



Benefits and Drawbacks of Outsourced Accounting

For at least the past decade, “outsourcing” certain corporate functions to a third party has been a hot topic in the business community. But whether a company is in the early stages of development or well established, the CEO should certainly consider the value of contracting out the accounting responsibilities to a firm that specializes in providing such services.

This short article summarizes the primary arguments that are most often cited by both champions and opponents of the issue.

Benefits -

- **Cost** – The potential for cost savings is the benefit most often cited as the decision driver for contracting out the accounting function. There are significant savings from reduced employee compensation; in addition, administrative costs related to employee benefits, payroll and unemployment taxes, staff training, recruitment, office space and IT equipment and software are also reduced. While the accounting service provider is in business to make money, economies of scale and efficiency can reduce the provider's per-transaction cost compared with that of a typical small business.
- **Maintain business focus** – Contracting the accounting function to a third party frees company management to focus on its core business. This is especially important when a company is in the early stages of development and the company founders are focused on developing products and establishing stable and growing revenue streams. Financial management is a valuable function that provides the critical information necessary to manage the company, but with time constraints, management needs to concentrate on long term return. Moreover, trying to play catch-up when record keeping falls behind is a difficult, time-consuming and costly process for any size firm.
- **Latest technology** – Most firms that provide specialized service are driven by competitive pressure to use and maintain the latest technology in order to provide the greatest service at the least possible cost. The hardware, software and associated technologies that these firms use may be expensive and out of reach of small- to medium-sized companies. Staying on top of trends in the technologies related to accounting systems and operations is time-consuming and an unnecessary chore for small company management.

- **Expertise and focus** – Outside accounting service providers are in the business of fulfilling a specialized function. It is what they do – and they will be staffed with appropriately trained and knowledgeable experts who know best how to perform the work. Since the service provider is focused solely on accounting, staff is isolated from the distracting rhythms of most office environments. Moreover, the service provider’s processes and procedures usually are standardized to maximize efficiency and minimize error. Internal controls related to segregation of duties, proper authorization and review generally surpass those of the typical small company.



Drawbacks -

- **Loss of control** – Any time a company contracts out a business function, whether accounting, HR, or IT, management loses some level of control. Service level agreements between customer and provider are typically put in place to define the performance responsibilities and expectations of both sides, but they are not and cannot be a substitute for direct management control. Even with the best of intentions, there will be times when information is needed and not provided, or a relationship with a supplier or customer may be ruffled.
- **Security** – Security of the service provider’s IT system and its potential vulnerability to hackers may be a concern. Computer crime is rising and with the global nature of the Internet, hack attacks may originate from anywhere on the planet. A service provider will likely have financial information related to several companies and is therefore a preferred target of white collar crime than a stand-alone and perhaps relatively unknown company. While it is true that a service provider will of necessity have robust IT security, the fact that hackers are able to penetrate banks, government systems and military databases is argument enough to warrant concern.

- **Confidentiality and privacy** – These issues are close cousins. Detractors argue that whenever information of a confidential and private nature is shared with outside parties, the potential for abuse is increased. Regardless of the confidentiality agreement between client and provider, once information is handed off to a third party anything could happen. Information related to the profitability of a product or customer is valuable to the originating company but is even more valuable to its competitors.
- **Potential negative publicity** – In a contracting economy where job insecurity is on the rise, the word “outsourcing” may carry an unintended negative message. This is more of an issue where a company contracts out an existing function at the cost of staff jobs – but any use of the word may damage a company's image when it outsources its core functions. On the other hand, outsourcing of support functions has been gaining acceptability.

In summary, there are both real benefits and real drawbacks to contracting out the accounting function. Each business owner should carefully weigh the arguments in determining whether such an arrangement best meets the needs of the growing company.