

## Key Considerations for Outsourcing Payroll

By Phil Fersht, HfS Research

**Payroll is the lifeblood of HR technology and outsourcing.**

Human resources data is the fulcrum of any business. The ability to have real-time, integrated information about staff profiles and performance, compensation, and location is paramount to providing management with crucial information to make decisions.

Moreover, for the international corporation, the benefits of managing an integrated global HR operation increase exponentially in today's markets. There is often no better platform on which to base this HR data than at the payroll level, where all the metrics necessary to ensure staff are fully accounted for, paid, organized and stored effectively. If companies can harness that, they can develop additional human capital-related programs using the data.

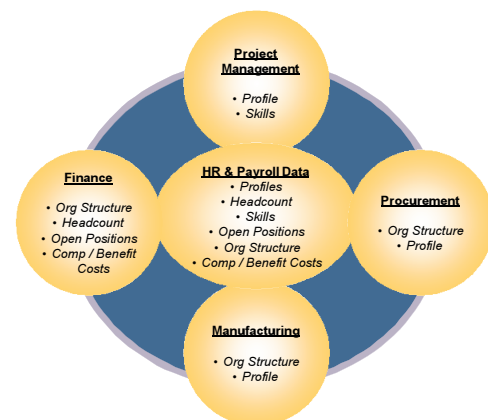


Figure 1. Payroll Data – The “Hub” of Organizational Data.

As Figure 1 illustrates, an integrated payroll system also supports the management structure of the multinational organization that has matrix-type organizational structures, which have product lines and managers working across national boundaries. Multiple interfaces into other applications and processes can give management the ability to have a truly integrated HR function.

The changing role of the HR leader, particularly in an outsourced environment, is to help facilitate the alignment of integrated HR data with senior management decision-making. A third-party HR service provider can offer the tools and service structure necessary to enable such alignment, but HR leadership must work to map out its internal HR process and systems.

Payroll is so central to HR and HR systems that if it is poorly integrated into other corporate data repositories, many companies find themselves in a situation where they cannot deliver organizational leadership with the data they need to make timely decisions.

**Outsourcing payroll can provide several key organizational benefits, but only if the customer works effectively with the right service provider and the transition is managed diligently.**

The problem lies in the fact that many organizations have been focusing on outsourcing payroll simply to cut costs and are missing out on the opportunity to leverage the payroll data platform to integrate and streamline processes. Consequently, HR and Payroll are not operating together in many organizations: the short-term gain is offset by longer-term integration issues.

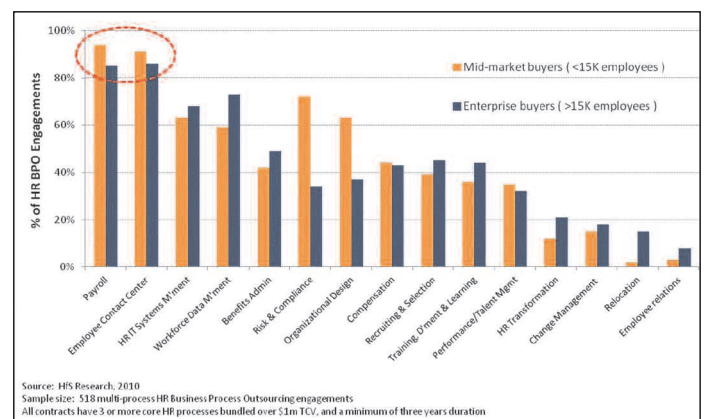


Figure 2. HR processes outsourced in multi-process engagements.

As Figure 2 illustrates, most organizations that have entered into multi-process HR business process outsourcing engagements center their solutions on the payroll function. Close to 90 percent of all organizations outsource payroll with an employee contact center service,

but only 60 percent actually focus on a solution that integrates payroll with their workforce data management.

HfS Research believes there should be many benefits for companies that outsource their payroll, provided the customer takes care to select the right provider for its needs, and organizes themselves internally to manage the provider effectively on a day-to-day basis.

Two of the main benefits are increased efficiency and cost savings. Companies that outsource payroll provide their employees with more time to focus on value-added and revenue-generating activities. In addition, as regulatory compliance is the service provider's responsibility, employees do not need to spend as much time keeping up with ever-changing tax laws and employment regulations. Furthermore, outsourcing payroll will help companies avoid penalties, if a tax filing or payment is submitted late or incorrectly. Most service providers will take care of any penalties or interest that accrues as a result of legislative mistakes.

### There are key steps you need go through when deciding whether to engage a payroll service provider.

**Conduct a thorough review of your company's existing business processes and analyze what specifically needs to change.** Hiring a change management consultant can assist with this. The consultant could analyze specifically what would change, review the impact, and make recommendations regarding what your company needs to ensure a successful partnership.

**Productivity, cost, and accuracy of current payroll activities need to be considered.** For instance, many companies struggle to complete payroll activities and feel it takes time away from completing other job responsibilities. Furthermore, a high level of precision and accuracy are key to producing a successful payroll. In addition, the administrative time it takes to print and distribute paychecks, manage data entry, and file tax forms is quite costly. Conducting a detailed activity-based cost analysis can provide the data you need to understand your current cost baseline. If your business continues to grow and your administrative costs are consistently high, outsourcing your payroll should bring many benefits.

**Decide how many employees and contract staff need to be covered by the payroll system.** As most payroll providers base their pricing on a per-check basis, the number of employees an organization has plays a big role in determining what the estimated costs would be.

**Determine what additional services/requirements your organization needs.** The types of employees you have can help you determine this. For instance, are your employees compensated based on an hourly rate or salary, are they part-time or full-time, contractors or temporary, and do they work in the office or remotely? These aspects will determine what types of additional services you need, e.g., time and labor management.

**Survey existing clients on how satisfied they are with the managed payroll services they currently receive from their service providers.** For this reason, providers have client references who are willing to speak with potential customers. Some key points you will want to research are as follows:

- What was their implementation process like?
- What were the pain points and are they still experiencing them?
- At what point did the partnership become stable?
- How knowledgeable is the team that processes their payroll and how accessible are they?

Many potential clients use these reference lists as an opportunity to find out answers they feel their sales representative wouldn't know/reveal and to alleviate some of their fears.

### What are the key questions to ask when selecting a payroll services provider?

Ask each of your potential service providers to develop a client service presentation that will address all of your questions, and also provide you with an overview of their organization. Outlined here are many of the critical areas for which you need definitive answers in order to narrow down your provider short-list:

- What type of technology does your service provider use? Can it be integrated with your current in-house HR system?
- Will the service provider have enough resources available to handle all of your business needs?
  - How many resources will be assigned to your account?
  - Will they be dedicated, or is your proposed service provision part of a shared-services model?
- If you choose to have your service provider answer your employee inquiries, will it be staffed accordingly to be able to handle your employee call volumes?
- Will the service provider be able to support you during your business hours? What type of after-hours support does it provide?
- What type of plan does each provider have to minimize disruption to the payroll process and enable its daily business operations and activities to be recovered and resumed in a timely manner following a disaster?
- What type of privacy measures are in place? This is extremely important since your service provider will be processing sensitive corporate information.
- What type of system is in place to track issues and escalations?
- What procedures will be in place to ensure that your service provider processes an accurate and timely payroll?
- Will there be any monetary compensation for performance metrics that are not met? What does the provider propose as standard penalties? Have you compared these with service level agreements in other organizations?
- Further to this, what quality measurements will be in

place? Is there performance reporting and how is this information presented/delivered to you?

- Will there be a step-by-step payroll run book and checklist in place?
- Will it run and analyze audit reports on a per-payroll basis to ensure a high level of payroll accuracy?
- Can the payroll provider provide you with the customized reports that are required for your organization?
- What type of year-end process does the service provider have in place? Will it produce your tax forms?
- Can we meet the delivery team prior to the deal being signed? Can we be provided with internal résumés for the resources who will be assigned to our account and schedule some times to conduct an interview? And, can we be provided with the following information on each proposed core representative who will be assigned to manage our account:
  - What type of experience do they have?
  - How long have they been with the company?
  - How well do they know payroll legislation?
  - Are they certified? (CPA and APA)

### What are the common mistakes made and challenges faced when outsourcing payroll?

**One of the biggest mistakes a client can make when selecting a provider is to base the decision solely on cost.** Some clients go for the cheapest option, while others go with the most expensive option thinking it must be the best. These clients often do not know the right questions to ask and, therefore, do not conduct the appropriate research. While cost is an important factor, it should not be the only one.

**Many customers do not engage the right people in the decision-making process.** Often, the individuals tasked with selecting a service provider do not have payroll experience and will not be involved in the day-to-day payroll process. This can result in the wrong service model being selected and a great deal of confusion regarding overall roles and responsibilities. When this happens, service providers often spend a great deal of time resetting client expectations and handling escalations from disappointed clients who feel they are not receiving the service(s) they should.

**Many customers assume the service provider will do everything.** Clients often do not have a good understanding of their roles and responsibilities and are often confused about what they should be doing. It is important for both the client and the service provider to understand the scope of their responsibilities to ensure a successful partnership.

**Many customers underestimate the amount of testing needed for system changes that are configured by the service provider.** There are often new requests that come up or problems with existing programming that require your service provider to make changes to the payroll and HRIT system configuration. It is the responsibility of the client to test these changes prior to giving approval to the service provider to implement them. Often, the customer does not test sufficiently due to time

constraints or lack of knowledge on how to complete testing.

Obviously there is a good deal to consider when outsourcing payroll. However, given the critical nature of this data to the rest of the HR service delivery model, the selection and transition to the right provider should be given more time and attention than one might believe!

**The customer's staff who works with the service provider on a daily basis are often not the individuals who were involved in the implementation phase.** This means they were not involved in developing the service level agreement/contract, project preparations, testing or even the initial client training. This poses a challenge in the early phases of transition, as there is often a lack of understanding of how the system works, what the service model is, and the roles and responsibilities of the governance team. It is costly and time-consuming to train staff to manage and configure the payroll system, which results in the service provider having to spend a great deal of time retraining its clients.

**What is the relevancy of operational metrics provided by the service provider on a monthly basis?** As mentioned earlier, when the staff with day-to-day operational responsibility for payroll is not involved in the development of the service level agreement, the metrics outlined in these contracts are too often not helpful in managing the ongoing relationship.

When clients have a large number of employees and office locations, it becomes very difficult to control internal processes and establish communication between different parts of the organization. There are often too many people on the client side involved in day-to-day issues, which makes it increasingly difficult for the service provider to manage client expectations. Clients who do not designate specific points of contact for the service provider often have many more escalations and unresolved issues.

### What are the bottom-line takeaways that customers must consider when evaluating whether to move to an outsourced payroll model?

**Get commitment from your service provider that the client services resources assigned to the account are available during the implementation phase.** It is important to ensure that resources understand the full scope of the project and have a full understanding of the client needs. Some things to consider:

- Has there been a thorough knowledge transfer completed between the implementation team and the provider's client services and support teams?
- Are all of the operational process documents finalized and have they been approved by all the key stakeholders?

**Research what type of training will be provided – does your service provider conduct general training or will they develop training specific to your company's requirements and setup?** It is extremely important that the people who are receiving the client training are the ones who are going to be supporting the payroll process.

**If your service provider will be handling your employee calls, ensure that you work with them to develop a comprehensive set of FAQs.** One recommendation is to coordinate reoccurring calls to discuss employee satisfaction, updating FAQs and employee concerns. It will be important to work with your service provider to develop an employee satisfaction survey to measure the quality of service provided to your employees.

**Work with your service provider to ensure that the performance metrics outlined in the service level agreement/contract are meaningful to your organization's needs, such as:**

- Resolution time – How quickly are issues resolved?
- Payroll accuracy – What was the accuracy of the payroll? What types of errors occurred?
- Timeliness – Was the payroll processed in a timely manner. Were pay-slips and standard reports delivered on time?
- First call resolution – What percentage of issues are resolved within the first point of contact?
- Average speed of answer (Contact Centre) – The average amount of time that has been taken to answer all calls in a given period.
- Call abandon rate – Percentage of the calls made by an automatic dialing device to prospective customers or by customers to a telemarketer that are not intercepted by a live operator before the prospect/customer disconnects.
- Response time to issues – How quickly are your issues responded to?
- System availability – What percentage of time is your service provider obligated to ensure that the system is available to you?

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### About the Author



Phil Fersht is founder and CEO of HfS Research Limited, a leading research analyst organization covering global outsourcing strategies. Launched in 2007, its blog “Horses for Sources,” has more than 100,000 regular visitors across the global outsourcing industry, and is a leading destination for collective opinion, research, analysis, and coverage of industry developments. Fersht is an industry analyst, practitioner, advisor and strategist across business process outsourcing (BPO) and IT services worldwide. While at AMR Research (Gartner Inc), he led the firm's BPO and ITO practice, and was previously a market leader for Deloitte Consulting's BPO Advisory Services. He is a frequent author and speaker on IT services, finance, HR and procurement BPO trends and issues and was named both an "FAO Superstar" and "HRO Superstar" by *FAOToday* and *HROToday* magazines for 2005-2010. He has a B.S. with honors in European Business and Technology from Coventry University, United Kingdom and a Diplôme Universitaire de Technologie in Business and Technology from the University of Grenoble, France. He can be reached at [Phil.Fersht@HfSResearch.com](mailto:Phil.Fersht@HfSResearch.com).