

Which is Better: Outsourcing or Shared Services?



In or out?

People have been arguing for years about the relative merits of outsourcing versus shared services. Yet the debate today is more relevant than ever. In some cases, organizations are unhappy with their previous decisions and are looking for a new approach. But more often than not, decision-makers are simply revisiting the subject in light of changing business conditions, such as new business strategies, new leadership, a major event such as a merger or acquisition, or maturing business practices.

Given current and future trends in shared services and outsourcing, which approach makes more sense? Is it better to outsource activities such as Finance, HR and IT to an outside vendor? Consolidate them to an in-house shared services center? Or perhaps combine the two approaches?

| | Point | Counterpoint |
|--|---|---|
| Outsource to a third party. <i>Contract with an outside vendor that specializes in the work you need done.</i> | <p>Outsourcing typically produces greater cost savings. Superior systems, processes, technologies and economies of scale – as well as easier access to offshore labor – often enable an outside vendor to do the work more efficiently. In many cases, outsourcing also delivers better quality by capitalizing on a vendor’s specialized knowledge, experience and talent.</p> | <p>Outsourcing vendors are not the only organizations with access to world-class systems, processes, technologies and talent. Organizations with sufficient capabilities and scale may be able to save money – and achieve better quality – by keeping services in house. Also, the cost of transitioning to an outsourced model can be significant and must be factored into the decision.</p> |
| | <p>Outsourcing tends to be implemented faster. It is in the vendor’s best interest to implement the services and solutions as quickly as possible. Also, less time is wasted on internal politics and inertia.</p> | <p>Although vendor self-interest can be a useful tool, it can also be a battering ram that produces the wrong results. Make sure the vendor’s actions align with your organization’s objectives. It might make sense to optimize your processes and systems before the transition, even if it takes a little longer.</p> |

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| | Outsourcing helps avoid future investments such as costly system upgrades. | Although the outsourcing vendor will be responsible for future upgrades, it is likely to focus on improvements within its own four walls. This can limit the ability to improve the end-to-end process, which is typically where the greatest value is found. |
| | Outsourcing provides greater flexibility by turning fixed costs into variable costs. | That's true from a cost perspective. But from a strategic perspective, locking yourself into an outsourcing contract may actually reduce your options and flexibility. |
| <p>Consolidate to a shared services center.</p> <p><i>Centralize the work, but keep it in house.</i></p> | A shared services approach gives you more control over processes and outcomes, which reduces risk. This is especially important for key activities that are strategic to the business or bound by strict compliance requirements. | Although it can be scary to relinquish control over critical activities, the reality is that leading vendors often have world-class processes and controls that present even less risk than your own. Taking advantage of such capabilities can help you achieve your strategic objectives. |
| | Your business requirements are unique – and so are the systems and processes needed to support them. They are competitive differentiators and should be kept in house. | This is one of the most common arguments in favor of shared services. It is also one of the most compelling – but only in the rare cases when it's true. More often than not, organizations' requirements and capabilities are not as unusual as they think. Outsourcing commodity activities gives you more time to focus on activities that are truly competitive differentiators. |
| | Shared services are more responsive to business needs because they are part of the same enterprise and have a closer relationship with the business units. | Closeness sometimes leads to complacency. Outsourcing vendors have the advantage of starting fresh. They can use the contract as a catalyst to drive work forward, instead of getting caught up in internal politics that might otherwise slow things down. |
| | With shared services, you don't have to share your strategies and other proprietary information with an outside party. | Outsourcing relationships can be just as strong and trustworthy as internal relationships. Also, well designed outsourcing contracts provide very rigorous procedures for handling and protecting sensitive information. |



My take

Peter Lowes, Principal, Deloitte Consulting LLP

The issue of “outsourcing versus shared services” is a perennial debate, and the right answer requires an objective look at the unique requirements of each situation. Unfortunately, decisions often are dominated by a few strong personal opinions, and by past experiences that are not relevant to the situation at hand.

In my view, outsourcing tends to make the most sense when an organization is looking for fundamental change, wants to move quickly, and views cost reduction as a top priority. The organization acknowledges the vendor’s superior systems, processes, talent, and scale economies – and wants to take advantage of them.

A shared services approach tends to make the most sense when control is a top priority, and when the activities in question are unique to the organization – and a competitive differentiator. However, success hinges on having adequate systems, processes, talent, and scale. If these are not on par with what an outsourcing vendor offers, it is hard for shared services to be competitive.

Our experience indicates that change initiatives driven by the business units often lean toward outsourcing because the focus is on bottom-line results, rather than on preserving the status quo. Conversely, change initiatives driven by the targeted functions themselves are more likely to adopt a shared services model, which is more of an incremental change.

Offshoring is sometimes thrown into the mix, further clouding the issue. It is important to understand that offshore labor is a viable cost-saving option both for outsourcing and shared services. That said, organizations with a strong interest in using offshore labor often favor outsourcing because it saves them the trouble of establishing and managing their own offshore operations. Outsourcing can also help an organization dodge criticism from employees, customers, the media, and the government that it is shipping jobs overseas. While that may in fact be happening, an organization can reasonably claim the decision is out of its hands.

Choosing between outsourcing and shared services does not have to be an either/or decision. Many organizations are best served by a combination of outsourcing and shared services – even within a single business function. Also, many activities can be managed effectively either way. Ultimately, success is not just determined by the approach you choose, but how well you execute it.

A view from Strategy and Operations

Susan Hogan, Principal, Deloitte Consulting LLP

Some organizations make the mistake of viewing outsourcing as the holy grail. The reality is that a shared services approach often makes good sense – as a steppingstone toward outsourcing, or as a long-term solution. Shared services is most viable as a long-term solution for organizations that have the scale and desire to optimize the processes themselves, and for processes where maintaining control is crucial. Examples might include processes such as financial reporting that are critical to regulatory compliance, or processes such as receivables that are key customer touch points.

Another subtle but important advantage of a shared services approach is that it gives you an opportunity to continuously improve your processes, instead of surrendering the benefits from such improvements over to a vendor. Organizations that opt for outsourcing should try to structure the contract so they share in the returns from any future improvements the vendor might make.

Similarly, if an outsourcing vendor will be running the operation with your existing processes and systems – rather than its own – it might make sense to invest in process optimization prior to outsourcing the work. This will enable you to negotiate a better price with the vendor, and help ensure a smoother transition. If you outsource a mess, it’s still a mess.

Bringing the debate to HR

Erica Volini, Principal, Deloitte Consulting LLP

In HR, the debate over outsourcing and shared services has been raging for well over a decade. Because HR Transformation initiatives affect every employee across the organization, they tend to be politically charged and draw interest from stakeholders throughout the organization – from business units to supporting functions such as Finance and IT. In order to cut through the noise, it often helps to start with a few key questions:

- What level of transformation / change that the HR function is looking to drive?
- Where is the driver for change stemming from – the HR function itself or a business mandate?
- Is driving cost out of the HR function a top priority for the organization?
- What is the organization’s culture and how does that align with an outsourcing approach?

Thinking about these questions can help you understand where your organization belongs on the HR service delivery spectrum. And while this debate can easily boil down to a choice between reducing cost vs. driving value, risk aversion vs. risk taking, and strategic function vs. transactional processor, it is the range of options within those choices that typically drives the final direction for the HR function.

Regardless of your decision, you will likely find it is just the beginning of the journey, not the end. Outsourcing and shared services both require a wide range of activities to capture the full value of the underlying HR Transformation effort. Everything from process redesign and technology integration to organizational restructuring, skills assessments and people transitions must be considered.

In fact, because they are rooted in many of the same concepts and activities, the line between outsourcing and shared services tends to blur over time. That’s just fine. At the end of the day, while the initial decision is an important one, it is the execution of that decision and the commitment of key stakeholders to the success of the transformation effort that will determine the ultimate success.

For more information, please visit: www.deloitte.com/us/debates/sharedservicesoutsourcing.

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