

U.S. Companies and Contracting for Services in the New American Economy

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U.S. CHAMBER OF COMMERCE



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Dear Reader,

The prevailing narrative that has taken hold regarding high-skilled immigration in the past few years has been marked by members of Congress and the media raising important questions about the benefits of high-skilled immigration. Press reports have inaccurately painted a picture that the H-1B program allows companies to replace American workers with “cheap foreign labor.” The U.S. Chamber embarked upon the publication of this report to set the record straight and provide a more balanced and nuanced analysis. This work focuses on situations where a company has decided to have non-core business functions performed by another company in order to compete in the marketplace.

This report, authored by Stuart Anderson from the National Foundation of American Policy, lays out some of the key facts that are all too often ignored in this ongoing debate. The practice of companies contracting out many non-core business functions to experts has been a common business for many years and the decision-making process is not driven by immigration law; it is driven by the business’s need to operate efficiently and to compete.

I am confident that you will find the information contained in this report useful and informative.

A handwritten signature in black ink, appearing to read 'Randel K. Johnson'. The signature is fluid and cursive, with a large, sweeping flourish at the end.

Randel K. Johnson
Senior Vice President
Labor, Immigration & Employee Benefits

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Abstract

The notion of companies contracting with other firms to provide services is a common business practice that has occurred for decades. Businesses make these choices for a variety of reasons, but generally these decisions to contract with outside firms to provide certain services are driven by the common sense purpose of restructuring operations to make them more efficient. Recently, these practices have come under increased scrutiny by the national media and federal officeholders, who are advancing misguided attacks on U.S. immigration policy. The basic argument made by these critics is that companies are contracting out to reduce costs because they can hire foreign workers more cheaply than American workers.

This paper strives to set the record straight on the legitimate business factors that drive decisions to contract out and the minor, if any, role immigration policy plays in those decisions in the real world.

Executive Summary

For decades, U.S. companies have contracted with other firms to provide services. This is done for a variety of reasons that include gaining access to specialized skills, introducing new technological solutions, and, often primarily, because it leads to obtaining better services at a lower price. This business practice is especially important when it allows companies to become more efficient by paying a firm to perform services for non-core functions (i.e., functions that are not central to the core of the company's products).

If U.S. companies faced little competition, no shareholder pressure to perform well, and no need to maintain profitability, then it might be possible for companies to meet all their needs with one group of in-house employees. However, that is no longer practical in today's competitive and rapidly changing technology environment. In the current business environment, companies that fail to adapt to new realities perish and, as a consequence, they are unable to provide jobs for anyone.

If not today, then someday, the jobs of many Americans who work in information technology (IT) at large U.S. companies may change, or even be at risk, due to the competitive pressures that drive companies to focus on core competencies and seek efficiencies and innovation, including by accessing new technology and the global labor market. Cloud computing, robotics, and technologies yet to reach the marketplace will eliminate some jobs, while also creating other jobs.

In the political arena, some people may want to use the plight of IT professionals who lose their jobs for another agenda. Economic and technological change breeds concern and blaming foreign nationals is often easy, as foreigners have few defenders. But the truth is U.S. information technology professionals at large companies face far more competition for their jobs from the advances of new technology and workers around the globe who never set foot on U.S. soil than from high-skilled foreign nationals permitted to work in America. (Anyone telling U.S. workers differently is not telling them the truth.)

It is in this context that one should examine the controversies over companies contracting out or outsourcing functions to other firms. The "gig" economy, independent contractors, work performed by consultants, and other labor arrangements have come under increased scrutiny in recent years. But by far the most controversy has arisen over any contracting situation that involves foreign nationals who set foot in a company's offices. As a result, parts of this paper focus on these situations.

Why does contracting out only become truly controversial and front page news when foreign nationals are seen on a company's premises? We may never know the answer, since that would involve reading people's hearts and minds. However, it is instructive that there was a complete lack of furor in 2015 when Citizens Bank laid off workers and outsourced functions to India and did so with no foreign nationals stepping foot in the bank, since the entire transition took place *via the Web and*

over the phone. In contrast, quite similar circumstances involving about the same number of employees at Disney, Southern California Edison and other companies resulted in national headlines and declamations at Congressional hearings after workers on visas appeared at the offices of those companies and, therefore, were blamed for the layoffs. One possible explanation for the lack of attention is that publicizing how the contractor for Citizens Bank accomplished the same thing as in these other cases *without* using visa holders undercuts the argument that H-1B visa holders or immigration policy drives contracting decisions rather than obvious business reasons, such as improving efficiency and focusing on core competencies. The contents of this report supports this explanation.

Research and interviews with companies and neutral advisors that provide technical expertise to U.S. companies illustrate the following in this report:

1) Contracting out services and functions is an important business strategy that allows companies to compete better in the marketplace, deploy capital strategically and preserve the jobs of employees unaffected by the outsourcing of certain functions.

Allowing companies to innovate through these new arrangements helps them develop new products and services for customers that can lead to job creation. Government action that has the effect of limiting the options available to U.S. companies as to which contractors they can choose and how such contractors are staffed will not save jobs but will likely raise costs, impede company efforts to improve efficiency and leave fewer resources available to employ U.S. workers and expand other parts

of the company. It will also push more and other types of work outside of the United States.

2) Obtaining the services of experienced contracting companies with expertise and access to the latest technology allows U.S. companies to focus on core competencies, which has been advocated by shareholders and investors in America for more than two decades.

“Focusing on core business functions is one of the primary reasons firms seek to contract with third party service providers,” according to Kevin S. Parikh, global CEO of Avasant, a management consulting firm. “Mature firms are now also seeking innovation and digital transformation to stay competitive and respond to the changing requirements of their customers.” A contractor that specializes in information technology or accounting can provide access to sophisticated technology or services, as well as a global footprint and best practices.

3) U.S. companies become more efficient by innovating and using new technology, platforms or processes that change the way work was done previously, *not* by replacing incumbent employees with “cheaper” workers to do the same jobs.

Cost savings are not achieved by one-for-one replacements but by new ways of performing the function. To accomplish this, U.S. companies go through a rigorous, competitive process, which would only make sense when spending millions of dollars on service providers. Companies seek out the best quality service at the best price. Even though it would be less expensive, companies do not equip their professional staff with “cheap” flip phones to use instead of

the latest smartphones or tablets. Nor do companies hire people off the street at random to be receptionists just to save money. Buying the cheapest of anything without regard to quality is a poor practice for both consumers and businesses, which is why a competitive bid process is used that takes into account both price and performance.

4) When large companies decide to contract out information technology or other services, the most important selection criteria is whether the vendor possesses the skill and expertise to deliver the service or solution.

Companies often hire third party advisors to guide the process, formulate requests for proposals (RFPs), solicit bids, receive presentations and help select a contractor. Contracting out typically involves soliciting from as many as 10 to 20 vendors, making it impossible or unlikely for the U.S. company to know ahead of time which company will win the contract, much less the national origin of each worker on the contract. Visa holders are often used in the transition from the old to the new system. Moreover, in delivering services any vendor must demonstrate expertise and experience in providing solutions to a client's problems, not simply be involved in what some incorrectly refer to as labor arbitrage (i.e., directly replacing a more expensive worker with someone doing the same job but far less expensively by willfully underpaying the new worker, which would be illegal under U.S. immigration law.)¹

When large companies decide to contract out information technology or other services, the most important selection criteria is whether the vendor possesses the skill and expertise to deliver the service or solution.

5) Immigration policy considerations are unimportant in the selection of a contractor, according to experts in business and contracting.

Immigration is not the key component or driving force presented in many press accounts by critics and, therefore, restrictions proposed on H-1B visas would not "save" jobs by preventing layoffs. Such decisions are made independent of immigration law. The composition of a contractor's workforce may become visible when transitioning to the new service provider or when new services are delivered. However, there is no evidence that U.S. employees in the cases cited in the media would have retained their jobs if a different contractor had been selected or H-1B visa holders had not been employed by the contractor. Once a company decides to contract out a function (or elements of a department), the jobs of employees of the U.S. company are at risk, whether a U.S. or foreign-owned contractor is selected, and whether the contractor employs only U.S. workers or a mix of U.S. workers and visa holders.

- 6) In one of the most frequently cited cases in the media, critics blamed Southern California Edison's decision to contract out on the company's alleged desire to replace incumbent employees with workers on H-1B visas, ignoring the key role played by a 2012 report that faulted the information technology management culture after a fatal shooting at the company.**

In December 2011, in the company's IT department, an employee shot and killed two managers. Southern California Edison commissioned a management report that cited "a fundamental lack of leadership" and "dysfunction." *Computerworld* reported, "Some of the [Southern California Edison] employees say the outsourcing move is linked to a 2012 report that found fault with the IT management culture." A study by the Hackett Group found 70 percent of companies that outsourced a function cited a "need to change organizational culture." There is no evidence that when deciding how to proceed in 2012, Southern California Edison knew which contractor it would use years later or the visa status of employees who might work for the contractor. Southern California Edison utilized a law firm to solicit bids from multiple vendors before it chose the companies it contracted with for information technology services. As in a handful of other recent cases, once Southern California Edison executives decided to contract out certain information technology functions, unfortunately the fate of those employees who would be laid off in the IT department was sealed – no matter which contractor was selected, even one with all U.S. workers.

- 7) No evidence has been presented in the dozen or so IT outsourcing cases cited prominently by critics in the media that employees in U.S. companies would have kept their jobs if the IT contractor employed only U.S. workers or if a different contractor had been chosen. As in the case of Southern California Edison, information obtained for this report finds that Fossil, Disney and other companies use a competitive bidding process involving multiple contractors, which would mean the companies decide to contract out key functions before knowing which contractor (or the makeup of the contractor's workforce) would be selected.** The existence of multiple bids would mean that U.S. workers at the companies likely would be slated to lose their jobs well before any of these companies chose which contractor it would use and before the contractor chosen sent any visa holders to transition the work to the new contract.² That means once the decision was made to go in a new direction and contract out certain functions (typically for a combination of strategic and cost-cutting reasons) the incumbent employees unfortunately were already going to lose their jobs due to workplace redundancies – and the choice of contractors, as well as whether the contractors' workers were U.S. workers or visa holders, would not have changed this.

This contradicts the argument that company contracting decisions center on the use (or existence) of H-1B visas. In the case of Disney, it's unfortunate, but the laid-off Disney employees were caught in the middle of a company decision that had at best a tangential relationship to immigration. The two

vice presidents replaced in Orlando in 2014 were not replaced by foreign nationals, but the hiring of two new vice presidents signaled a change in direction for Disney. The contracting companies chosen by Disney employed people on temporary visas but the evidence indicates Disney's restructuring decision was 1) consistent with contracting out done by other companies across the country and in their industry 2) consistent with Disney's past efforts to structure its technology divisions with a mix of in-house personnel and outside contractors, and 3) part of an effort to change its technology focus.

- 8) Efficiencies created by contracting out allow companies to adapt to changing business climates and free up vital resources.** Concerns about ESPN and "cord-cutting" in television have affected Disney's stock price, showing even large companies must be aware of the bottom line.³ Meanwhile, Cengage, a textbook publisher, has attempted to change from a company that primarily *prints* its products (large textbooks) to one that *digitally* produces and delivers its books and other educational materials. To accomplish this quickly, Cengage made a reasonable decision to turn to a company with technical expertise in this type of work, a decision focused on timing as well as saving money in the long run. In fact, another publisher, the parent company of the *Los Angeles Times*, which had been critical in its columns of Southern California Edison's outsourcing decision, announced its own plans to "outsource key functions of our legacy information technology department to create a more agile operation environment and to drive our overall business transformation." About 200 information technology workers

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at the newspaper publishing company would be laid off and work would be performed overseas by the new contractor, reported *Computerworld*. Experts estimate contracting out certain functions can save companies 15 to 70 percent on costs. That savings can free up capital to compete in the global and domestic marketplace.

For many companies this means helping to innovate and develop new products and services, which can lead to increased hiring of American workers in other parts of the business. For companies facing financial difficulties these cost savings can be critical to financial solvency and the ability to retain and hire other American workers.

9) Technological change affects far more jobs than the alleged threat posed by visa holders. Cloud computing, automation and, in the future, artificial intelligence are far more likely to disrupt the U.S. workplace and jobs than anything pertaining to immigration policy. “Automation and cloud will play a tremendous role in the future of outsourcing,” according to Steve Hall of Information Services Group. “We are already seeing business cases that eliminate 40 percent or more of the labor associated with many functions based on a high degree of automation.” For more than a century, technology has exerted a great impact on the labor market. The only difference is that today the pace of technological development has accelerated.

10) There is little evidence to support the argument that certain companies “win all the contracts” because they hire “cheaper” workers on H-1B visas. Several companies, including many U.S.-based firms, are larger than the Indian-based companies operating in the U.S. market and often win contracts over them when competing for business. Moreover, because of the wide availability of talent in Asia and Europe, many of the large outsourcing contracts awarded contain an offshore component regardless of the company that wins the contract. When visa holders are hired, they are paid the *higher* of the prevailing or actual wage paid to “all other individuals with similar experience and qualifications for the specific employment in question.”⁴ The visa holders help in providing the newly-designed function, rather than replace individual U.S. workers on a one-for-one basis, since, if willfully paid less than a U.S. worker, that would be unlawful and also would not improve efficiency (since

it would simply duplicate the status quo with different workers). To the extent some companies win contracts it is because they have developed expertise over many years and deliver services that U.S. companies find of value. Finally, there is no evidence that vendors win contracts simply because they employ H-1B visa holders. If that was the case, then anyone reading this paper could start a company, hire visa holders and win contracts.

11) Several myths about consulting companies and H-1B visas have entered the policy debate, including the belief that two Indian companies use most of the H-1B visas or that preventing consulting companies from obtaining high-skilled workers would eliminate the need to raise the H-1B visa cap. The annual quota on H-1B visas is too low and restricting the use of such visas by certain companies would have little impact on the availability of H-1Bs for other employers. Contrary to the assertion of one U.S. Senator at a recent hearing, two Indian-based companies (TCS and Infosys) did not receive “more than half” of the H-1Bs in FY 2014. TCS and Infosys actually received 10.7 percent of new H-1B petitions approved from the 85,000 petitions subject to H-1B annual statutory limits in FY 2014. Overall, the “7 outsourcing firms based in India” identified by the *New York Times* had 16,573 new H-1B applications approved in FY 2014, which would represent 19.5 percent of the 85,000 H-1B petitions subject to the annual statutory limit. In the context of the 156 million people in the U.S. civilian labor force in 2014 (it’s approximately 159 million today), the 16,573 new H-1B petitions for Indian-based outsourcing firms equaled only 0.01 percent of the U.S. labor force.

12) Policymakers and others would benefit from gaining a deeper understanding of how and why contracting decisions are made. They should consider consulting with the advisors who help companies evaluate contracting decisions. Such individuals do not have a vested interest in immigration policies and understand the complexities of technology and company outsourcing choices. Those advisors would explain the key factors used in selecting a vendor and that immigration does not figure into a company's decision on whether to keep functions in-house or to contract with a vendor to provide the services. “I would say cutting off the H-1B visa program wouldn't really impact outsourcing overall, as the H-1B visa holders have a limited and specialized role in the outsourcing process (specifically, in pushing through the transition phase),” concludes Alex Kozlov, director of content at Alsbridge. Third party advisors confirm that immigration has little impact on contracting out and usually in the transition phase, well after a company has made the initial decision to outsource a function. “In our experience the H-1B visa issue plays a very minor role in outsourcing strategies, much less in decisions to lay off workers,” said Jeff Augustin, managing director, Alsbridge.

13) Media attention has inflated the perception of the prevalence of certain incidents and has lacked context. Across the U.S. economy, every year approximately 20 million people in America lose their jobs due to layoffs, business closures, and other reasons, illustrating how press attention at times has lacked context.

14) To attempt to prevent all layoffs in America would be economically harmful because it would mean the government is intervening to make it difficult to dismiss employees, which, in the long run, has been shown to discourage employers from hiring in the first place. Government protection of incumbent employees has been shown to lead to high unemployment rates. For example, the United States has flexible labor markets and its unemployment rate in 2016 was at or below 5 percent. In contrast, France, which makes it difficult for employers to dismiss incumbent employees, has an unemployment rate of about 10 percent in 2016. While being laid off from a job can be traumatic and frustrating, most U.S. workers in such situations do not remain unemployed for long periods. A number of those laid off in incidents cited in the media were offered jobs by the new contracting firms.

15) Some have attempted to use contracting out and layoffs by Disney and Southern California Edison to argue that Google, Facebook, Microsoft and other companies must not need to hire high-skilled foreign nationals. But these are separate issues and situations. A key reason H-1B visas are important is because they typically represent the only practical way for high-skilled foreign nationals, including international students, to be hired and work long-term in the United States, particularly since employment-based green cards are usually unavailable for years at a time. When companies recruit on U.S. college campuses, they discover that 77 percent of the full-time graduate students in electrical engineering and 71 percent in computer science are

international students. That means if U.S. companies were to ignore foreign nationals they would be conceding to competitors many of the potential new members of the labor force in key fields.

16) Immigration attorneys say using H-1B visas to perform temporary services, as many employees of contractors do in the United States, has long been a legal use of the visa category. Some have argued that “outsourcing” companies have been using up the supply of H-1B visas each year. However, the real problem is the low quota on such visas. In FY 2014, FY 2015, FY 2016 and FY 2017, tens of thousands more H-1B applications were received in the first week than could be accommodated by the 65,000 annual quota and 20,000 exemption for individuals who possess a master’s degree or higher from a U.S. university. For example, in FY 2016, 233,000 H-1B applications were filed in the first week alone – 148,000 more than the 85,000 limit. That means even if none of the 7 large Indian-based companies filed for H-1B visas (they used about 16,500 in FY 2014) it would have made little difference in the availability of H-1B visas.

17) The most controversial part of recent news stories has been the contention by laid-off employees that they were told to “train their replacements.” The contracting companies say this is not a case of employees “training their replacements” but rather gathering information to assist the transition from the old system to the new system. Moreover, the contractors’ employees are not replacements but assisting with the transition or fulfilling a separate function (i.e., learning about the systems, “keeping the lights on” and continuing certain operations while

the new IT or accounting system is put into place). This short-term information gathering does not mean a “one for one” replacement has taken place. In fact, the numbers generally do not match up

(i.e., in one case cited in the news, 8 people came on-site to gather information from 67 laid-off employees.)

However, even if the contracting companies are correct, the perception of the process has become a flashpoint in the debate and proven disturbing to laid off workers, which should warrant new consideration of how best to accomplish these transitions with minimal turmoil.

Recent news stories and statements by some elected officials have operated under the incorrect premises that contracting out by large companies is rare, happens primarily when a company with H-1B visa holders approaches a U.S. company, and is done so U.S. companies can rid themselves of long-time employees and replace them with less expensive foreigners on visas. This report shows far from being rare or focused on replacing long-time employees with temporary visa holders, contracting out for services is commonly done by Fortune 500 companies and has been going on for decades. Moreover, immigration policy is not important to a company’s decision to contract out certain non-core functions to improve its efficiency.

Notably, in a 400-page book critical of contracting out/outsourcing by David Weil, a current high-ranking Department of Labor official, the words “immigration” and “H-1B visa” do not even appear in the index. Companies contract out functions to save money but also to solve problems, to become more competitive and to focus on core competencies.

Changes in immigration policies are likely to lead to unintended consequences. Some members of Congress have cited the cases of Southern California Edison and others to propose legislation, such as S. 2394, that would come close to eliminating the ability of employers to hire high-skilled foreign nationals on H-1B visas. That would be a mistake. Productivity growth is vital to the U.S. economy and H-1B visa holders have played an important and positive role in such growth. “When we aggregate at the national level, inflows of foreign STEM workers explain between 30% and 50% of the aggregate productivity growth that took place in the United States between 1990 and 2010,” concluded an economic analysis of H-1B visas and U.S. productivity.⁵ The economists also found a positive impact on native wages: “We find that a 1 percentage point increase in the foreign STEM share of a city’s total employment increased the wage growth of native college-educated labor by about 7–8 percentage points.”⁶

There are provisions under current law to address violations of H-1B visas. The Department of Labor conducts investigations of companies after receiving a complaint from an aggrieved party or credible source, and in other circumstances. The Department of Labor maintains a list of companies it has investigated and disbarred from using H-1B visas.⁷ It is worth noting that none of the companies on the list are household names. U.S. Citizenship and Immigration Services also has conducted on-site inspections to ensure compliance with the law, including 30,000 such audits in FY 2010 and FY 2011.⁸

New visa restrictions would likely accelerate the pace of work moving outside the United States. For example, in addition to accomplishing transitions via the Web, contracting companies could hire a core of

U.S. workers to go to a client’s site, gather information, and prepare all the work to be sent outside the United States. That would place the work outside the reach of U.S. immigration law, as well as potentially other U.S. laws, such as federal tax law, and prevent the benefits of more of that work taking place here.

While we sympathize with anyone unfortunate enough to lose their job, Congress should be careful not to enact policies that would have the unintended consequence of harming other U.S. workers, including those who rely on company management to ensure the overall financial health and competitiveness of their company. It is not possible to formulate government policies that prevent layoffs in general without inflicting economic harm on the U.S. economy and the flexibility of U.S. labor markets. The global nature of business and the technological ease of moving work means that efforts to restrict the use or employment of H-1B visa holders inside the United States inevitably will mean more work will be conducted outside the United States.

The best approach is to let our markets function and avoid introducing new laws or regulations that would distort the market and send work outside the United States that would have stayed here. The U.S. immigration system is already highly regulated and, as experts on outsourcing note, company decisions on whether to contract out a function will not change even if H-1B visas are eliminated entirely. We should recognize that focusing on core competencies makes U.S. companies more competitive and better able to withstand economic storms in the global economy, which can help to keep the U.S. economy strong in the 21st century.

Introduction

Losing a job is a terrible thing. The anxiety and the uncertainty grips a person, causing regret and anger. In the case of individuals who lose their jobs at companies that contract with another company that employs individuals on temporary visas it becomes something else – front-page news.

Every year in America, approximately 20 million people lose their jobs involuntarily.⁹ Twenty million. In the JOLTS report, the U.S. Department of Labor uses the term *involuntary separations* to denote layoffs and discharges.¹⁰

Almost none of the job losses involving those 20 million people results in a news story. Yet job losses that appear connected to trade or immigration are controversial because, to put it simply, trade and immigration involve foreigners. And the idea of an American losing a job to a foreigner is more controversial than losing a job to another American – or losing a job because

of larger economic forces, industry trends or competitive financial pressures.

However, if one examines the dozen or so cases in the past 5 years where U.S. worker job losses have been connected in the media to a contractor that employs visa holders it would appear critics lack evidence on a key question: *Would these employees have kept their jobs if U.S. immigration law prohibited contractors from employing visa holders?* The evidence suggests the employees would *not* have kept their jobs. Decisions to contract out functions are driven by both internal and external factors, such as competitive pressures, financial or management difficulties that highlight the need for change, and common industry practices that have nothing to do with immigration.

The question of whether these individuals would have kept their jobs is important, since those arguing for changes in the law make clear they believe immigration policy – and immigration policy alone – is the reason these workers lost these jobs. There is little nuance in the argument on this issue, as a letter from a group of senators stated, “A number of U.S. employers, including some large, well-known, publicly-traded corporations, have reportedly laid off thousands of American workers and replaced them with H-1B visa holders.”¹¹

No one questions that the companies cited in news stories decided against keeping certain functions or services in-house and that the contractors that received the contract employed some number of visa holders.

Table 1 Involuntary Separations (Layoffs/Discharges) in the U.S. Economy: 2011 to 2015	
Year	Number of Involuntary Separations (Layoffs/Discharges) Annually in America
2015	20,942,000
2014	20,420,000
2013	19,903,000
2012	20,952,000
2011	20,756,000

Source: U.S. Department of Labor Job Openings and Labor Turnover Survey.

The real question is: Did factors exist that make it likely that the companies cited in the media would still have decided to contract out functions even if the contractors they chose used all U.S. workers? If other logical factors or events drove the decision-making process, then blaming U.S. immigration policy would be an attempt to use the unfortunate job losses of workers for political or other ends.

What are some of the other factors that would make it likely for these companies – indeed any companies – to contract out for services? Examining cases in the news and the existing literature on contracting out, in addition to interviews with experts in the business, reveals a number of these factors:

- Competitive pressures in the marketplace that compel companies to focus on core competencies and contract out non-core functions, including accounting and information technology.
- Financial and management difficulties within a company that lead to decisions to change the way of doing business, including reducing costs or turning to companies that specialize in developing new financial or information technology systems.
- The ability to use an outside, independent advisor that can assist the company in assessing needs, preparing requests for proposals, and evaluating bids and contractors to ensure company objectives on technological transformation are met.

The real question is: Did factors exist that make it likely that the companies cited in the media would still have decided to contract out functions even if the contractors they chose used all U.S. workers? If other logical factors or events drove the decision-making process, then blaming U.S. immigration policy would be an attempt to use the unfortunate job losses of workers for political or other ends.

The Process and Considerations When U.S. Companies Contract Out Services

The gap between what some critics seem to believe is the process companies use when contracting out a function and what happens in the real world is sometimes the size of the Grand Canyon. Some policymakers have expressed the view that typically a contracting company will hire a large number of visa holders and then approach large U.S. companies and make a sales pitch to them along the lines of: “We have all these workers and we can provide them to you cheaply to do the same jobs, so then you can lay off all of your American workers.”

Several experts in the field said that is not at all how the process for awarding contracts works. In reality, the process for awarding, large IT outsourcing contracts typically is quite lengthy and includes a request for proposal, presentations, interviews and sometimes as many as 10 to 20 initial bidders. Moreover, it rarely, if ever, is initiated by the contracting companies themselves, which are typically not contacted until a decision is made to outsource the function (and possibly lay off workers). It is important for policymakers, members of the press and the general public to understand how and why companies seek out firms to provide services for non-core business functions – and that blaming immigration policy for these company decisions can often make as much sense as blaming the weather.

To gain a better understanding of the company decision-making process, policymakers should consider consulting with third party advisors. These are the firms to which large U.S. companies turn to receive impartial advice in deciding whether contracting out is a good choice for their businesses. These advisors help articulate objectives, establish a process for evaluating potential service providers, and, if it reaches that stage, assist in negotiating and overseeing contracts.

These advisors include firms well-known in the business world, such as Gartner, Everest Group and Pace Harmon. After examining Congressional hearings and statements by elected officials, it is unclear if any third party advisors have been consulted to explain the process large companies use when deciding whether and how to contract out services. If such advisors had been consulted, they would have provided a more accurate and nuanced picture of how and why companies make these decisions.

Interviews conducted with 10 of the leading third party advisors on outsourcing and management consulting paint a consistent portrait of how contracting works in practice – one much different and, it turns out, more mundane than recent dramatic depictions of large companies contracting out certain in-house functions.

The Typical Process: Requests for Proposals and Competitive Bids

“A request for proposal is standard industry practice for new outsourcing engagements,” according to Jeff Augustin, a managing director at Alsbridge, which has advised approximately 60 percent of the Fortune 500.¹² Augustin said that, as a general rule, all Fortune 500 companies today contract out services for non-core functions. The existence of requests for proposals (RFPs) is important in the context of recent controversies over immigration, since it means the typical process involves soliciting multiple bids. A company using requests for proposals and competitive bidding would not know ahead of time - particularly at the start of the process - which contractor it might use or the visa status of any employees the contractor it chooses might employ.

“Typically a client will outline the scope of operations involved, its objectives and requirements and vendors will respond,” notes Augustin. “The responses are short-listed to 2 or 3 finalists who then go through a rigorous review based on a wide range of criteria, including price, technology and process management expertise, skills, cultural fit, transition timing and other factors.”¹³

Rich Kabrt, a partner at the Everest Group, explains that the process for large U.S. companies often begins with seeking advice from firms like his (and others interviewed for this report). “Typically companies do compete [put out for bid] this work often with the expert assistance of a sourcing advisory firm. It can start with a request for information or RFI (10 to 20 firms) to see who might be appropriate and then short-list to a smaller

number of firms to receive a request for proposal or RFP (4 to 8 firms). Depending upon the complexity of service, the RFP can then lead to follow-on rounds of solution and contracting refinement with a further down-selected group (2 to 3 firms) to ensure the best fit long-term value solution.”¹⁴

Competitive bidding is standard practice. “Companies that are embarking on outsourcing IT (information technology) or business process functions typically go through a competitive bid process,” confirms Steven Kirz, managing director at Pace Harmon, a management consulting firm. “When conducted properly, the company doesn’t know which provider will ultimately be selected. The premise of conducting a competitive procurement is to identify the most qualified provider to meet a company’s specific needs and requirements.”¹⁵

In fact, Kirz notes, when the process starts, the U.S. company does not even know for certain it will contract out the function. “To begin the process, a company first performs an assessment of its needs and requirements from a business and technical standpoint,” according to Kirz. “Given this information, the company then compares the anticipated result of the procurement with an outsourcing provider engagement versus handling it with internal resources. Based on this analysis... if the decision is made to outsource the function, then the company proceeds with creating an RFP [Request For Proposal]. The RFP is put out to bid, the most qualified provider is selected, and negotiations commence.”¹⁶

Far from the explanation suggested by some elected officials, namely that contracting decisions result from solicitations by contractors offering “cheaper labor,” large U.S. companies take a much more methodical approach. “Decisions on what to retain and what to outsource/offshore, whether to do-it-yourself or find a partner, which locations to pick, and other related aspects

are strategic in nature, since their outcomes have a long-term impact on the business,” explains Hemant Puthli, partner and senior vice president at the Neo Group. “Leading companies typically arrive at such decisions through a formal, structured process that is based on hard data and overlaid with human assessment by experienced experts.¹⁷



Contracting Out: Benefits and Primary Motivations

Why do companies contract out a function, whether information technology, accounting or others that had been performed in-house? Experts in the field cite focusing on core competencies as a primary factor. “All outsourcing decisions are made with an overarching theme of core vs. non-core, or a discussion on if the function is a core competency,” notes Steve Hall, a partner at Information Services Group (ISG), an advisory firm.¹⁸ Kevin S. Parikh, global CEO of Avasant, concurs: “Focusing on core business functions is one of the primary reasons firms seek to contract with third party service providers.”¹⁹

Parikh cites other factors for contracting out functions, including “increased flexibility, transforming services to meet new market standards, access to sophisticated technology and service delivery platforms and access to global footprint and knowledge, world class capabilities and best practices, and others.”²⁰

Reducing costs, of course, is an important motivator for contracting out, but it is not the only one and not in the perhaps simplified way argued by some critics. Cost savings are often the result of innovation and using new technology, platforms or processes to replace the way work was done previously. “Although cost reduction is generally one of the primary triggers for contracting out a function, mature firms are now also seeking innovation and digital transformation to stay competitive and respond to the changing requirements of their customers,” notes Parikh.

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“Outsourcing also enables the management to free up internal resources for strategic initiatives that drive their core business functions while business-as-usual processes are better delivered by specialist service providers.”²¹

Steve Hall of Information Services Group explains how cost today plays only a partial role in outsourcing/contracting out. “Cost was certainly the driver in the early days of outsourcing, but as the market has matured, the cost play has become less important,” notes Hall. “In most cases, companies outsource a function because it allows them to free up resources and capital on more critical functions.”²²

Table 2 What Do Companies Hope to Accomplish by Contracting Out?	
Desired Capabilities Obtained Through Sourcing Strategy	Percent of Companies Saying Critical or Very Important
Access to Labor with Specialized Skills	100%
Ability to Meet Compliance Requirements	75%
Ability to Deliver Timely, High-Quality Business Analytics	75%
Ability to Introduce New and Innovative Technology Tools	57%

Source: Hackett Group Sourcing Study, 2013, responses of “top performers.”

Even though cost reduction is not the only motivation, the potential for significant savings that can be used for more productive purposes within the company is enticing. “Cost savings can range from 15 percent at a minimum to as high as 70 percent,” according to Rich Kabrt of the Everest Group. “U.S. companies’ global competitiveness is enhanced by well-designed and executed outsourcing in selective areas that free up resources and funds to invest in the core competencies that drive growth and value. The level of skilled resources needed over the past decade cannot have been fully met domestically [in the U.S.]”²³

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The 15 percent to 70 percent estimate in cost savings cited by the Everest Group fits within the estimates of other firms. The advisory group Alsbridge concludes: “Cost savings benefits from outsourcing for an individual organization can vary from 30 percent to 40 percent. Now, with automation, we’re seeing additional cost reductions of up to 50 percent and more.”²⁴ Pace Harmon’s estimate: “We’re currently seeing enterprises saving 30 to 50 percent in the first year when clients competitively procure what has already been outsourced in IT infrastructure services, amounting to millions of dollars in savings.”²⁵ These savings can be seen not only with offshore solutions but also on contracting out for cloud services to domestic providers, including Google and Amazon.²⁶

H-1B Visas: No Relevant Impact on the Decision to Contract Out

A strong misimpression has emerged from news stories that companies choose to contract out functions primarily as a way to lay off long-time workers and replace them with cheaper foreign workers on H-1B temporary visas. Third party advisors get paid based on their expertise and make a variety of recommendations on whether to contract out a function and, if so, to which firm. In other words, they do not have a self-interest or “dog in the fight” over immigration policy. As part of this research, third party advisors were asked whether or not U.S. companies hire contractors that employ H-1B visa holders in order to lay off a company’s incumbent employees, as has been alleged.

“That’s absolutely not the case,” according to Jeff Augustin, managing director, Alsbridge. “In our experience, the H-1B visa issue plays a very minor role in outsourcing strategies, much less in decisions to lay off workers. Where we see visa holders playing a role is during the transition phase from one service provider to another or from an in-house operation to an outsourced service provider.” In other words, when H-1B visa holders are used by a contractor it is often as part of the “bridge” from the old way of operating to the new approach adopted by the vendor hired by the U.S. company. “This transition period is critical to the success of an outsourcing initiative, as a lot of moving parts have to be put in place in a very tight timeframe,” explains Augustin. “If you don’t get it right the whole business case for outsourcing in the first place is

seriously compromised. As a result, many providers will bring in H-1B visa holders with specialized skills and experience to help manage the transition.”²⁷

Other experts echo Augustin, labeling as untrue the notion that companies use immigration policy as a way to rid themselves of incumbent employees. “These stereotypes are completely false,” according to Steve Hall with Information Services Group. “Enterprise buyers of outsourcing services are business savvy and risk averse. The visa rules have been scrutinized for the past 10-plus years and are well understood by most enterprises who follow the well-defined rules. Large outsourcing engagements are strategic in nature and are not based on lower on-site rates for visa holders. These deals are typically delivered in a managed service model, meaning that clients pay for output, not necessarily the number of resources or the allocation of resources on-site or offshore.”²⁸

Despite the attention offshore transactions receive, much contracting is purely domestic. “In our experience a significant amount of contracting happens only within the U.S.,” notes Steven Kirz of Pace Harmon. “By some measures, in some functions, this is increasing quickly.”²⁹ According to Jim O’Connor, a principal at The Hackett Group, “From a definition perspective, it is important to understand that outsourcing does not equal offshoring.”³⁰ A new trend within the United States is “rural sourcing,” notes Pushkar Soman, a senior consultant at

Quint Wellington Redwood, with companies identifying “locations within the U.S. where costs are relatively low but typical offshoring challenges in culture, language, and security do not apply.”³¹

Diversity in delivery models, including work that stays onshore, attracts little public attention. “As outsourcing has grown, there are many different delivery models that include offshore, nearshore, and onshore,” explains Steve Hall. “Many of the traditional offshore service providers, such as Tata Consulting Services (TCS), Infosys, Wipro, Cognizant, etc., have built large capabilities in the U.S. market to deliver services. Despite the rhetoric in the press regarding H-1B visa abuse, many of these firms employ thousands of U.S. citizens to develop software, manage enterprise infrastructure, or perform business process outsourcing functions.”³²

Before deciding whether to contract out a function, do companies even know in advance something as specific as the composition of the vendor’s workforce, including whether it includes visa holders? “I don’t see companies getting to that level of detail on the vendor’s delivery model,” according to Kris A. Doering, a research director at Gartner. “Companies are very focused on industry trends and what their competitors are doing. If their industry is contracting or focused on low cost, then those companies are typically very focused on cost savings and are willing to outsource (offshore) more of their functions to save money. Almost all companies are interested in reducing the cost of their IT services.”³³

In sum, given the way companies decide whether to contract out a function, the available evidence indicates immigration policy is not relevant in the decision to keep functions in-house or to contract with a vendor to provide the services.

“I would say cutting off the H-1B visa program wouldn’t really impact outsourcing overall, as the H-1B visa holders have a limited and specialized role in the outsourcing process (specifically, in pushing through the transition phase),” concludes Alex Kozlov, director of content at Alsbridge.

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Cloud Computing, Automation and Robotics, Not Immigration, Have Big Impact on Employment and the Future of Contracting Out Functions

It can take many years for those outside of an industry to catch up on technological changes and their impact. That is the case today with cloud computing, automation and robotics. While policymakers seem fixated on immigration, which economic studies show have little to no impact on the unemployment rate of natives, new technology is a far more “disrupting” force in the workplace.

In cloud computing, explains Alex Kozlov of Alsbridge, rather than a physical data center for a company’s data, or a computer for an individual’s data, the cloud model allows data to “move around” a network of internet-hosted servers while responding to peaks and valleys in demand. “Cloud is changing outsourcing by changing the competitive dynamic and bringing in new players like Amazon into the mix,” according to Kozlov. “Traditional outsourcers are responding with their own cloud services. Cloud is also changing outsourcing contracting models in terms of how resources are allocated (traditional data center versus space on the cloud network).”³⁵

Kevin S. Parikh of Avasant argues that cloud computing has turned into a game-changer for many businesses: “Organizations are leveraging cloud’s elastic infrastructure to reduce their upfront investment and scale cost-effectively. Since cloud-based

applications are standardized, it reduces the need for implementation and customization. Service providers are partnering with cloud platform and application vendors to offer bundled solutions. This is changing the way organizations engage with third party service providers. Cloud computing is enabling organizations to differentiate and innovate, and this is creating new and disruptive ways for contracting out functions and services.”³⁶

Alex Kozlov notes the relationship between automation and cloud computing. “There is some connection between cloud and automation, as cloud enables more and more data to be stored and accessed, and automation makes it easier and faster to process and analyze data. So this is leading to rapid advances in big data/analytics, such as detecting buying patterns/preferences for retailers, or impacts of wellness programs for healthcare providers/payers.”³⁷

Automation allows the digitalization of tasks and functions that traditionally have been performed by humans. “The tasks that are being automated are becoming increasingly sophisticated and include areas such as monitoring applications and computer systems to detect problems, managing network traffic and resolving IT problems,” explains Kozlov. “In terms of the impact on outsourcing, this is the real game changer, because the business model is changing...

to a model where you have a virtual robot who does the same job 24x7x365 – with minimal start-up and maintenance cost and zero wages to be paid. In other words, no matter how low the wages, people can't compete."³⁸ According to Brad Pickar, partner and senior vice president, Neo Group, "Clients will increasingly demand that their outsourcing vendors commit to automation goals and it will become a requirement during vendor selection processes. In some cases, it will eliminate the need to deal with a vendor at all. That's why the vendors are investing heavily in building up capabilities in this area."³⁹

The implications for contracting out in general and "offshoring" in particular are profound. "Businesses are rethinking their whole approach to offshoring. Overall, this trend is forcing all the outsourcing providers (both U.S.-based and Indian) to fundamentally change their business models – rather than putting lots of skilled bodies on the job in a cost-effective manner in an offshore location, they're having to figure out how to help clients take advantage of automation and put these smart robots into place," notes Jeff Augustin (Alsbridge).⁴⁰

Steve Hall of Information Services Group concurs that we should continue to expect big changes in the workplace due to technology. "Automation and cloud will play a tremendous role in the future of outsourcing," he said. "We are witnessing significant investments by many of the large

"Automation and cloud will play a tremendous role in the future of outsourcing," he said. "We are witnessing significant investments by many of the large outsource providers... in the development of automation solutions. We are already seeing business cases that eliminate 40 percent or more of the labor associated with many functions based on a high degree of automation."

outsource providers... in the development of automation solutions. We are already seeing business cases that eliminate 40 percent or more of the labor associated with many functions based on a high degree of automation. When machine learning is added to the equation, we will see even more automation of the IT outsourcing market as machines are virtually swapped to eliminate a potential failure." He notes that many of these changes have benefited U.S. companies, since Amazon, Google, and Microsoft cloud-based solutions "are growing at a tremendous rate."⁴¹

Increasingly Common for Companies to Focus on Core Competencies

For another perspective on contracting out, we can turn to David Weil. Weil currently holds an influential government post as Administrator of the Wage and Hour Division at the U.S. Department of Labor and is the author of *The Fissured Workplace*, which he wrote when he was a professor of economics at the Boston University School of Management. Weil explains the benefits of contracting out for companies but also believes it carries costs for employees and limits the ability of labor unions to attract new members.

For years, U.S. companies have been focusing on core competencies and contracting out functions unrelated to their primary product or service lines. “In focusing on core competencies, businesses seek to expand their margins and their markets, thereby improving the profitability

of their operations,” writes Weil. “At the same time, by shedding non-essential activities, they seek to push out activities that would be more costly if maintained within the boundaries of the firm.”⁴²

It is significant that in Weil’s 400-page book on contracting out the words “immigration” or “H-1B visa” do not even appear in the index. The only reference to immigration policy in the book relates to J-1 visas for youth summer employment, citing the controversy over such work at a Hershey’s packing plant.⁴³ The absence of much or any discussion of immigration in Weil’s books lends credence to the view, supported by much evidence, that contracting out services is not an immigration issue but primarily about companies deciding to focus on core activities.



Contracting Out For Services Has Been Going On a Long Time

How did contracting out for services become such an important part of the American business landscape? David Weil points primarily to new technology and pressure from shareholders and investors to become more efficient. “Technological developments increasingly allow businesses to focus on core competencies while shedding activities not central to the firm’s operation. With the falling cost of coordination resulting from new information and communication technologies, productive reconfiguring of the boundaries of companies and entire industries naturally occurs,” writes Weil.⁴⁴

Starting in the 1980s and early 1990s, investors, including private equity companies, had a simple message: “Firms should focus their attention and their resources on a set of core competencies that represented distinctive capabilities and sources of comparative advantage in the markets in which they competed.”⁴⁵ Weil notes that “Anything that did not directly support those core competencies would be carefully evaluated as to whether it should 1) remain part of the business at all; 2) be restructured to be done more efficiently internally; or 3) be outsourced to some other party that could provide the necessary activity externally at lower cost. In essence, the message was, Find your distinctive niche and stick to it. Then shed everything else.”⁴⁶

Apple is an example of a company that decided to focus on core competencies and experienced spectacular results, with

its stock price increasing from \$7 in 2003 to over \$600 in less than a decade.⁴⁷ The overall market capitalization of Apple increased by an extraordinary \$600 billion between 1995 and 2015. By 2012, according to Weil, Apple employed 63,000 workers directly, while relying on 750,000 workers employed by contractors of Apple to make, assemble and distribute Apple products.⁴⁸

Over the past 15 years, the “search for core competencies” has resulted in downsizing conglomerates and companies to a more manageable size and focus. More recently, this “search for core competencies” has led to shedding functions such as human resources, information technology services, and accounting.⁴⁹

While David Weil discusses problems that can arise for workers, he also acknowledges significant benefits when companies today focus on core competencies. “There are indeed positive aspects of the reorganization of production for companies, investors, and consumers, and finding new ways to organize production can enhance social welfare,” writes Weil. Focusing on core competencies and the benefits of specialization, facilitated by flexible organization forms, can lead to the development of new and better products available at lower prices.”⁵⁰

Companies of Various Sizes Contract Out Services and for Reasons Unrelated to Immigration

Domestic outsourcing or contracting out for services has increased across industries, including computer services. A paper published by the National Bureau of Economic Research concluded, “A variety of evidence has pointed to significant growth in domestic contracting out over the last two decades... yet, the phenomenon is not well documented.” The researchers found, “In the other four occupations—janitors, security guards, computer occupations, and accountants—we look for growth in the share of workers in business services as an indicator of growth in contracting out in that occupation, and we find evidence of growth in contracting out in two. According to OES [Occupational Employment Statistics] data, the share of workers in computer occupations employed in business services increased dramatically, from 39 percent in 1990 to over 50 percent a decade later.”⁵¹

The Society for Human Resource Management (SHRM) has surveyed its members on the extent to which they contract out services. If immigration critics are correct, then we should find that companies rarely contract out functions, except when immigration policy offers the opportunity to do so. But according to various surveys over the years, employers have contracted out for many functions, including even the recruitment of employees.

A September 2015 SHRM survey found, “Nearly two-thirds of organizations

(64%) said they outsourced at least some recruitment activities. More than one-half (55%) indicated some recruitment was partially outsourced – meaning, the organization retained some control over the outsourced function (for example, it shared access to information with the vendor).”⁵² The survey found (large) companies with at least 500 employees were much more likely to contract out recruitment to an outside vendor or contractor.

Why did the companies contract out recruitment? “The top reason for outsourcing recruitment was the speed of hire/need to hire quickly (49%), followed by gaining access to the vendor’s talent/expertise (36%),” according to the survey. “One out of five organizations said that their company/industry had difficulty attracting specific types of talent (20%) or wanted to allow HR staff to focus more on strategy (19%).”⁵³

Recruitment is only one function that employers contract out. Just within the human resources department of companies, the variety of functions that are now contracted out is surprising. According to another SHRM survey, 73 percent of employers contracted out background checks, 67 percent contracted out flexible spending account administration, 65 percent employee assistance/counseling, 60 percent health care benefits administration and between 55 percent to 46 percent contracted out a variety of functions that included payroll administration, retirement

benefits administration and pension benefits administration.⁵⁴

That survey was completed in 2004 and a follow-up SHRM survey in 2008 found more employers expecting to contract out for services. In some cases, employers contract out an entire function, while at other times part of the function is retained in-house. The 2008 survey asked employers whether they expected to increase or decrease the contracting out of human resources functions over the next 5 years: 33 percent expected it to increase, 17 percent expected it to decrease, and 50 percent said it would remain about the same.⁵⁵

Table 3 Percentage of Employers Contracting Out Human Resources Functions	
Function	Percentage of Employers Contracting Out Function
Background/Criminal Background Checks	73%
Flexible Spending Account Administration	67%
Employee Assistance/ Counseling	65%
Health Care Benefits Administration	60%
COBRA	55%
Pension Benefits Administration	55%
Temporary Staffing	54%
Payroll Administration	48%
Retirement Benefits Administration	46%

Source: Society for Human Resources Management; 2004 survey. Respondents answered “outsource completely” or “outsource partially.”

Examining Cases in the News

Recently a number of news stories have focused on incidents when companies contracted out work and laid off incumbent employees. The cases received attention after it was found the contractor had employees working on temporary visas. The central inference in these stories, which became a direct complaint in the hands of some officeholders, is that the visa holders caused the layoffs.

The following is an examination of a number of the cases that have received media attention due to the presence of foreign nationals. The key questions to keep in mind while reviewing incidents cited in the media are:

- 1) Did other factors exist that make it likely the company would have decided to contract out the work whether or not the contractor employed temporary visa holders?
- 2) Did the company use a competitive bid process that would make it unlikely to know when it decided to start the process of contracting out work what the make-up of the workforce of the contractor it chose would be?
- 3) Is it common for similar companies to contract out this type of work, meaning immigration was unlikely to be the driving force in the decision-making process?
- 4) What is the evidence the incumbent employees would have kept their jobs absent the existence of a contractor that employed individuals on temporary visas?



Southern California Edison: Was a Shooting and the Consultant's Report that Followed the Chief Motivation for IT Outsourcing?

In 2014, a utility company, Southern California Edison (SCE), began laying off workers in its information technology (IT) department and offering others voluntary severance agreements. "The Southland's largest utility said it is laying off about 400 information technology employees, with an additional 100 leaving voluntarily," reported the *Los Angeles Times*. "The layoffs are necessary, the company said, to stay competitive."⁵⁶

The controversy arose when laid-off employees reported that the contractors chosen by Southern California Edison employed foreign nationals on temporary visas. As in other cases, the news (and editorial) coverage implied that Southern California Edison decided to contract out for a single reason – U.S. immigration policy. In essence, the argument went, that a large U.S. company, in this case, a utility company, discovered a provision in the immigration code and used it to lay off a large number of workers and replace them with "cheaper" foreigners. A simple matter. Case closed. Little of the coverage hinted at other factors in play.

A review of recent history at Southern California Edison indicates two important facts that cast doubt on the narrative that what drove the company's decision was a desire to use foreign workers to lay off and replace long-time employees. First, Southern California Edison's information technology department had experienced significant

problems that the company needed to address, with contracting out to a new firm considered a logical option. Second, the company did not simply lay off and replace the workers in question. Instead, Southern California Edison used an outside advisor, a law firm, that utilized a competitive bid process before the company selected two contractors. With a competitive bid process being used, it is unclear how Southern California Edison could have known in advance which company would have received the contract or the composition of any contractor's workforce.

In December 2011, tragedy and violence struck the information technology department at Southern California Edison. "On Friday afternoon, December 16, 2011 in the workplace at Southern California Edison's (SCE) Rivergrade [Irwindale] location, an employee fatally shot two supervisors, and wounded two others before taking his own life," begins a report by a management consulting team hired by SCE after the incident.⁵⁷

The confidential report produced by the management consulting team sheds light on Southern California Edison's later decision to contract out significant parts of its information technology functions. "In the aftermath of this tragic event, SCE engaged Incident Management Team (IMT), an independent consulting and training company

with internationally renowned expertise in crisis response, threat assessment and violence prevention programs, organizational change and leadership development. ... The purpose and scope of the initial sixty (60) day phase of engagement was to conduct a comprehensive assessment of the workplace climate and culture within the Information Technology & Business Integration (IT&BI) organization, and to make recommendations to build upon strengths and diminish risks in the workplace.”⁵⁸

In crafting its recommendation, Incident Management Team conducted “group and individual meetings with 725 employees, contractors and contingent workers, managers, directors and executives” at various SCE locations and reviewed other materials, including survey results and internal documents.⁵⁹

The 24-page report paints a disturbing portrait of the management of the information technology department at Southern California Edison. “An analysis of the information identified key issues which include workplace climate and culture concerns and stressors related primarily to a fundamental lack of leadership in many areas, and resulting in loss of trust, lack of respect, fear of retaliation, inefficient decision-making processes, poor communication, lack of work/life balance, abusive management styles, lack of management accountability, perceived absence of fairness and a shortage of recognition.”⁶⁰

The problems reported were so deep-rooted it is difficult to imagine simple fixes to address the underlying issues. “There are managers and executives within IT&BI [Information Technology & Business Integration] who appear to be autocratic, overly authoritarian and draconian in their approach.”

“Employees share experiences of humiliation in front of other employees, verbal abuse, reprisals and favoritism. Other managers and supervisors are absent, and provide little direction, support or mentoring,” according to the report. “When there are problems or failures, managers reportedly blame downward and are not held accountable nor do they take responsibility. Employees reported a pattern of managers punishing and scapegoating subordinates instead of working together to ameliorate the problem. This creates an ever-widening chasm between managers and subordinates, and sends issues ‘underground’ to avoid detection.”⁶¹

Anyone reading the report would conclude that, in general, the managers in the information technology department at Southern California Edison were not doing a good job. “Employees perceive managers to be more concerned about how they ‘look’ from above, and less concerned about how they are viewed by their subordinates,” the report noted. “This fosters an unhealthy culture and climate by sending a message to employees that it is more important to focus on how things look from the top than how they actually are down below.”⁶²

Computerworld, which closely covered the Southern California Edison situation, posted the Incident Management Team report online and quoted SCE employees who linked the report to the decision to outsource parts of the information technology function. “Some of the SCE employees say the outsourcing move is linked to a 2012 report that found fault with the IT management culture,” according to *Computerworld*. “⁶³

Computerworld reported, “Prior to the outsourcing agreements, the SCE employees said there were a series of layoffs, including managers.”⁶⁴

Southern California Edison decided to go beyond laying off the managers, which means if the problems were caused primarily by poor management, then long-time workers likely would have viewed more extensive changes as inappropriate. The Hackett Group found 70 percent of companies that outsourced a function cited a “need to change organizational culture.”⁶⁵ The management consulting team report painted such a distressing picture in the IT department at Southern California Edison that executives may have believed the best choice was to contract out much of the function, whether or not this was fair to the employees who worked under those managers.

Given the dysfunction cited in the consulting team’s report, SCE executives must have questioned their own ability to choose new managers who would perform better than the previous managers criticized so roundly in the consultant’s report. What assurance would Southern California Edison executives have that the new managers would perform well? The decision was to jettison much of this (non-core) function and place it in the hands of an outside contractor that specialized in this area.

Once that decision was made, it sealed the fate of the employees who would be laid off in the information technology department. At that point, Southern California Edison executives chose to contract out much of the IT work and lay off or offer voluntary severance agreements to employees the company believed were no longer needed due to the new contract.

SCE did not award a sole-source contract without bid, a fact that undercuts the argument that immigration policy led to the decision to contract out the function. Instead, as noted earlier, the company tasked a law firm to solicit bids from at least 8 companies, including U.S. companies, and those businesses competed for the contract. This became news only after it was discovered that the two companies who won the contract employed some number of employees on temporary visas. As related above, there appears to be considerable evidence that the fate of those SCE employees who lost their jobs had been decided a long time before the contracts were awarded.

The *Los Angeles Times*, particularly its columnists and editorial page, was a leading critic of Southern California Edison. Ironically, in 2016, *Computerworld* reported that Tribune Publishing, which owns the *Los Angeles Times*, “is laying off as many as 200 IT employees as it shifts work overseas.” A Tribune Publishing spokesperson told *Computerworld*: “We have made the strategic decision to outsource key functions of our legacy information technology department to create a more agile operating environment and to drive our overall business transformation. This decision will allow us to better serve our customers, improve our systems and capabilities and create more opportunity for innovation.”⁶⁶

Technology Overhaul Leads to Controversy at Disney

Disney is another company whose contracting out of information technology services resulted in front page news. Similar to Southern California Edison, a decision that appeared to be unrelated to immigration policy soon became an “immigration story” for Disney, with news stories implying the only reason for Disney’s restructuring, decision to contract out and the subsequent layoffs had been due to the immigration status of its contractor’s employees.

The news reports did not start out that way. On October 28, 2014, the *Orlando Sentinel* reported a story with the headline: “Disney’s Technology Group Undergoing Restructuring.” The story began, “Disney’s global technology group for its parks-and-resorts division is undergoing a sweeping reorganization that is expected to result in some employees losing their jobs.” The article noted that as part of the reorganization the company decided to lay off two long-serving IT vice presidents and replaced them with “two other vice presidents with different skill sets.”⁶⁷

The article explained the change as Disney shifting its information technology focus away from primarily maintenance into developing new ways of using technology, noting, “Less than 30 percent of the technology staff works in roles Disney considers ‘new capabilities development.’ In the new organization, that will become 65 percent.” According to an expert cited in the article, this was not surprising.

“That says you’re moving people away from maintenance into development and you want to get into a type of situation where you’re really kind of reinventing the way you’re managing your technology,” according to Robert Niles, publisher of ThemeParkInsider.com.⁶⁸

The *Orlando Sentinel* article explained the business rationale for the moves and, in a matter-of-fact manner, reported that contracting out was part of the restructuring. “Disney is also outsourcing additional information technology jobs,” according to the article. “Most of the positions affected are in Orlando. Some are in Anaheim, Calif., where the company has Disneyland.” The *Orlando Sentinel* then added, “Outsourcing work is typical in information technology, said Duncan Dickson, an instructor with the University of Central Florida’s Rosen College of Hospitality Management.”⁶⁹

Eight months later, what was once a boring news item about a company restructuring turned into a major news story about a big company replacing Americans with foreigners. “About 250 Disney employees were told in late October that they would be laid off,” reported the *New York Times* in a front page news story in June 2015. “Many of their jobs were transferred to immigrants on temporary visas for highly skilled technical workers, who were brought in by an outsourcing firm based in India. Over the next three months, some Disney employees were required to train their replacements to do the jobs they had lost.”⁷⁰

However, the *Los Angeles Times* reported that although “Disney eliminated 250 technology positions at the Walt Disney World resort in Orlando, Fla. and replaced them with 320 new roles. Some 120 workers were rehired, 40 retired or moved to other companies and 90 took severance packages.”⁷¹ Disney also said that after the layoffs and other changes the company “had a net gain of 70 tech jobs.” The company also argued that it has created nearly 30,000 jobs in the United States over the past decade.⁷² Due to the controversy in Orlando over the contracting firm employing individuals on temporary visas, Disney rescinded a planned layoff of 30 information technology professionals in New York and Los Angeles.⁷³

Disney employees were caught in the middle of a company decision that had only a tangential relationship to immigration. The two vice presidents replaced in Orlando were not replaced by foreign nationals, but the hiring of two new vice presidents signaled a change in direction for Disney. The contracting company chosen by Disney employed people on temporary visas but by all indications Disney’s restructuring decision was 1) consistent with contracting out done by other companies across the country and in their industry and 2) consistent with Disney’s past efforts to structure its technology divisions.

Accounting and Finance Functions Contracted Out Frequently

If companies generally never contracted out finance and accounting functions, then a case could be made that immigration policy led to the incidents in the news of contracting out such functions. However, a significant amount of evidence shows that companies frequently contract out or outsource their finance and accounting functions. “Finance and accounting was one of the first processes that companies outsourced, and the practice continues to boom,” writes Joe Mullich in *ForbesBrandvoice*.⁷⁴

Mullich reports on a study of 150 companies in the United States, Canada and the United Kingdom by Ovum research. “Driving efficiency is a high priority for CFOs [chief financial officers] who want to outsource finance and accounting functions,” notes Mullich. “Most survey respondents saw the main strategic aim of the accounting department as delivering efficiencies, whether that is within the department itself or across the company as a whole.”⁷⁵ He notes CFOs of large companies concentrate on outsourcing to improve “far-flung global operations,”⁷⁶ while smaller companies have become more open to outsourcing because the companies they contract with offer solutions to their problems.

“Many companies don’t realize going in that they manage an outsourced provider more stringently than their in-house resources were managed,” according to Jag Dalal of the International Association of Outsourcing Professionals. “Outsourcing outcomes are more likely to use clear metrics, such as

Understanding that contracting out accounting functions is a widespread, long-standing practice – and done for legitimate business reasons – provides context to news reports that may leave the impression such business agreements are both controversial and only take place when a contractor employs visa holders. It would be more accurate to say that contracting out only becomes controversial and, therefore, a news story when a foreigner or visa holder is spotted at the company’s offices.

savings and service-level achievement. That allows a company to have continuous improvement in their accounting and finance operation, while the company itself can focus limited resources on its core competencies.”⁷⁷

Understanding that contracting out accounting functions is a widespread, long-standing practice – and done for legitimate business reasons – provides context to news reports that may leave the impression such business agreements are both controversial and only take place when a contractor employs visa holders. It would be more accurate to say that contracting out only

becomes controversial and, therefore, a news story when a foreigner or visa holder is spotted at the company's offices.

That proved to be the case at Toys “R” Us, New York Life and Cengage, which all contracted out accounting functions – and all appeared in news stories because visa holders worked for the contractors. A front page *New York Times* article (September 29, 2015) reported that Toys “R” Us laid off 67 people, “mainly in accounting,” and contracted out the functions to a company that would perform the work in India. There was no allegation of a one-for-one replacement, whereby each worker directly replaces another worker who was laid off, since the article cited only 8 workers on visas from Tata Consultancy Services (TCS) who came on-site to work. There also was no allegation of U.S. workers “training replacements,” but rather of extensive “shadowing.” The *New York Times* reported a worker on a temporary visa “studied and recorded [an American] accountant’s every keystroke, taking screen shots of her computer and detailed notes on how she issued payments for toys sold in the company’s megastores.”⁷⁸ Toys “R” Us used an outside advisory firm as part of the business review process.

The same *New York Times* article reported on the case of New York Life. The company laid off 300 accounting and information technology workers. Given the scope of New York Life’s overhaul, it would be difficult to say the company did this because of something in the U.S. immigration code. “The layoffs at New York Life were set in motion in 2014 when the company announced a \$1 billion plan for an ambitious upgrade of its financial and data technology systems,” according to the *New York Times*. “Since New York Life is not a technology company, said Mr. Werfelman,

the company’s spokesman, it turned to outside contractors for the upgrade.”⁷⁹ Werfelman said that contracting out this function “was part of a transformation of its technology systems that would soon result in more jobs in the United States.” The company said it expected to hire 1,000 employees and 3,500 agents in 2015.⁸⁰

The *New York Times* article also reported on Cengage, an educational publisher that laid off approximately 30 accountants in Ohio and Kentucky. The workers were given severance packages and the work was expected to go to India as part of a contract with Cognizant. Cengage spokeswoman Susan M. Aspey, said it contracted out because it needed to install “higher-grade accounting systems” and, she said, “To do this quickly and efficiently.”⁸¹

Cengage also decided to make changes in information technology, laying off 75 positions in information technology, which, when combined with the 30 in accounting, would come to about 3 percent of its approximately 4,000 person workforce. “Cengage, in an email statement, acknowledged a reduction in the workforce of 75 positions. An additional 20 positions have been moved to Cognizant and most employees have accepted those positions, the firm said,” reported *Computerworld*.⁸²

The crucial context missing from criticism of Cengage is the tremendous upheaval in the publishing industry. Cengage has attempted to change from a company that primarily *prints* large textbooks to one that *digitally* produces and delivers its books and other educational materials. It makes little sense to conclude the visa status of the contractor, rather than the need to adapt to the sea-change in publishing, motivated Cengage’s decision to change its information technology.

A Cengage spokesperson said in a statement that the reason for contracting with Cognizant was that the “business is evolving and we now serve more customers with software than print materials.” In addition, the spokesperson added, “Over a period of nearly a year, we reviewed our technology systems and staffing. We were very transparent with the team about this process. We determined that we needed a more flexible staffing model that could better serve the cyclical nature of our business, and a different model of software support for our customers. To do this quickly and efficiently, we needed the support of an outside partner. We chose Cognizant, a U.S. firm that supports several companies in the education industry.”⁸³

While not a direct factor in its decision to follow the trend of other companies in contracting out accounting and IT functions, Cengage’s actions were also influenced by the need to be financially responsible for the good of the company and the 97 percent of employees not affected by the contracting decision. In July 2013, Cengage Learning filed for bankruptcy with a goal to “significantly reduce its approximately \$5.8 billion of outstanding debt.”⁸⁴ The company emerged from its Chapter 11 reorganization in March 2014.⁸⁵



The Larger Global Context

While some members of Congress and news reports have highlighted cases of contracting out that involved layoffs and foreign nationals on temporary visas, the available evidence suggest most of these situations revolve around international trade more than immigration. In the case of Toys “R” Us, the *New York Times* reported, “By late June, eight workers from the outsourcing company, Tata Consultancy Services, or TCS, had produced intricate manuals for the jobs of 67 people, mainly in accounting. *They then returned to India to train TCS workers to take over and perform those jobs there.*”⁸⁶ Nobody thought the 8 people would replace 67 people by working in the United States. Instead, the 8 people facilitated TCS delivering the services in India.

Sometimes positions are sent elsewhere in the company but outside the United States. Similar to Cengage, watchmaker Fossil needed to adapt to new competition and the changing marketplace for watches. “We run a global IT shop because we have operations outside the U.S., and some of the outsourced positions will be on-site in our facilities,” said a Fossil spokesperson.⁸⁷ As is typically the case, Fossil used a competitive bidding process before awarding the contract. Other companies have also added to their own facilities abroad.⁸⁸

In sum, the fact pattern in many of the cases that have made news is one of “trade in services,” in which a company supplies services to a U.S. customer, often a large U.S. company, and most of the services are delivered outside the United States. The foreign company sells services, rather than machines or other goods. “The United

States is a relatively open economy for trade in services, although not the most open,” according to J. Bradford Jensen, a professor of economics at Georgetown University and author of *Global Trade in Services*. “The United States has a comparative advantage in many tradable services and it makes sense for it to pursue increased liberalization of service trade.”⁸⁹ In other words, given how many services the United States exports, it would be a particularly bad idea for our government to enact measures against trade in services to “protect” jobs in the U.S.

Nearly all economists agree that free trade is beneficial to Americans and the U.S. economy. “Free trade increases prosperity for Americans – and the citizens of all participating nations – by allowing consumers to buy more, better-quality products at lower costs,” writes Donald J. Boudreaux, a professor of economics at George Mason University. “It drives economic growth, enhanced efficiency, increased innovation, and the greater fairness that accompanies a rules-based system. These benefits increase as overall trade – exports and imports – increases.”⁹⁰

Economists view jobs in the context of trade differently from most elected officials. “What trade does affect is the composition of activities in the economy,” explains J. Bradford Jensen. “Jobs are created in some sectors and lost in other sectors, reallocating economic activity across industries.”⁹¹ Boudreaux explains, “Over time, free trade works with other market processes to shift workers and resources to more productive uses, allowing more

efficient industries to thrive. The result is higher wages, investment in such things as infrastructure, and a more dynamic economy that continues to create new jobs and opportunities.”⁹²

None of this implies dislocation is not a potential result of trade. “Free trade drives competitiveness,” notes Boudreaux. “Free

trade does require American businesses and workers to adapt to the shifting demands of the worldwide marketplace. But these adjustments are critical to remaining competitive, and competition is what fuels long-term growth.”⁹³



Placing Numbers in Context

Economists and statisticians know that media attention can cause people to overestimate the likelihood or prevalence of something. (Think about the safety of flying in an airplane vs. driving in a car.) The impression created about job losses related to H-1B visas and IT outsourcing falls into this category. As noted earlier, plausible reasons exist that have little or nothing to do with immigration policy for why companies decided to contract with outside firms to perform certain functions and focus on core competencies. Competitive bidding for the contracts adds further weight to the argument that the immigration status of a contractor's employees has not been the reason for these decisions. Moreover, the stories have left the impression that incumbent employees would have retained their jobs if a different contractor was selected (of which there is no evidence).

For reasons of brevity, we can refer to the incidents cited in the news as job losses connected to "H-1B and IT outsourcing." We did our best to review news stories, books and Congressional testimony in an attempt to identify all of the cases cited in the media of "H-1B and IT outsourcing" connected to job losses. With the caveat that in most if not all of the cases that have received media attention the employees at those companies would likely have lost their jobs no matter which contractor was chosen (including a U.S. contractor employing only U.S. workers), we found an average per year of fewer than 600 jobs lost/layoffs between 2010 and 2015. It is possible that scouring the Internet, books and Congressional testimony did not reveal every alleged case in the previous 6 years.⁹⁴ But it seems to

have captured at least the most notable cases, the ones cited by critics.

The point is not to be exhaustive but rather to illustrate how media attention can inflate the perception of the prevalence of these incidents and lack context: Every year, approximately 20 million people in America lose their jobs due to layoffs, business closures, and other reasons. That means if approximately 600 people lost their jobs each year under the circumstances described in the notable or significant cases, then that would represent about 0.003 percent of the 20 million people who lose their jobs involuntarily each year in America, according to the DOL's Job Openings and Labor Turnover Survey (JOLTS).⁹⁵ If the number was twice as high or 1,200 people laid off it would still only represent 0.006 percent of those 20 million.

To attempt to prevent all layoffs in America would be economically harmful because it would mean the government is intervening to make it very difficult to dismiss employees, which would carry unintended consequences in the long run. In other words, the best – and perhaps only – "solution" on this issue for incumbent employees could be the worst one for the country. And that solution would be to "protect" incumbent workers in the same way that some European countries, such as France, have been trying to move away from in an effort to reduce unemployment. Here is the problem: Once a government makes it difficult to dismiss employees, then employers become more hesitant to hire employees in the first place, since dismissals may be costly or impossible.

The lack of flexibility in the country's labor market is a major reason why the unemployment rate in France was about 10 percent in 2016.⁹⁶ In comparison, the U.S. unemployment rate has been at or below 5 percent in 2016.⁹⁷



“Training Their Replacements” vs. “Keeping the Lights On”

The most controversial part of recent news stories has been the contention by laid-off employees that they were told to “train their replacements.” In a representative quotation from a news article, one writer states, “Fossil employees have extra work to do: train their Indian replacements.”⁹⁸ The contracting companies say this is not a case of employees “training their replacements” but rather providing information as part of the transition from the old system to the new system. The workers who come on-site are filling a temporary role in the transition. According to Jeff Augustin of Alsbridge, this information gathering “needs to involve some detailed interaction between the teams to really understand how the work is done. The process also has to be very structured and disciplined, because it has to take place quickly to adhere to the schedule.”⁹⁹

Contracting companies and sourcing advisors say the term “train their replacements” does not accurately convey the reality of the situation. First, there is no “one for one” replacement, they say, but rather a transition, with the people who come on-site unlikely to even be the same people who later perform the jobs in question. Under U.S. immigration law, it is unlawful to lay off an American and replace him or her with an H-1B visa holder by willfully paying below the required wage (the higher of the prevailing or actual wage paid to similar U.S. workers).¹⁰⁰ Moreover, it is noted, if companies wanted to keep doing the same thing but less expensively they wouldn’t need to hire contractors at all but could simply fire

long-time employees and replace them with less experienced domestic workers who would do the same job.

Contractors argue that during the transition to the new system it is necessary both to do an assessment of current processes and to “keep the lights on,” meaning current operations must continue while a new accounting or information technology system is put into place. Contractors also argue that U.S. citizen workers are typically part of this transition, but don’t attract the same attention, including in the media, as visa holders.

Often times, perception can become reality. Even if the contracting companies are correct, the process has become a flashpoint in the debate and disturbing to laid-off workers, which should warrant new consideration of how best to accomplish these transitions.

Potential Ramifications of Congressional Action

Some members of Congress have taken advantage of the negative publicity to introduce legislation that would severely restrict the ability of employers to hire any high-skilled foreign nationals. A press release from Sen. Ted Cruz (R-TX) cited some of the cases in the news in proposing a radical series of legislative changes to H-1B visas (S. 2394), including prohibiting individuals with a bachelor's or master's degree – approximately 90 percent of H-1B visa holders – from obtaining a visa until they first worked 10 years abroad, which would largely eliminate high-skilled immigration to the United States.¹⁰¹

Among the unfortunate aspects of S. 2394 and other legislation are the unintended consequences of the provisions contained in these bills. For example, S. 2394, co-sponsored by Senator Cruz with Senator Jeff Sessions (R-AL), would enact a series of significant changes to U.S. immigration law, including a \$110,000 minimum salary for H-1B visa holders, eliminating Optional Practical Training (OPT), which allows international students to work in the U.S. after graduation, as well as the aforementioned requirement that any foreign national with a master's or bachelor's degree to work outside the country for 10 years before becoming eligible for an H-1B visa.

Less attention has focused on measures in the bill to make it easier to sue employers and to prohibit an employer from requiring a U.S. worker “to sign any nondisparagement or nondisclosure

agreement...that conditions receipt of any financial or nonfinancial benefit from the petitioner employer upon the nondisclosure of such petitioner employer's potential misuse of the H-1B visa program.”¹⁰²

There is no legal requirement for U.S. companies to offer severance payments to workers who are laid off and when such severance is offered, nondisparagement and nondisclosure agreements are generally standard. Payments are often connected to ERISA (Employee Retirement Income Security Act) and nondisclosure agreements, in particular, are often contained in employee handbooks. The provision in S. 2394, if it became law, would likely have the unintended effect of discouraging employers from offering severance (i.e., money) to laid-off employees in any situation where the nondisparagement or nondisclosure agreements could be called into question.

This would hurt employees in a number of ways, not only denying them money but also permitting employers to go beyond confirming dates of employment if asked by another company. “Most nondisparagement clauses tend to be mutual and it could have a chilling effect on offering severance,” explains Lawrence Z. Lorber, senior counsel at Seyfarth Shaw LLP. “The standard in the bill, ‘potential misuse’ of H-1B visas, is such a vague standard the provision could have a far-reaching impact on these types of very standard clauses, an impact well beyond the intention of the bill's authors.”¹⁰³

A related clause in the bill also seems designed to help trial lawyers. It would make it easier for attorneys to convince clients to sue employers in situations related to H-1B visas. The bill would explicitly grant U.S. district courts, U.S. courts of appeals and the U.S. Supreme Court “jurisdiction to address civil actions” and “appeals of civil actions” by “any person claiming misuse of the H-1B visa program.” To make it even easier for lawsuits to proliferate, S. 2394 also states a person “shall have standing to pursue a civil action claiming misuse of the H-1B visa program...regardless of

whether such person has exhausted all administrative remedies in connection with such claims.”¹⁰⁴

“Not having to exhaust administrative remedies, such as filing a complaint and having it adjudicated by the Department of Labor, would make it much easier for trial attorneys and clients to sue companies that employ H-1B visa holders,” said Lorber. “The fact of an investigation or a lawsuit is generally a loss for a company regardless of the final disposition.”¹⁰⁵



H-1B Visas: History, Legal Background and Numbers

A popular perception is that H-1B temporary visas have only one legitimate use – finding foreign nationals with “unique” or “hard to find” skills who U.S. companies will later sponsor for permanent residence (a green card).¹⁰⁶ And that is a legitimate and common use of H-1B visas. Companies such as Google, Microsoft or Facebook identify individuals, often (but not exclusively) international students, who are recruited and go on to long careers in these organizations.

When companies such as these recruit in the United States, they discover that 77 percent of the full-time graduate students in electrical engineering and 71 percent in computer science are international students.¹⁰⁷ In fact, one reason H-1B visas are so important is that such visas are typically the only practical way to hire high-skilled foreign nationals, including off of U.S. college campuses. Hiring individuals on employment-based green cards is generally impractical because of the long waits due to low annual quotas and per country limits, with Department of Labor bureaucratic requirements an additional factor. L-1 visas require the individual to have worked for the employer for at least one year abroad.

While some may argue there is no need for U.S. employers to hire *any* high-skilled foreign nationals and that there is little demand today for people with science and engineering degrees, such sentiments generally do not come from human resources specialists whose jobs involve recruiting. “Companies both big and small are vying to recruit the same small pool of

highly sought-after students graduating with STEM – Science, Technology, Engineering, and Mathematics – degrees,” noted a *Yahoo Finance* article. “At the top schools like a Stanford [or] MIT, it’s pretty common for students to get anywhere from 5 to 10 offers,” said Jessica Gilmartin, chief business officer for Piazza, which connects students with employers. “We’re typically seeing very generous six-figure salaries plus bonuses plus equity,” according to Gilmartin. Incentives to attract these students, she said, include, “having dogs at the office, having parks for your dog, having free laundry, free food, breakfast, lunch dinners, nap pods. Really the list goes on and on.”¹⁰⁸

Some elected officials have cited government data to argue that many individuals with science, technology, engineering and math (STEM) degrees are not working in STEM fields. The implication is individuals are going to college, gaining degrees in computer science and then settling for work at a fast food restaurant. The problem is with the way the federal government classifies occupations, not a crisis in the labor market. For example, an individual with a computer science degree who is promoted to manager or is a CEO or other executive, or even a university professor, would be classified as working outside of a STEM degree by the federal government. *Approximately 11 to 12 million people* are gainfully employed at jobs in the U.S. economy that use their bachelor’s level expertise (or higher) in science or engineering but are *not* counted

in official statistics as working in a STEM “field,” according to the National Science Foundation.¹⁰⁹

Another legitimate use of H-1B visas long recognized under U.S. immigration law is to enter the United States (or change status in the U.S.) to perform temporary services. Some people may not *like* this use of H-1B visas but it has been permitted under the law for many decades. The original language on the H-1 visa in the Immigration and Nationality Act of 1952 stated it would be used by an alien “of distinguished merit and ability and who is coming temporarily to the United States to perform temporary services of an exceptional nature requiring such merit and ability.” In later years, the phrase “distinguished merit and ability” was reserved for fashion models and it was made explicit that a professional could also enter the United States with an intent to stay permanently.¹¹⁰

The Immigration Act of 1990, established a new subset of H-1 visas, called H-1B, and placed a 65,000 annual limit on the visas. The demand for H-1B visas has outstripped the supply for 14 consecutive fiscal years. Under the law, an individual in H-1B status “*is coming temporarily to the United States to perform services...*”¹¹¹ That definition remains. Current law also requires (among other requirements) the individual be in a “specialty occupation,” defined as an occupation that requires “(A) theoretical and practical application of a body of highly specialized knowledge, and (B) attainment of a bachelor’s or higher degree in the specific specialty (or its equivalent) as a minimum for entry into the occupation in the United States.”¹¹²

Warren Leiden, counsel emeritus, Berry Appleman & Leiden, was executive director of the American Immigration Lawyers

Association when the Immigration Act of 1990 Act became law. “The statement that Congress never intended highly skilled workers to come here temporarily to perform services is not historically accurate,” he said. “H-1s were available long before the 1990 Act, and the INA [Immigration and Nationality Act] has always simply required that they be members of a ‘specialty occupation’ coming to the U.S. to work in that occupation.” He notes that controversies over individuals working for contractors have been around for a long time. “I remember that there were contracting companies back in the 1980’s that used H-1s. I guess that nobody has ever liked the contractors, but it’s always been a legitimate use under the law.”¹¹³

“The Immigration and Nationality Act has long provided employers speedy and flexible access to highly skilled workers through the H-1 and H-1B visa categories, including allowing them to come here to perform services temporarily,” according to Robert P. Deasy, deputy director for programs, American Immigration Lawyers Association.¹¹⁴

In international trade agreements, the United States has also accepted the legitimacy of individuals coming to the United States to perform temporary services. In fact, GATS, which took effect in January 1995, codified the 1990 Act’s definitions of H-1B and L-1 visas, viewing the performance of work on such visas as legitimate to facilitate “trade in services.” GATS stands for the General Agreement on Trade in Services. It is a World Trade Organization (WTO) agreement negotiated by the President and passed by Congress.

Several provisions of bills that have been proposed in Congress to prevent “outsourcing” companies from employing

individuals on H-1B or L-1 visas are likely to violate U.S. trade commitments under GATS, including S. 2394 and S. 2266, according to an analysis of similar provisions in earlier legislation.¹¹⁵ “A number of provisions in legislation proposed to change U.S. law on H-1B and L-1 visas present a significant likelihood of being found to be inconsistent with U.S. commitments under the General Agreement on Trade in Services,” concluded a legal analysis by a law firm experienced in international trade law.¹¹⁶ “Passing legislation with measures that violate GATS risks retaliation against U.S. companies and can undermine U.S. efforts to open markets in other nations to American goods and services.”¹¹⁷

In March 2016, India filed a complaint with the World Trade Organization over fees Congress imposed on H-1B and L-1 visas.¹¹⁸ A goal of Prime Minister Narendra Modi’s invitation to visit America and address the U.S. Congress in 2016 was to forge closer economic and strategic ties between India and the United States. Passing measures that result in trade disputes with India does not help to further those objectives. In August 2016, India and the United States signed a “landmark agreement” to increase military cooperation between the two countries.¹¹⁹

H-1B Visa Numbers in Perspective

A key problem with H-1B visas is the annual limit is too low, which has led some to argue “outsourcing” companies have caused the annual limit on H-1B visas to be reached each year. However, this claim is not supported by the math. The limited supply of 85,000 (65,000 plus a 20,000 exemption) H-1B visas has been exhausted each year for the past 14 fiscal years, particularly the last few years.¹²⁰

Based on the numbers, even if certain “outsourcing” companies had been prohibited from filing for H-1B visas in recent years it would have made little difference in the overall supply of visas available to other companies. In FY 2014, U.S. Citizenship and Immigration Services reported receiving 124,000 H-1B applications in just the first week of filing.¹²¹ In contrast, in FY 2014, “7 outsourcing firms based in India” had 16,573 H-1B applications approved, according to the *New York Times*.¹²² Even doubling that number to include a broader definition of “outsourcing firms,” including U.S. companies, means that the supply of H-1B visas would still have been reached during the initial filing period whether or not such firms filed H-1B applications.¹²³

For FY 2015, 172,500 H-1B applications were filed in the first week of the filing period, and 233,000 such applications were received in the same period in FY 2016.¹²⁴ That means in both years, during just the first week, about 87,500 to 148,000 more applications were filed for FY 2015 and FY 2016 respectively than the 85,000 annual limit would permit.¹²⁵

In a recent Senate hearing, Sen. Richard Durbin (D-IL) suggested that “more than half” of the annual H-1B quota is used up each year by “two” Indian-based companies (TCS and Infosys).¹²⁶ This is not correct. TCS and Infosys combined received 9,104 new H-1B petitions in FY 2014, which would represent 10.7 percent of new H-1B petitions approved from the 85,000 petitions in FY 2014 subject to H-1B annual statutory limits, according to USCIS data.¹²⁷

The *New York Times* reported figure of 16,573 new H-1B petitions from Indian-based outsourcing firms would represent 19.5 percent of the (85,000) H-1B petitions subject to the annual statutory limit in FY 2014.¹²⁸ (In FY 2015, the figures were lower, at 14,610 new H-1B petitions approved for the these 7 Indian-based companies, or 17 percent of the 85,000 H-1B petitions subject to the FY 2015 limit.)¹²⁹ These numbers appear trivial in the context of the overall U.S. economy, as well as in a global context. The size of the U.S. civilian labor force in 2014 was 156 million (it’s about 159 million today).¹³⁰ The 16,573 new H-1B petitions for Indian-based outsourcing firms in FY 2014 equaled 0.01 percent of the U.S. labor force, a small proportion by any reasonable standard.

The technological revolution that has taken place in America and around the world since 1990 has been the key driver of the demand for high-skilled labor, both native-born and foreign-born. Congress set the original 65,000 annual limit on H-1B visas and the 140,000 annual on employment-based green cards (for permanent residence) in the 1990 Act before the World Wide Web existed on a global scale for individual users.

Moreover, back in 1990 other innovations had yet to be introduced, including smartphones, mobile applications, streaming video, social media and 3-D printing.¹³¹

Advances in information technology and the Internet not only have increased the demand for skilled labor, but also have encouraged companies to find more effective ways to utilize new technology to improve their business operations, which has led to significant increases in contracting out non-core functions. The use of H-1B visas by outsourcing companies reflects the market demand for these types of services.



Conclusion

Contracting out, technological advances and access to the global labor market have combined to cause people to seek out enemies when, in reality, there are no enemies. There is only change and a desire by companies to stay competitive in the face of that change. “Washington can’t protect workers against technological and competitive obsolescence,” writes *Wall Street Journal* columnist Holman Jenkins. “America’s salvation has been a dynamic that, over time, creates more good jobs than it destroys.”¹³²

Contracting out or outsourcing is critical to allowing U.S. companies to compete in the global economy. A company can hire a contractor that specializes in information technology or finance to establish a new system that frees up needed capital, allows for scalability when revenues rise or fall, and gives access to additional talent and technology, notes Pushkar Soman, a senior consultant at Quint Wellington Redwood, a global consultant and training firm.¹³³ Fortune 500 companies regularly contract out functions, experts note, and it usually only becomes controversial when, often during the transition phase and months after the decision to outsource was made, incumbent employees find visa holders on-site, raising concerns U.S. workers are being replaced by foreigners.

This report asks critics and neutral observers to acknowledge several facts. One fact is that companies contract out work frequently and for reasons unrelated to U.S. immigration policy. The most important reason is to focus on core competences, which can make companies

“Automation and cloud will play a tremendous role in the future of outsourcing,” he said. “We are witnessing significant investments by many of the large outsource providers . . . in the development of automation solutions. We are already seeing business cases that eliminate 40 percent or more of the labor associated with many functions based on a high degree of automation.

more competitive, particularly by accessing new skills and technology not sufficiently available within the company. Is this done to save money? Yes, often that is the case. But companies are also looking to improve performance by working with contractors that specialize and have a proven track record with other clients. The cost savings come not from bringing in “cheaper” foreign workers to do the same exact jobs in the U.S., but by implementing new systems and processes that include automating functions that were previously performed in-house by the company.

Another fact is that particular instances of contracting out services that have made news have precipitating events or history with little or no connection to immigration. In the case of Southern California Edison, an outside consultant’s report following an on-site shooting in the information

technology department painted a picture of such poor management that even laid-off employees said the report played a key role in the company's decision to outsource IT functions.

Moreover, Southern California Edison did not simply decide to lay off incumbent workers and replace them with foreign workers on visas, as press reports and statements by elected officials have implied. Instead, the company used an outside advisor and solicited bids through a competitive process, making it virtually impossible for the company to know when the process began such details as the visa status of individuals hired by the yet-to-be-selected contractor.

Disney had a history of contracting out for information technology services that went back at least a decade. Like other companies, Disney uses a competitive bid process before it decides which contractor it uses. Disney, as in previous efforts, sought to structure its technology divisions with a mix of in-house personnel and outside contractors as part of an effort to change its technology focus. Unfortunately, people lost their jobs. But there is little evidence that immigration law, rather than a company decision to restructure and change its technology focus, was to blame.

In the case of Cengage, the company needed to move quickly to transition from a publisher that printed large textbooks to one that made a high percentage of its offerings to students available online in a digital format. Competitive pressures demanded these changes. Even the parent company of the *Los Angeles Times*, a newspaper that criticized Southern California Edison's outsourcing, found, like Cengage, it needed to outsource IT work to move more quickly into the digital age in the battle for consumers.

In short, a close reading of the cases presented in the media where "H-1Bs and IT outsourcing" were blamed for layoffs reveals immigration policy played at best a tangential, often "after the fact" role rather than the cause or precipitating event portrayed by some critics. H-1B visa holders may have been used during the transition phase to a new system but there is no evidence that if the contractor had used U.S. workers during that transition phase – or a different contractor was selected – the results would have been any different for the incumbent workers who lost their jobs at these companies.

It is unfortunate when people lose their jobs and we sympathize with anyone who is laid off. But as noted earlier, the media attention has at times lacked important context, including an answer to the question: What is the evidence the U.S. employees at the company would have kept their jobs if a different contractor had been selected?

Even if every layoff happened as critics contend, which the evidence indicates it has not, crucial context also has been missed by not placing any particular layoff in the context of the overall U.S. economy: Every year, according to the U.S. Department of Labor's JOLTS report, approximately 20 million people in America involuntarily lose their jobs due to layoffs, dismissals, business closures, etc. That means if 600 people lost their jobs each year in the types of cases alleged by critics, then that would represent about of 0.003 percent of the 20 million "involuntary separations" each year in our quite large U.S. economy. Even if the number were twice as high it would come to 0.006 percent of 20 million. And that assumes that incumbent employees would have retained their jobs if their company for some reason chose a different contractor.

While critics and neutral observers are asked to accept the above mentioned facts, companies that supply services also need to accept certain facts and are not blameless for the media controversies.

First, it has become evident that the current process of obtaining information from incumbent employees is disturbing to U.S. workers who are losing their jobs. While the companies insist it is necessary to receive information from incumbent employees to ensure a smooth transition for clients, the belief that workers who will soon be out of work are “training their replacements” has taken hold. New ways of gaining necessary information to avoid service interruptions while implementing new systems and processes should be considered.

Second, contracting companies must address the belief that they do not adequately attempt to train and recruit U.S. workers. In August 2015, Carnegie Mellon University (CMU) announced it received a \$35 million donation from Tata Consultancy Services. The donation “will support education and cutting-edge research by CMU faculty and students.”¹³⁴ It represented “the largest corporate gift to CMU and the largest gift from outside the U.S.”¹³⁵ In February 2016, *Mint* reported, “Three major Indian information technology firms – Infosys Ltd, Tata Consultancy Services Ltd (TCS), and Wipro Ltd – have joined US President Barack Obama’s ‘computer science for all’ initiative as part of a public-private collaboration.” Infosys pledged \$1 million, TCS will provide grants for teachers in 27 American cities and Wipro “announced a \$2.8 million grant for a multi-year project in partnership with Michigan State University to involve over a hundred school teachers, with the aim of nurturing excellence in science and mathematics.”¹³⁶

Efforts like these could help convince people the industry is interested in building up the U.S. workforce. In addition, the industry should ensure sufficient training of management is taking place to help guarantee proper human resources policies are implemented.

As explained in this report, given the way U.S. companies decide whether to contract out a function, the available evidence indicates immigration policy does not play an important role in the decision to keep functions in-house or to contract with a vendor. Despite this, some want to use news coverage of layoffs and contracting out to implement a broader anti-immigration agenda. Though the sentiment is not widespread, individual lawmakers have questioned whether *any* high-skilled foreign nationals currently should be permitted to work in the United States, except under the most constrained and bureaucratic procedures. They have attempted to use contracting out by Disney or Southern California Edison to argue that Google, Facebook, Microsoft and other companies must not need to hire high-skilled foreign nationals, since other large companies are laying off workers. But these are separate issues and situations.

Changes in immigration policies are likely to lead to unintended consequences. New visa restrictions would likely accelerate the pace of work taking place outside the United States, including for research and development. In addition, common sense would indicate contracting companies could hire a core of U.S. workers to go to a client’s site, obtain the necessary information, and prepare all the work to be sent outside the United States. That would place the work outside the reach of U.S. immigration law and U.S. statutes. Would members of Congress outlaw Americans from working

for contracting companies? It is difficult to see how that would be legal.

Perhaps the best evidence that this issue has little to do with immigration came in August 2015, when it was announced that Citizens Bank in Rhode Island would do the same thing that Disney, Southern California Edison and other companies had done – contract out for specialized services and, as part of the restructuring, lay off between 150 to 350 IT workers.¹³⁷ Why did this outsourcing from Citizens Bank not receive front page stories and denunciations from Congressional and other critics? It is likely because it contradicted the narrative that the use of H-1B visa holders is what causes the layoffs. “Bank IT employees are training replacements in India to take over their jobs,” reported *Computerworld*. “IT employees who were contacted say this ‘knowledge transfer’ is being accomplished remotely, over the Web and in teleconferences.”¹³⁸

In other words, by accomplishing the transition via the Web, the contractor avoided any sightings of foreign nationals on the premises of Citizens Bank and the potential negative publicity that would cause, although there is no information available that indicates this was the reason the contractor conducted the transition in this manner. However, it provides substantial evidence that anyone who believes changing immigration policy will prevent contracting out will be sadly mistaken.

The best approach is to let our markets function and avoid introducing new laws or regulations that would distort the market and send work outside the United States that would have stayed here. Focusing on core competencies makes U.S. companies more competitive and better able to withstand economic storms in the global economy.

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