportunity that often goes unexploited. The first step in turning HR into a strategic advantage is to engage an ESO. With an ESO, the factors that render HR transactional are outsourced to an environment that is designed for transactional efficiency. With the transactions covered by the ESO, the company is free to focus on strategic growth initiatives. Outsourcing makes capital available for investment in other areas of the business that lead directly to financial returns.

The key to using an ESO to drive company growth is to capitalize on the potential that results from implementing the ESO model. The company can streamline its HR operation and realize a cost savings. High-performing companies instinctively know to plan for the use of these resources to drive growth. An ESO solves a tactical problem. High-growth SMBs use this tactical solution as a platform for strategic growth. ESOs reduce costs and deliver opportunity. SMBs that recognize the opportunity can generate substantial returns simply through the reduction of internal complexity. With an ESO, HR becomes strategic.

## Appendix A: Cost Savings through ESOs

### Assumptions:

- Two hundred employees
- Three HR professionals<sup>1</sup>
- Twenty terminations
- Twenty new hires
- One litigation event

Number of Instances	Cost Description	Total Cost	Comments
3	HR professionals	\$180,000	2 HR Generalists, 1 HR Manager
1	Benefits administration	\$40,000	Differential paid without using a PEO
20	Recruiting/new hire expenses	\$240,000	Assumes no headcount growth, strictly replacement of existing employees
20	Termination	\$90,000	See above item
1	Litigation event	\$150,000	Reflects potential litigation costs, including settlement or severance to avoid litigation
10	Employee lost productivity	\$22,500	Ten hours per employee for ten employees
<b>Estimated Total Annual Cost</b>			<b>\$723,500</b>

1. Time to Go East? An Outlook for IT and Business Process Offshoring to Eastern Europe. McKinsey & Co., June 2006
2. Salary.com
3. Schiff, Jennifer. "Outsourcing Human Resources Reaps Benefits for Small Businesses". SmallBusinessComputing.com. April 6, 2006.  
<http://www.smallbusinesscomputing.com/biztools/article.php/3596341>
4. Recruiting costs are based on an average salary of \$60,000 per year and recruiting costs of 30% of the base salary.
5. Termination costs are based on an average salary of \$60,000 per year and termination costs amounting to 15% of the base salary.

## Appendix B: ESO/Strategic HR Opportunities and Obligations

Opportunities	Obligations
<p>ESOs enable a company to focus resources on growth activities</p> <p>HR shifts its focus from tactical transactions to strategic initiatives</p> <p>Error rates are reduced, and response times shrink</p> <p>The employee population supported by HR spends less time pursuing resolutions to HR-related issues</p> <p>Total cost of HR declines</p> <p>Newly available resources facilitate market share capture and revenue growth through strategic investment</p> <p>Strategic HR can lead to a more nimble and proactive organizational structure</p>	<p>Company has to plan for the use of resources; answers do not come automatically</p> <p>Changes to the staffing model may be necessary</p> <p>An internal investment may be required to get started</p> <p>After engaging the ESO, the company has to plan the use of resources to facilitate growth</p>

## About Odyssey OneSource

Odyssey OneSource understands business owners do not go into business to deal with the hassles of becoming an employer. As a pioneer of the professional employer industry, Odyssey OneSource allows business owners to focus more on the growth and profitability of their businesses and less on necessary administrative and HR functions. Providing outsourced services in human resources, risk management, payroll and tax administration, employee benefits and training & development, Odyssey strives to meet the unique needs of every client through its personalized approach and commitment to the best service in the industry.

To learn more, visit [www.odysseyonesource.com](http://www.odysseyonesource.com) or call 888.680.8800.

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