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## Strategy

## Are You In or Out with HR?

By: Linda C. Ray

Before he even served his first sandwich, Bill Duke signed a contract with an outside human resource organization to handle all his personnel issues. And after one successful year as a single-store franchise owner, Duke is pleased with his decision.

"It is one less headache for me," Duke says. "I can concentrate on running the restaurant and not worry about payroll and benefits and compliance and all that." Duke, who utilizes the services of AlphaStaff Group Inc., as his human resource outsourcing (HRO) firm, says he will stay with AlphaStaff as he expands. The Jacksonville, Fla., Camille's Sidewalk Café franchisee hopes to run five stores in the next five years.

Duke is one of a growing number of franchisees and franchisors using outside firms (also known as PEOs, or professional employer organizations) to run their human resource operations. According to the National Association of Professional Employer Organizations (NAPEO), the PEO industry generates approximately \$42 billion in gross revenues annually. About 700 PEOs offering a wide array of employment services and benefits are operating in 50 states. The Harvard Business Review recognized the industry as "the fastest growing business service in the United States during the 1990s."

And the franchise world is no exception. Jay Starkman, CEO of AlphaStaff, says that his franchise client base has been expanding rapidly in the past three years. Founded in 1997, AlphaStaff always had a few franchisees such as Duke, but recently signed on franchisors such as U.S. Lawns and Hampton Inns, which offer the HR component as part of their franchise offering.

Ken Hutcheson, president of Floridabased U.S. Lawns, says he is a passionate cheerleader for outsourcing HR. After one of his very successful franchisees got tapped with a huge workers' comp bill in 1993 that very nearly put him out of business, his company said, "We can't deal with that anymore" and signed its first outsourcing contract. He signed with AlphaStaff in 2003.

"In watching small business owners over the years, I've seen more emotional and financial distress over payroll than anything else," Hutcheson says, "especially tax laws." And he says that dollar for dollar, outsourcing is cheaper. "I've sat down with franchisees, and we did the math." While U.S. Lawns does not require franchisees to use an HRO, the company strongly recommends the practice—and recommends AlphaStaff to every one of their 144 franchisees, but Hutcheson says many choose local HROs and a few prefer to do it themselves.

"From a franchisor's perspective, we have a helper-type personality," he says. "And when one of my franchisees calls saying they have an employee who hasn't showed up for three days and can they fire him, I don't know what to say. That's not my expertise. So I can refer him to the experts. It limits their—and our—legal exposure."

## Premium Opportunitie



**They do it all**

Starkman says an HRO component creates a real competitive advantage for franchisors when selling franchises because it provides additional tools to help them succeed. "When looking to buy a franchise, a person will look at one that offers an HR package and one that doesn't," he says. "It's value. We can give them everything from payroll services, access to a medical plan, 401(k) pooling with a larger body of people, to compliance advice. That way the franchisee can focus on running their core business."

An HRO also offers franchisors the advantages of standardized reporting and managing of the franchisees. Liability control is built in too, says Starkman. "The franchisor no longer has to worry if the franchisee is following all the labor laws," he says. "We do it for them. We make inspections and make sure all compliance rules are followed."

AlphaStaff, headquartered in Boca Raton, is often brought in during initial franchisee training. Services can include hiring, firing, retention review, employee handbooks, and safety training. Starkman says the firm is flexible enough to build an HR program around the needs of its clients, such as providing a direct link through the franchisor's web site for payroll input.

For franchisees such as Duke, Starkman says outsourcing is economically feasible from the get-go. Duke says that the fees he pays AlphaStaff are definitely less than he would have to pay for an HR person's salary.

And he can't even measure the savings in his own time dealing with employee issues. He says that once during the past year, AlphaStaff even helped him to avoid a legal issue—and accompanying legal bills. In addition, an HRO can save clients money on benefits by aggregating the costs among all its clients. "We can provide better rates when they use our buying power," Starkman says.

**Franchising outsourcing?**

There are two kinds of relationships a company can have with an HR provider: as consultant to the owner or existing HR staff, or as co-employer. In the co-employment model, the PEO relationship involves a contractual allocation and sharing of employer responsibilities between PEO and client. As a co-employer, a PEO contractually assumes substantial employer rights, responsibilities, and risk through the establishment and maintenance of an employer relationship with the workers assigned to its clients. Essentially, the employee works for both the client and the PEO.

Other firms are emerging in this HRO growth industry, serving primarily as consultants. The Human Resource Department, Ltd., (THRD) is a Cleveland-based HRO that works with franchisees and franchisors in this capacity. The company won't write the checks or purchase benefits, but instead will do the research and provide policies and personnel manuals for all of a company's HR needs.

Chuck Niles, owner of THRD, says PEOs are growing in double digits nationally and will continue to grow in the coming decade. "The whole field of HR over the past 10 years or so has seen a trend of employers to outsource much of their day-to-day and administration functions," Niles says. "It's not their core business."

He says the HR outsourcing phenomenon in franchising follows on the heels of other industries that saw advantages of outsourcing beginning in the late 1960s, when security was outsourced. As companies looked to downsize and save money, the trend moved to janitorial services and payroll. "Most everybody uses an outside payroll service like ADP and Ceridian now," Niles says. "Even we do. They are the specialists. They can keep up with all the tax laws and medical laws that just keep growing. It really takes a specialist these days."

For himself, Niles has seen so much growth and learned so much from his franchise clients that he is now selling franchises of THRD. One has opened in Atlanta and he is negotiating a number of others nationwide.

"The management of human resources requires a multi-disciplinary approach," says [Maureen McKay](#), an associate at the Mississauga, Ont.-based law firm [Pallett Valo, LLP](#). "There are potentially very significant legal implications for almost any decision that a franchisor might make about the management of its human resources."

Whether the franchisor handles all of these issues in-house or not, it is the franchisor who must consider the implications of HR decisions, as the franchisor ultimately will be held accountable for them.

"In all cases, human resources personnel and consultants should be sufficiently familiar with the law (including employment standards, employment equity, workplace safety, pension and benefits, and human rights legislation) as it applies to their work and the people that they manage to know when significant legal implications are likely to arise, and to consult with the franchisor's legal advisors about all relevant issues before recommending or implementing a particular course of action," she says.

McKay advises any client who outsources to have in writing from their HRO:

- the extent to which it is relying on the HR or franchise consulting firm;
- all assurances and promises made by the HR or franchise consulting firm; and
- the HR or franchise consulting firm's authority to make, and the extent of its responsibility for, decisions about HR.

In general, McKay says that HR issues are so critical to a franchise system's success that at least some HR expertise should be held inhouse.

"A good in-house HR person or team can, however, manage and use the resources of a specialized HR and franchisee selection firm to assist with the management of human resources at a corporate level, as well as the identification, selection, and management of franchisees, on an ad hoc basis," she says.

While outsourcing devotees rave about the benefits of outsourcing, others are more reticent and only willing to take advantage of a specialist for part of their HR solution.

Lois Marshall, president of The Marshall Group, has been a corporate recruiter in the franchise world for more than 30 years. Marshall says that she has not seen a dramatic rise in HR outsourcing.

"I know in other industries they do it a lot," Marshall says. "I haven't seen it a lot in franchising." Instead, Marshall sees pieces of the HR role outsourced when a narrow expertise is in demand, such as for her skills at finding and placing top franchise executives.

"The culture is often so difficult to outsource," she says. "When I'm placing an executive, I require a lot of leeway to learn the culture of a company, and I have access to at least 10,000 resumes. We track franchise careers, and know who is where and what they have been doing."

### **Outsourcing variations**

For others, outside technology offers a level of expertise and consistent reporting often lacking within an organization. Insight Direct, for example, offers its ServiceCEO business management software, which focuses on the service industry and is used by more than 40 franchisors and their franchisees. Clients include Mr. Handyman, Maid Pro, and Coit Carpet Care.

"Most of our clients mandate the use of the software to their franchisees," says Chief Operating Officer Chris Chapman. "It's a little more difficult in the service industry because they need to cultivate employees, their main product. Finding ways to reduce employee turnover is huge."

ServiceCEO, he says, takes some of the biggest HR load off the owner. Tasks such as employee scheduling and tracking are done instantly online. Employee data, contact information, skill sets, and available work hours are all integrated for instant use. A franchisee can take a customer call and with one touch can find out who is closest to the customer, when he can be there, and what jobs he can handle.

In business for eight years, Boston-based Insight Direct has seen a huge jump in franchise business in the past three years. "We don't have a big marketing budget, mostly online," Chapman says. "But word of mouth is really working."

Still others eschew outsourcing all together, saying that because employees are the most important element to both the franchisor and franchisee, sensitive and personal work done by a human resources department is best kept in-house.

"The reason we keep our HR inside the culture of our company is because we take care of our people and are able to do an efficient job of it ourselves," says Judy Irwin, vice president of HR and training for Golden Corral, with 121 company restaurants and 370 franchises owned by 200 different franchisees. "We feel real strongly about our processes. For example, we have a psychological test that we train our in-house people to administer to potential franchisees. To outsource that, you would be paying someone who doesn't have the same accountability as someone who is working here."

Golden Corral continues to add benefits to its plans as well, which are available to franchisees and their employees. Group benefit plans are available to franchisees at the same rates as corporate employees pay, and a new benefit that helps an employee with mortgage costs has proven very popular.

Irwin says that her team remains flexible with franchisees and works closely with them to make sure they understand compliance and reporting procedures. "If they miss an open enrollment, we don't automatically shut them out; we might call and explain the importance of the deadlines and work with them," she says. "We understand that they don't always know the rules. It's our job to help them understand. And there's a huge difference between saying that and doing it."

Linda Ray is a North Carolina freelance writer specializing in business and franchising.

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