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How Organizations Can Reduce or Contain Costs

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Every organization recognizes the importance of producing and delivering product, services and programs in the most efficient manner possible. Those dollars spent on activities that add little value and/or do not support the strategy could be put to better use by reinvesting in innovative technologies, people, facilities and other assets, generating dividends for shareholders or funding stock buybacks, driving new/expanded program or project launches or, simply, lowering prices or fees to attract and retain customers, clients or members.

There are a number of proven ways to reduce (or contain) costs that can provide savings opportunities and they are discussed in this summary of actionable steps to take.

Backdrop

Although the unemployment rate in the United States remains low by historical standards and the stock market continues to reach new highs, organizations continue to face significant financial pressures:

- Many not-for-profit organizations are finding that the funds available through grants and contracts are limited due to federal government cutbacks, state reductions as they rebuild their coffers, and competition for private money. In certain cases, new regulations and reporting requirements create costly compliance burdens, and there is uncertainty regarding the impact of recent tax legislation on charitable giving.
- Local governments recognize that the level of financial support from the federal and state governments for critical social service, health and educational programs is at risk. In addition, there are pent-up needs to address long neglected capital projects like rebuilding roads and infrastructure as well as state obligations to shore up pension plans for retirees.
- Businesses are now coping with the uptick in the price of petroleum-based products used to operate plants and transport goods, challenged by the need to invest in digital and social media to reach their target audience and realizing that the imposition of reciprocal tariffs is driving up costs and may erode their ability to sell goods and services to foreign buyers.

Focusing on Employee Compensation and Benefits

Compensation is generally the primary cost-cutting target since headcount often represents an organization's largest expense. Some time-tested savings include:

- Reducing the size of the employee base is a common step. However, management should realize that organizational performance may be adversely affected and they should not assume that the remaining staff will simply carry the additional workload.
- Freezing compensation at current levels and providing incentive bonuses if pre-defined organizational or personal goals are achieved. For certain jobs, establishing meaningful and measurable targets is challenging.

- Shifting to a more variable workforce structure can be accomplished by tapping on-call part-time resources or contractors who can augment full-time staff without incurring the cost of benefits. For instance, a trade association may add-on part-time staff prior to and during their member conferences when they require more hands on deck, a college may decide to increase their hiring of adjunct faculty (instead of full-time professors), and a manufacturer may decide to use part-time staff to handle seasonal spikes in sales.

In terms of benefits, the following examples are indicative of what might be realized:

- The employer pays the premium for basic/low cost health coverage and subsidizes higher cost plans, where more of the cost is borne by the employees through their payroll deductions, co-pays and higher deductibles.
- Many organizations have sunset their defined benefit plans in favor of 401-K or similar arrangements, with an employer match up to a defined level.
- Offering tiered benefits could provide long-tenured employees with a more expansive set of benefits (e.g. paid-up health and life insurance post-retirement) while newer hires receive more limited coverage.

Scrutinizing the Types of Products, Services and Programs Provided

Rethinking business strategy and deciding what products, services, projects, programs and initiatives should be supported going forward is worth exploring. As an example, a biotechnology company might examine the full life cycle cost of developing new compounds that might become commercial drugs (including research, clinical trials and regulatory approval), the likelihood of success and the drug's market potential as a basis for determining which initiatives should be continued, scaled back or phased out. In the case of a global foundation, senior leadership might choose to concentrate their awards for greater impact and, in so doing, might reduce the number of grants awarded and the number of administrative staff and travel costs needed to vet applicants and monitor the work of the award recipients.

Targeting Occupancy Costs for Space and Facilities

Unless you own the building or space in which you operate, your lease likely contains escalator clauses that drive up occupancy costs over time. To reduce the expense:

- Revisit space requirements, especially if a significant portion of your staff spend the majority of their time out in the field with customers or grantees. Sharing offices/desks or allowing personnel to work from home under a virtual office arrangement may fit your operating model.
- Shrink the footprint by consolidating facilities or even sharing space with another organization.
- Redesign the office layout, allocating less square footage to each employee. Electronic document repositories should allow you to reduce the amount of office space dedicated for the storage of paper files.
- Consider whether it is necessary to be in a "Class A" building if a nearby "Class B" building would work just as well. Landlords interested in attracting employers to "Class B" buildings often provide significant incentives in the form of buildout dollars, lower rent and the possibility of subletting space. One professional services firm maintains their "corporate headquarters" in the high-rent district for client meetings and relocated its back office functions to another part of the city where the costs are lower.

One notable success story involved a social services agency that sold its headquarters to a developer willing to pay a premium to develop the property as a mixed use retail and residential complex. The agency relocated to another part of the city and now possesses a healthier balance sheet with more funds available to support their mission. Other examples include a consumer products manufacturer that entered into a sale-leaseback arrangement for its plant and distribution center, and museums and libraries to generate income by renting out space as a venue for weddings, corporate functions and film productions.

Revisiting Supplier Arrangements

Expenses related to utility (e.g. energy, telephones), travel (e.g. airfares, lodging), technology (e.g. hardware, software, cable) and supplies may be targets for reduction. Savings can be realized by negotiating favorable deals based on anticipated spending levels and/or forward buying product at the times during the year when suppliers heavily promote items. In order to capitalize on these opportunities, management must know its usage patterns to secure favorable terms. With regard to technology, further value can be gained by simply using videoconferencing to limit the number of trips to branch offices or customer sites and extending the useful life of computer hardware and software before replacement.

It always pays to closely examine invoices to ensure that the amounts billed are based on the prices agreed-to for the goods and services received. One professional services firm found, for example, that their landlord charged tenants for energy usage in common building areas, which was contrary to the lease terms; the same landlord also added a quarterly charge for cleaning of office windows and carpets, even though the service was never performed.

Avoiding Waste and Misuse of Resources

Looking at how a company's resources are used may shed light on areas where there is waste or possibly misuse. For instance, while allowing employees to watch movies on company-provided computers may contribute to a relaxed work environment, the usage of additional bandwidth may ultimately result in the need to purchase more network capacity. Also, if staff are allowed to ignore policies regarding the allowable classes of air travel, these costs may spiral out of control. One service organization learned from a former spouse that their mailroom and production department manager had a side printing and binding business that involved the use of company photocopiers and supplies. Nobody questioned why the manager worked numerous weekends or why so many supplies were constantly reordered.

Determining Whether Outsourcing Certain Functions Makes Sense

Outsourcing can help an organization stay focused on their core functions, while allowing other parties to support non-core activities. The main reason to pursue this model is to augment the workforce, add specialized skills/expertise, foster organizational agility and shift or share responsibility with a service provider. Some of the possibilities include:

- Information Technology: server/network management/monitoring, security, planning, end-user support, web presence development/deployment, datacenter operation, training, disaster recovery
- Finance and Investments: planning, bookkeeping, reporting, Form 990 and tax filings, advising on portfolio positions as well as tax strategy
- Legal: contracts, risk management, litigation, privacy
- Human Resources: recruiting, onboarding, compensation analysis, payroll
- Real Estate/Facilities and Purchasing
- Marketing, Communications, Public Relations, Grant Proposal Development and Program Administration
- Internal Audit/Compliance
- Fundraising: promotional campaigns, proposal development, events, donations
- Contract Manufacturing: production of goods to specifications set by the customer
- Shipping: using trucking companies to handle the transport of raw materials or finished goods in lieu of owning a fleet and having to maintain and staff it

In considering outsourcing, beware the risks of transferring the work offshore. Progressive organizations not only perform detailed reviews of the contracts and master service agreements but also implement a monitoring process to ensure ongoing compliance with the agreed-upon service levels. Many organizations prefer an on-shoring approach, since many parts of the United States provide more favorable labor costs.

An interesting alternative to outsourcing is co-sourcing, which more favorably balances risk and reward. Such arrangements are predicated on the shared commitment by both the customer's and service provider's staff to collaborate in order to achieve a common objective or outcome. Co-sourcing arrangements encourage vendors to focus on the value they bring to their customers. Many private and public sector organizations, for example, retain ownership of the information systems planning, application development and security functions, while directing or overseeing the staff of the service provider responsible for operating and maintaining the servers and network situated at the provider's datacenter. In this way, the organization exerts control over those functions that provide a competitive advantage and are closely aligned with their strategy, retains the process knowledge, prevents total dependence on a third party and, if necessary, allows for an easier transition to another service provider.

Getting Started

First, before taking any cost reduction actions, most organizations would benefit by carefully reviewing how their critical functions operate. By identifying those processes that provide little value, act as bottlenecks and lend themselves to automation, management will have a better sense of the resources required to sustain performance going forward.

Second, make sure that your financial accounting function provides the information necessary to make sound cost reduction decisions. Financial information that is late, incomplete, inaccurate or poorly presented prevents you from:

- Understanding exactly where you stand in terms of cash flow, performance against budget and overall fiscal health
- Obtaining a view of expected fiscal year outcomes based on actual results to date along with a current reforecast for the remaining period
- Planning what will happen when specific changes occur so management is better prepared to respond to varying conditions and avoid a "firefighting drill"

Third, reassess the impact of each change on your operations and strategy and be attuned to unexpected consequences. Some organizations have learned the hard way that in their rush to cut costs, they failed to consider employee severance obligations, how they would cover for skill sets lost, the effect on the morale of those remaining, and the possibility that others may leave in fear of being overworked or that their own positions are in jeopardy

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