



A Practical Guide to Fractional Service Providers

Upgrading talent without breaking the bank.

by David Working

Business owners in the middle market are all too familiar with the task of trying to optimize cost structures – getting the most efficiency and “bang for the buck” out of facilities, equipment, customer relationships, and many other elements of a successful enterprise. People have always been vital and important to businesses, but over the last several years, we’ve noticed a shift in attention toward people in a different way. Searching for ways to optimize human capital, while fighting the inefficiencies of talent markets, is an ever-present challenge for businesses in the middle market. The human capital corollary to the engineer’s triangle (fast, cheap, reliable – pick two) seems to be availability, relevant experience, and compensation expectation.

An example could be a stable, modestly growing manufacturing business in a small town outside of a major metropolitan area in the Pacific Northwest. It has just outgrown the capability set of its hardworking bookkeeper and needs some expertise in setting up more robust financial oversight and reporting capabilities, but attracting capable, senior-level finance talent to its town with a handsome compensation package seems like overkill.

An increasingly popular way for businesses to address this issue is through the use of fractional service providers, which have proliferated significantly in their breadth and depth of service offerings in the middle market. For a variety of functions and roles—including accounting, finance, marketing, sales, project management, and others—a fractional solution can offer a way for a business to access additional capability at a lower total cost than bringing on a full-time hire.

DEFINITIONS

Some definitions are in order, before readers start to think that we’re describing what you all might think of as “consulting.” Consulting and fractional service are both subsets of outsourcing human capital. We segment among a few different ways to support internal teams with outsourced providers:

- **Traditional consulting.** Consulting is hiring a person or a team to accomplish a closed-end project with a scope of work and

defined deliverables. Consulting may be entirely off-site, like when an intellectual property specialist performs a freedom to operate search on your behalf; or it can be on-site, like when an operations firm brings in a strategy consulting team for a three-month organizational redesign. Either way, the firm is hiring a skill set or extra bodies for a specific, defined project, and they usually remain distinct from existing operations.

- **Interim executives.** Interim executives are usually experienced industry veterans, and are hired for an open-ended but impermanent time period to help shepherd a company through a particularly trying time. Situations might include bankruptcy, a transaction process, post-merger integration, or a period of extraordinary growth. Sort of a specialized branch of consulting, these executives differ by becoming part of the fabric of the client – taking on direct reports, coming to the office every day, and fully stepping into their role to a degree more akin to a full-time hire than a consultant.

- **Fractional service providers.** Fractional service comes into play when a business is in need of an ongoing service, but the dedicated time for that service doesn’t defend the hiring of an FTE. A fractional professional or team becomes part of the organization, but for a certain number of hours per week or days per month. Imagine a project manager who organizes and runs update meetings for the same 4 hours every week, or a controller who takes a week to direct closing the books every month.

“UNBUNDLING” OF FUNCTIONS

The economics of each solution depend on the “unbundling” of functions from people. Said differently, not every function is a perfect match for a single person’s time, attention, and capabilities. In the case of the fractional service provider, imagine our original example of a manufacturing firm in a small town – it may have 5 hours’ worth of “CFO” work, 10 hours’ worth of “controller” work, and 35 hours’ worth of “bookkeeper” work in a week. If the company is cost-conscious, it may hire a local bookkeeper—at a bookkeeper’s competitive pay—and try to help that person to “stretch”

to cover the controller-type work, while other executives flex to cover the few hours of CFO-type work. When compared to hiring an experienced CFO from out of town to do all 50 hours of work (the majority of which is beneath her pay grade), this setup appears appropriate.

While this seems like an adequate solution on paper, it rarely comes to pass as described. The “stretch” expectation of the bookkeeper is often a source for frustration, both on the side of the bookkeeper (expected to accomplish a role they do not have the background for) and on the side of management (because the work often ends up not being accomplished to the expected standard). The CFO work often ends up unaddressed, behind a long list of other tasks executives are facing down in any given week. In our observation, many middle-market businesses struggle with getting caught in this pattern.

Fractional services provide a third option to this scenario. The firm can hire a bookkeeper and compensate him appropriately for the work for which he is qualified, and hire a more experienced professional on a fractional basis (for a few hours per week) to cover the higher-level work. The firm comes out with strong coverage of its needs without overpaying for unused capacity or improperly allocated resources.

NOT ALWAYS THE ANSWER

Outsourcing is not the answer to every human capital problem, and businesses should be careful to understand their situation and the options available to them. There are a few critical questions a business owner or manager can ask to help shape their decision tree:

- What’s the time period for the needed role? Does the business need this capability indefinitely, for a few weeks, or something in between? Will the role change significantly over that time?
- What’s the time requirement of the role week-to-week and month-to-month? Is this a full-time job, or is it a piece of a person’s week or month? Is the time requirement predictable? Is the time requirement volatile?
- How specialized is the capability needed?

Is it trainable or does it require significant educational or professional experience?

- How deep is the local talent pool?

Does the capability exist within commuting distance? Could the role be accomplished remotely?

- Is your firm growing or otherwise changing significantly in a short period? Would staffing flexibility be worth a premium to your business during this time?

- Are you expecting a meaningful transition in the business, like a turnaround or a transaction?

LABOR MARKETS HAVE CHANGED

Labor markets for experienced professionals have changed over the last 20 years, creating a

labor supply interested in holding these types of positions. It is now possible to obtain quality capabilities on a fractional basis, and competent help can be found for less-than full time roles. Some experienced professionals are tired of the range of functions and duties required of a full time position as they flex down to cover all needs. By taking on several part-time roles, this person can concentrate on the narrower functions in which they are both excited and expert. Other experienced professionals choose not to work full-time in order to allow time for other priorities, usually family or other obligations. A full-time job in our current economy is a 50-60 hour-per-week job, not the 40 hours

expected a generation ago, and there exists a robust talent market of people looking to fill those 50-60 hours in creative ways. An experienced person in one of these situations can bring talent the company could never afford to hire on a full-time basis.

As outsourced solutions become more sophisticated, middle-market business owners would be well-served to understand the offerings. Optimizing a team can unlock meaningful value for a business without over-reaching on cost, and an advisor familiar with the company's situation and the breadth and scope of solutions can help work through actionable options. **zs**



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ABOUT ZACHARY SCOTT

Since 1991, Zachary Scott has assisted owners of privately-held businesses in the greater Pacific Northwest to plan and execute major business or ownership transitions through three service lines: sell-side M&A, acquisition and investment advice, and direct investing. For more information on Zachary Scott, go to **ZacharyScott.com**.

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