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Skills and Scale

Why Emerging Companies Must Innovate How They Resource Back-Office Functions

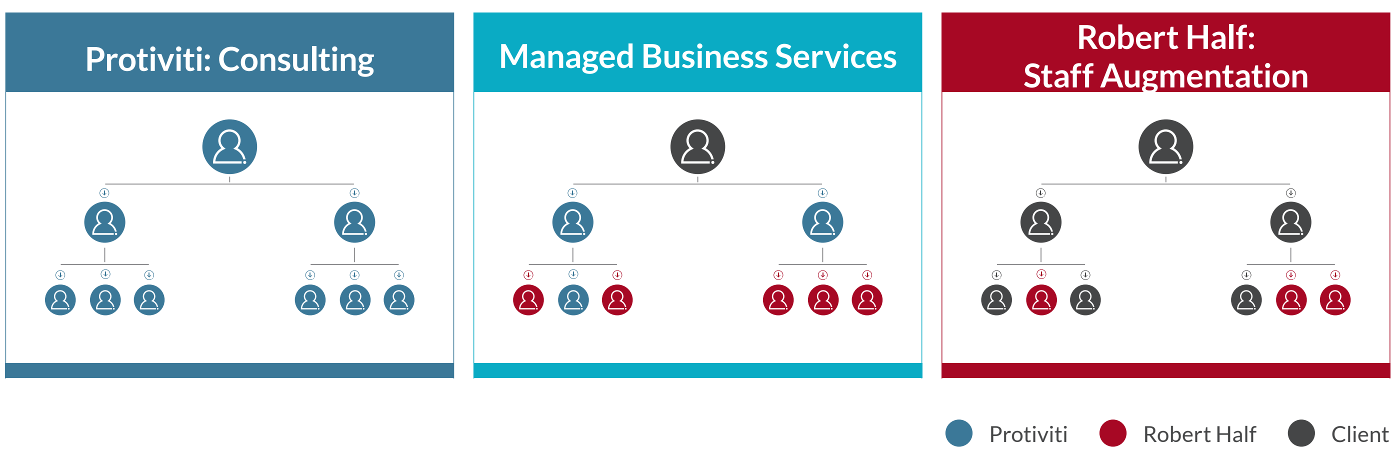
The Next-Generation Finance and Accounting Labor Model

Introduction: Would You Bring a Mainframe to a Hack-a-thon?

You are gearing up for your company's biggest code sprint of the year. As you organize everything you'll need, you definitely won't plan to bring to the task a 1950s-era mainframe computer — not if you want to succeed and certainly not if you want to avoid major back strain. The UNIVAC mainframe, introduced in 1951, measured 25 feet by 50 feet and was composed of thousands of tubes and crystal diodes. Its maximum storage capacity could handle just the first two pages of this document.

It seems obvious to state that organizations need to leverage the latest methods, technologies and processes. Consider, though, that many emerging companies — high-growth firms progressing through Series A-C funding, to pre-IPO stage, exit and beyond — are taking an outdated approach by employing the finance and accounting labor model equivalent of a 1950s mainframe. The irony of this dated approach to human resource allocation would be rich if there was not so much business value at risk. After all, startups excel at devising innovative products and services complemented by cutting-edge business practices that delight customers and disrupt markets.

By sticking with a reactive, hire-or-outsource approach to staffing the finance and accounting function, emerging companies are limiting their growth potential. The typical startup mentality, whereby employees are overtasked and overworked in anticipation of a big payday, can place a company's potential at risk. There's a better way. Established enterprises already are testing and refining a new finance and accounting labor model, one that relies on a divergent talent-sourcing approach, more strategic planning and the deployment of common functional "building blocks" (see below and page 8 for information on the Protiviti/Robert Half Managed Business Services approach). Leaders in emerging companies should recognize the benefits of this new model, the risks inherent in not rethinking their approach to labor, and the inflection points along their development curve where the need to skill and scale the finance function as smoothly as possible is especially acute.



The 'Either-Or Problem': The Trouble With Traditional Resourcing Approaches in Startups

Startups and other emerging companies operate at breakneck speed and in a decidedly lean-and-mean manner. Their rapid pace is fueled by a critical quest for cash that drives organizations to do nearly anything to convert their prospects to customers, drive revenue and exceed expectations. The lean operating model, with the primary focus on customers and products, is vividly apparent in how earlier-stage companies resource their back-office functions — which is minimally, at best.

While highly conducive to minimizing costs, this business cadence is ultimately unsustainable and makes predicting future operational needs, even in the short term, extremely difficult. A combination of factors — sudden spikes in customers and revenue; scrambles to satisfy big, unique requests from different customers; and thinly resourced finance and accounting teams — gives rise to multiple and frequent severe resource challenges in finance and accounting.

Addressing these issues requires flexibility, innovation and technical expertise in managing accounting resources, technology, processes, and compliance with requirements such as generally accepted accounting principles (GAAP). When these qualities are present, finance and accounting functions support and even can accelerate the company's growth; when these capabilities are in short supply, finance and accounting functions contend with disruptive resource challenges, process snags, technology shortcomings and other back-office friction that hinder organizational growth.

Few emerging companies manage their finance and accounting labor models with the type of foresight, innovation and agility that went into making their product and/or services offering so appealing. Despite their startup status and mindset, too many emerging company leaders deploy a decidedly old-school labor model defined by a number of traditional frameworks, approaches and thinking, including:

- A failure to innovate — In most organizations, including emerging companies, innovation is primarily focused on customer-facing capabilities. The traditional labor model — in use since the days of landlines and mainframe computers — is begging for disruption.
- Relying on an either-or model — Under a traditional resourcing approach that many finance and accounting functions still adhere to, hiring is an either-or proposition: Either hire full-time equivalents (FTEs) or fully outsource the finance and accounting function (or major portions of it). Such a binary mindset is limiting. It poses challenges and can cause a cascading set of negative effects. Focusing solely on hiring FTEs requires valuable time and can be particularly expensive in startup-heavy cities and regions where talent is at a premium. Additionally, certain skills are in short supply and can be extremely difficult to find. Conversely, many of the outsourcing solutions available to firms of all sizes require conformance to standardized processes and adoption of shared platforms that severely limit a company's ability to adapt and evolve with the business or provide the access and insight to make critical business decisions. Compounding these challenges, the outsourced model rarely, if ever, offers an integrated or coordinated path forward when a company outgrows the service or platform.
- The "fix it later" fallacy — Many emerging companies make finance and accounting talent (and related process and technology) decisions in ways that are intended to be temporary. The underlying rationale for such decisions is a belief that these foundational building blocks "can be fixed" as an exit event approaches. What inevitably occurs, however, is that entire finance and accounting functions are built upon a series of unscalable workarounds and stop-gap processes, managed by individuals who are stretched thin and may lack the expertise to develop

a more sustainable solution. This inelegant finance and accounting architecture requires much more than a quick fix by the time an IPO or sale emerges. Unwinding that patchwork of workarounds requires an extensive and excruciating effort, especially in the face of high-stakes deadlines. As an example, one emerging business services organization provided so much flexibility to its customers that the company had to support more than 400 invoice templates. The resulting support requirements forced it to scale back-office resources commensurate with its explosive sales growth. By the time the organization felt the pain, the resolution was quite expensive.

- Failing to build in accounting from the start — Increasingly, companies are having to make significant decisions about the nature and architecture of their businesses and products that — oftentimes unknowingly — involve, affect or hardcode significant accounting decisions or other disclosable data at very early stages of the company lifecycle and product development. While not long ago many of these choices would have been limited to certain segments such as software, the rise of the IoT and other trends are rapidly eliminating industries that do not somehow involve the accounting group in relevant transactions or generate disclosable data at the end-product or infrastructure level. A lean, or outsourced, accounting function may be ill-prepared or too removed from day-to-day operations to provide the near- or long-term requirements that will affect the company's ability to produce accurate, reliable and auditable financial statements and disclosures.

Plan for These Five Inflection Points

We believe emerging companies should embrace a new finance and accounting labor model now. Getting started on this shift requires a strong awareness of the need for a more innovative approach to skilling and scaling these functions. This awareness tends to arise during a series of five pivotal turning points that occur throughout the growth lifecycle.

During the following inflection points, finance and accounting functions either thrive or falter in their mission to support growth based on their ability to skill and scale.

01 **The transition from a bookkeeping tool to an integrated accounting package:** As an emerging company's revenue, customer base and organizational complexity rise, it reaches a point where a simple bookkeeping tool, such as QuickBooks, becomes inadequate to handle the company's finance and accounting needs. Deciding when to move to a more sophisticated information system requires an assessment of the function's current and future talent needs. This crucial technology transition raises numerous questions, including some that concern other back-office functions: *Will accounting roles be hired as FTEs, outsourced or co-sourced? Does the current team have the skills and knowledge needed to operate a more sophisticated system?*

What type of IT support do we need to optimize our technology investments? What is the scope of the implementation process and to what extent will it pull our people away from crucial, customer-related activities?

02 Revenue spikes, rapid hiring and new customers: As business thrives and sales soar, finance leaders will need to bring on additional resources. How they do so is crucial to determining how well they manage other growth-related inflection points. Is the decision made to simply hire, onboard and train new accountants and/or clerks? Or are other elements of the function's ability to scale — systems, banking relationships, processes and more — also assessed so that a more forward-looking decision can be made later to reduce other change-related friction and costs? In many cases, securing a major new customer can trigger numerous additional requirements that must be handled by finance and accounting as well as other back-office functions.

03 Expanding geographic reach: Often, the complexity of finance and accounting processes intensifies in response to more subtle milestones. The opening of a new office in another global region may not generate a flood of new revenue immediately, but addressing the unique finance, accounting and tax requirements of operating in new countries requires new skills that may not be on staff or available through existing outsourcing relationships. For example, the opening of a new sales office in Europe or the outsourcing of development or manufacturing capabilities to Asia creates complexities that often expose the inflexibility of the traditional labor model and the skills and experience available within it.

Back-office innovation is not an afterthought.

04 Business retraction: Emerging companies sometimes face the reality that their business is declining. Whether a temporary setback or something more permanent, the reality of having more people than what's needed is not acceptable in today's business environment. Frequent layoffs can ruin morale and lead to unplanned levels of attrition. They also may require those left behind to work extreme overtime under difficult circumstances. In such instances, it's vital that these companies have the ability to scale down quickly and then respond to a recovery even more quickly.

05 An exit event: There are a staggering number of finance and accounting requirements attached to an IPO, a disposition event and a more traditional sale. When the accounting and finance function's ranks are too thin or insufficiently skilled to meet these requirements, which typically come under intense deadline pressures, it can delay the exit event and/or result in a lower valuation. As a simple example, if the accounting team cannot resolve accounts receivable that exceed 180 days, it will have a negative impact on the company's ability to take on additional debt.

Each of these five inflection points requires CFOs and other finance and accounting leaders to make strategic decisions, which trigger ripple effects that help determine the speed and ease with which the function manages future growth transitions. For that reason, these inflection points should also prompt finance executives to reflect deeply on the efficacy of the labor model they use. If their approach to talent is not as flexible, configurable and agile as it can be, they should consider embracing one that is more in line with the innovative, customer-facing capabilities their business partners have developed.

Back to the Future of Labor

The best time to consider a new approach to the labor model is before any of those inflection points arrives. Each of the ensuing growth phases emerging companies attain after receiving their initial funding is accompanied by new challenges that require new finance and accounting skills and expertise.

An ERP implementation requires finance professionals with technology and change management skills. A potential sale requires banking and investment expertise. A market downturn requires cost-reduction experience. And so on. Within many early-growth firms, accounting can be almost entirely outsourced with little risk. Later in the company's development, however, as new demands arise, the same company will need a CFO who knows the business and is present in the office so that he or she can interact with the CEO and other leaders in real-time. As these CFOs manage changes of greater magnitude and with growing frequency, they need to be able to scale up (and down) their teams quickly to execute these efforts.

By sitting down and creating a strategy to address how to respond to fast-changing resource needs, emerging companies are better positioned to avoid the many risks intrinsic within the traditional labor model. This planning can also familiarize emerging company leaders with the new labor model that a growing number of large and established businesses use. Google parent company Alphabet employs roughly equal numbers of full-time and contract workers. Microsoft adheres to a similar model, relying on a large percentage of contract or managed services staff as part of its overall workforce.[1]

The new labor model comprises, among other elements, a managed services approach that aligns full-time employees, external consultants and interim professionals in a far more coordinated fashion. The model is especially attractive to companies that need ongoing access to external partners who, over the lifespan of the relationship, develop a deep knowledge of the organization's strategies, opportunities and risks.

This emerging labor model is actually based on a decades-old concept, the "Shamrock Organization," by the organizational behavior and management expert, Charles Handy. Handy's model organizes the workforce of the future into three categories (or "leaves" of a shamrock):

1. Full-time employees who form the company's "professional core"
2. A "contractual fringe" consisting of resources the enterprise leverages by contracting with other organizations to provide additional capabilities[2]
3. A "flexible labor force" consisting of resources deployed to address interim resource needs

Handy's framework proved revelatory in that it inspired and foretold the widespread adoption of traditional outsourcing in the late 1990s through the 2000s while also pointing to a solution that addresses the mounting 21st century strains on the traditional labor model.[3]

Given its still-emerging nature, the new finance and accounting labor model is applied differently by different companies. That said, most, if not all, of these approaches share a set of common qualities and capabilities, including:

- A long-term plan for addressing current resource needs — When making decisions about current resource requirements, future people, process and technology changes should be considered. Whatever source an emerging company uses to hire a payroll clerk during an early growth spurt should also have the ability to deliver an ERP-skilled accounting manager or an accounting director with GAAP and revenue recognition expertise that the company will need later in its growth trajectory.

[1] Weber, Lauren. "The End of Employees," *The Wall Street Journal*, Feb. 2, 2017: www.wsj.com/articles/the-end-of-employees-1486050443.

[2] Handy, Charles. *The Age of Unreason*, Harvard Business School Press, 1989.

[3] Handy, Charles. "The Shamrock Organisation," London Business School, Jan. 14, 2015: www.london.edu/faculty-and-research/lbsr/the-shamrock-organisation#.WtS0kWEh3Cw.

The most agile and flexible labor model deploys a well-organized blend of FTEs, interim professionals, external experts and managed services.

- Blended, cost-effective and location-savvy talent sourcing — As Handy laid out, the most agile and flexible labor model deploys a well-organized blend of FTEs, interim professionals, external experts and managed services. Further, when a single external partner can deliver all of these resourcing models over the long term, recruiting, hiring, onboarding, training and knowledge transfer can be performed in an agile manner. It's also important to note that at various stages of early growth, finance and accounting people, processes and technology can, and perhaps should, be managed externally through suppliers. However, at certain points, those resources are managed much more effectively inside the company. How easily, quickly and cost-effectively these types of transitions can be performed represents a crucial determinant of whether the finance and accounting function drives or hinders profitability and value-generation.
- Common building blocks — Object-oriented programming operates on the idea that standardized collections of computer code can be deployed as building blocks to accelerate software development, increase developers' productivity, and ease maintenance and upkeep. The new labor model shares these features; in that way, this approach can be viewed as "object-oriented accounting," where relatively standard and repetitive accounting services (e.g., payroll, accounts payable, tax compliance and reporting, ERP upgrades) can be deployed quickly and cost-effectively during high-growth periods.

Example of Future Labor Model in Finance

Professional Core	Contractual Fringe	Flexible Workforce
Strategic Finance	Accounting Operations (accounts payable, accounts receivable, collections, account reconciliations)	Projects
Risk Management	Tax Compliance	Accounting Operations (peak demand)
Treasury	FP&L (business analysis, management reporting, reporting technology)	Address Staff Vacancies
Tax Strategy	Payroll	Backlog Cleanup
Accounting Operations (general accounting, financial reporting)		
FP&A (forecasting, planning)		

In Closing: Continuity Is Crucial

How well the finance and accounting function in a startup, emerging or pre-IPO organization responds when revenue surges and other sudden changes influence the long-term performance of a growing firm is a crucial determinant of its ability to manage these inflection points. In addition, such growth and changes have the potential to affect the finance function's overall continuity — specifically pertaining to organizational knowledge, process efficiency and technology expertise.

Unfortunately, the traditional labor model offers little in terms of continuity: New skills tend to be brought on board as quickly as possible to meet pressing needs without much thought for how well those sourcing decisions align with future finance challenges and talent needs. Like the UNIVAC mainframe, we would argue that the traditional finance labor model has a history of success, but in another era.

An increasing number of businesses, and especially emerging companies, are leaving the past behind for a much more data-driven, fast-moving present. Succeeding today and well into the future requires new ways of thinking and operating, as emerging companies demonstrate so vividly with their innovative customer-facing offerings. Now, it's time to apply similarly innovative thinking to disrupting finance and accounting and other back-office functions so that these operations remain agile and relevant.

Is Your Labor Model Outdated?

As emerging company leaders assess the degree to which their finance and accounting functions will drive or impede growth, they should ask the following questions:

- *Are we skilling and scaling finance and accounting in a thoughtful manner — and with speed and ease?*
- *Do we design and operate our back-office functions with a level of innovation similar to what we bring to customer-facing offerings?*
- *Are we retaining and sharing institutional knowledge as we expand our finance and accounting function?*
- *Are we experiencing difficulty in hiring, onboarding or retaining finance and accounting professionals?*
- *How often do we consider a need to revamp or rebuild our finance and accounting function?*
- *Are we overusing quick-fix workarounds for problems?*
- *Are we paying consulting rates for temporary, lower-skilled accounting resources?*

If more than a few of those responses are not aligned to your organization's growth plans, it's time to consider a new approach to managing the finance and accounting function.

By sitting down and creating a strategy to address how to respond to fast-changing resource needs, emerging companies are better positioned to avoid the many risks intrinsic within the traditional labor model.

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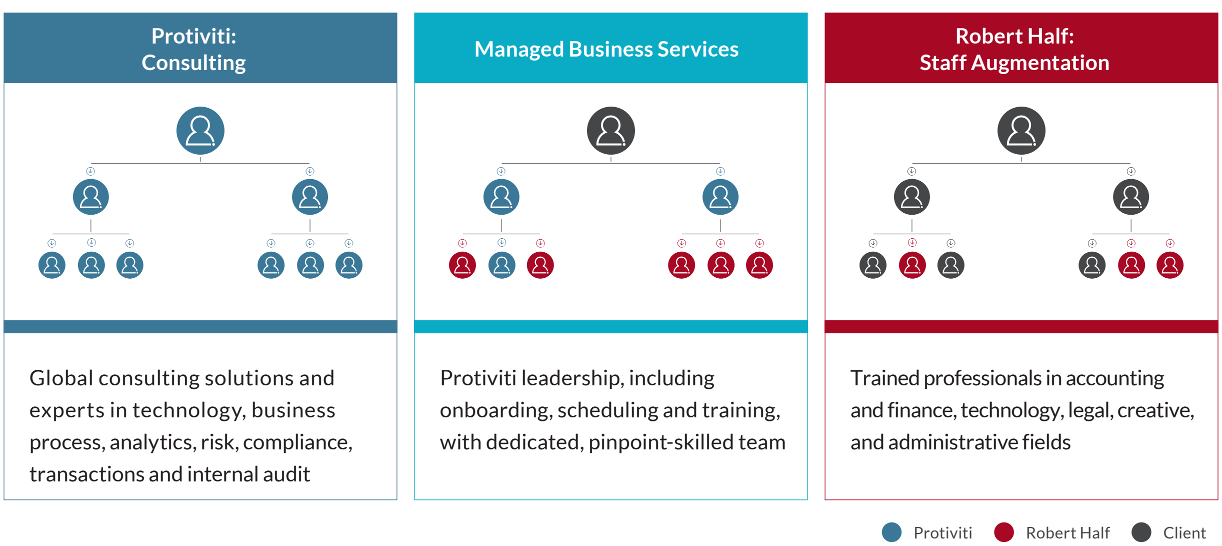

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