

# HR Insights

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## Pros and Cons of Outsourcing HR Functions for Small Businesses

Small businesses often have fewer resources than larger ones, potentially making it more efficient to outsource certain functions rather than keep them in-house. Certain functions of an organization's HR operations are common options for outsourcing. According to a study by staffing agency Kelly Services, 36% of all employers outsource part or all of their HR responsibilities, with the most outsourced functions being payroll (56%), recruitment (49%) and benefits (40%). This article outlines options for outsourcing and highlights the benefits and drawbacks of outsourcing HR functions so small businesses can consider whether this strategy is right for them.

### Outsourcing Options

Small businesses may choose to outsource functions for various reasons; for example, organizations may not have enough resources to hire personnel, or they may want to increase efficiency and focus time and energy on other matters by delegating HR tasks. Whatever the reason for outsourcing, there are different ways employers can go about implementing this strategy.

One outsourcing option is to hire a professional employer organization, which provides comprehensive HR services. Alternatively, there is HR outsourcing (HRO), where individual tasks can be outsourced to third-party providers. With HRO, rather than delegating all HR tasks to an outside party, only one or a few functions, like payroll processing, will be outsourced. Further, employers may also choose to leverage technology vendors when outsourcing. Many technology vendors now offer services such as Form I-9 compliance software, time and attendance tracking.

Ultimately, a small business's decision on whether to outsource will be specific to their individual needs. It is important for employers to consider whether to outsource all or some of their organization's HR functions because the

type of outsourcing they engage in could lead to a different outcome for their business.

### Benefits of Outsourcing

There is a range of advantages to outsourcing some or all of a small business's HR tasks. Employers may realize the following benefits:

- **Money savings**—HR costs can add up quickly, so outsourcing may be more cost-effective for some employers. Outsourcing can be especially useful for time-consuming, repetitive tasks such as payroll processing. According to a 2023 Priorities for Business Leaders survey by Paychex, an HR services company, HR administration can cost an organization roughly \$234,000 each year for employers with five to 500 employees. For businesses where that monthly expense is not feasible, outsourcing could effectively decrease costs if done strategically.

**Reduction in errors**—Small businesses may find that owners or HR professionals wear a number of different hats, which can create challenges when it comes to specializing in specific HR functions. Without a proper team and resources, it can be rather simple to make HR-related errors. Hiring outsourced services to deal with some or all of a company's HR needs can help reduce the risk of compliance-related errors and potential litigation because the professionals at HR services companies specialize in what to look for and how to address it.

- **Increase in productivity**—When a small business without designated HR personnel outsources certain HR tasks, it allows its employees to focus their efforts on other tasks and increase productivity. In fact, Paychex reported that nearly 7 in 10 small business leaders spend one week per month on HR tasks. By outsourcing the more time-consuming tasks, the time gained back can be focused on other matters that help improve a business's bottom line. Further, outsourcing HR functions can help small businesses develop initial HR-related strategies and tools and strengthen weak areas, which can help them scale efficiently and become more productive in the long run.
- **Compliance enhancement**—Especially when it comes to smaller businesses, it may not be feasible to have dedicated in-house HR professionals. Yet, that doesn't make compliance any less of a priority. By being able to outsource certain areas where employers don't have in-house expertise, such as legal or accounting, small businesses can increase their compliance efforts and mitigate potential risks.
- **Reduction in availability**—Outsourcing HR responsibilities can also mean that there isn't an internal HR professional on-site or, if there is, they may not have access to all of the information that the outsourced HR companies do. This can make it difficult for employees to contact HR as frequently as they may like or need.
- **Forfeiture of in-house expertise**—Delegating tasks to professionals outside the organization can cause a business to risk losing that area of knowledge altogether. When an employer freely outsources all HR-related tasks, they may no longer pay attention to them, which can effectively separate them from a portion of their business. If employers outsource too much of their HR operations or simply no longer focus on tasks they choose to outsource, the resulting lack of in-house knowledge can create disconnects between the outsourced HR professionals and the organization. It can also lead to increased confusion if employers are no longer providing the requisite attention to the outsourced tasks.

Looking at these advantages of outsourcing, it's evident that small businesses can benefit from seeking assistance from professional HR services.

### Drawbacks of Outsourcing

While many small businesses may benefit from HR outsourcing, the drawbacks may not make it worthwhile for some. These disadvantages should be considered when deciding whether to outsource HR-related tasks:

- **Lack of familiarity**—Having people outside of an organization handle the personal matters that are present in many components of HR—such as each employee's personal identifiable information or their compensation and benefits package information—runs the risk of a depersonalized experience for employees. While experts in their fields, external HR professionals are less likely to personally know the individuals they are helping, and they are likely unfamiliar with the company culture. This can lead to employees feeling like there is a disconnect between them and the people assigned to handle their information.

Weighing the drawbacks of outsourcing HR tasks is important for a small business before they make any decisions. Such disadvantages can help employers consider the factors that affect their HR outsourcing decisions.

### Summary

While saving money or increased compliance could make outsourcing HR functions the right decision for some small businesses, factors such as the forfeiture of in-house experts and decreased availability may keep others from outsourcing. Employers should consider all benefits and drawbacks before choosing to outsource any of their small businesses' HR functions.

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