Building a Business Case for Outsourcing

Employee Benefits Administration & Payroll Outsourcing

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...helping companies optimize their HR / benefits / payroll service partnerships
Agenda

- Trends in outsourcing
- What is a business case?
- Components of a successful business case
Trends in Outsourcing
The Outsourcing Spectrum

Outsourcing Spectrum

Traditional Co-sourcing BPO

• Transactional
  • Employee Support
  • Web capabilities

• Responsibility sharing
  • Systems driven
  • Portable & scaleable

• Cost minus
  • Entire shop
  • What’s included

Important Questions
What are the reasons for outsourcing? What is HR?
What are current costs? Who calculates cost?

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### Planning and Policy

### Source & Select
- External Recruiting
- Internal Staffing
- Job Design & Evaluation
- New Hire Orientation
- Offer & Screening
- Orient and Assimilate
- Performance Planning
- Promotional Orientation
- Temporary Services

### Develop & Counsel
- Employee Assessment
- Employee Relations
- Performance Management
- Professional and Personal Development
- Training

### Reward & Retain
- Benefits Administration
- Compensation Management
- Employee Assistance Services
- Employee Financial Planning
- Employee Retention
- Incentive-Based Compensation Programs
- Recognition Programs
- Wellness Programs
- Workers’ Compensation

### Redeploy & Retire
- Expatriate Management
- Outplacement & Career Transition
- Relocation/Expatriate Counseling Administration
- Retiree Processing and Counseling
- Terminated Employee Processing
- Transfer and Reorganization Processing

### Manage Information
- Audit and Control, HR Information Interface Access, HR Information Maintenance, HRIS Development and Maintenance, Management Reporting, Performance Measurement
Firms Outsourcing Payroll
The Outsourcing Spectrum

Payroll Outsourcing - G2N

- 39% Outsourced
- 61% In-House

Printing W2s and 1099s

- 46% Outsourced
- 54% In-House

Tax Filing & Deposits

- 48% Outsourced
- 52% In-House

Source: ADP Market Research, 2002
Reasons Given for In-house Processing
The Outsourcing Spectrum

- Control: 39%
- Lower Cost: 35%
- Prefer In-House: 16%
- Payroll Complexity: 14%
- Flexibility: 10%

Source: ADP Market Research, 1999 and 2002
Top Payroll Issues Have Not Changed
The Outsourcing Spectrum

- Taxes 32%
- Accuracy 23%
- Timeliness 15%
- Compliance/Regulations/Laws 14%
- Time & Attendance 10%
- Technology 9%

Source: ADP Market Research, 1999 and 2002
Payroll Tax Compliance
The Outsourcing Spectrum

- **Today: Tax Codes Are Complicated and Changing Rapidly**
  - 1,900 plus changes to the US tax code since 1995
  - 7,500 plus federal, state and local tax jurisdictions
  - 45,000 total pages of federal tax rules
  - Resulting in 9.5 million employment tax penalties annually

Source:: Institute for Policy Innovation, 2002
Firms Outsourcing Benefits
The Outsourcing Spectrum

- **FSA Administration**
  - 33% Outsourced
  - 67% In-House

- **COBRA Administration**
  - 40% Outsourced
  - 60% In-House

- **Open Enrollment**
  - 19% Outsourced
  - 81% In-House

- **Employee Call Center**
  - 15% Outsourced
  - 85% In-House

Source: ADP Market Research, 2002

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Firms Outsourcing HR
The Outsourcing Spectrum

HRIS
- 12% Outsourced
- 88% In-House

Screening & Selection
- 34% Outsourced
- 66% In-House

Personnel Administration
- 8% Outsourced
- 92% In-House

Recruiting
- 26% Outsourced
- 74% In-House

Sources:
1 ADP Market Research, 2002
2 Gartner, 2002

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What is a Business Case
The Big Picture

- An exercise in logic
- A compelling argument for change
- A justification for action

Does this make sense??????

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What is a Business Case
Considerations

- How does your organization justify change?
- What financial return is expected?
- What is culturally valued?
- Is there a standard format for business case presentation?
- Who needs to approve the business case?
- Who should be involved?
What is a Business Case
The players

- Size of capital request
- Ask one question:
  “Who can derail this process once it’s begun?”
- HR, finance, IT, legal, procurement, divisional personnel, stake holders
What is a Business Case
Components of a Business Case

- What needs to change
- Why it needs to change
- Process used to decide how to change it
- How will we be better off financially
- Non-financial ways we will be better off
- What is the final recommendation
What is a Business Case
Components of a Business Case

- Executive Summary
- Case for Action
- Process Undertaken
- Financial Analysis
- Non-Financial Analysis
- Recommendation

Different components
Different formats
What is typical???
Business Case Components
Executive Summary

- First in the business case
- Last to be written
- Recap salient points of business case
- Follow format of rest of business case
- Liberal use of bullets & white space
- Remember, this is an “executive” summary
- How much detail do your execs want?
- Level of detail appropriate to audience

“A well written executive summary should write itself”
Business Case Components
Case for Action

“If it ain’t broke, why fix it?”

- Relate examples of how it’s broken
- What is the cost to the company in time, expense, risk, service levels, organizational agility
- “Why do anything?”

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Business Case Components
Case for Action

Fundamentally: Why Outsource??

- Important in setting future expectations
- These are the items upon which success or failure will be judged
Why Outsource?

I want to focus on my core business

We can’t react quickly enough to change!

Headcount reduction

Costs!

Customer Complaints!

I’ve got to get my risk under control

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Business Case Components

Process

- Describe the process undertaken
- Indicate parties involved
- Indicate reasons for key decisions
- Describe analysis used
Business Case Components
Financial Analysis

- Different tools available
- Dependent on company expectations
- Understanding current costs
- ROI Analysis – cost of capital
- TCO Analysis
- Baseline
Business Case Components
Financial Analysis - Today There is A Measurement Gap

- Only 16% of senior HR executives feel their firms are effective in achieving ROI from HR technology investments. – Mercer

- Only 16% of senior financial managers are confident in their grasp of ROI from HR technology investments. – Mercer

Sources:

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Business Case Components
Financial Analysis – Example

- Multi Divisional Corporation
- Each division in a different HRIS environment
- Desired standardization
- Looked to new software and approach
Cost/Benefit Analysis

Benefits - Hard Dollar Savings

- Hard dollar savings are derived from two main sources:
  - A headcount reduction of 81.6 in the H.R. function; and
  - Savings from elimination of legacy systems costs such as licenses, maintenance, system support, etc.

- Many of these reductions will be accomplished by encouraging increased use of flexible staffing arrangements such as modified and part-time H.R. employees and job sharing where appropriate.

- These savings alone will provide a 25 month payback on ABC’s investment in the XYZ system with a 17.7% IRR.
Cost/Benefit Analysis

Benefits - Hard Dollar Savings

- Total annualized direct savings from both staff reductions and elimination of legacy systems will exceed $7,208,000.
- Data was provided by ABC Human Resources for 86 planned headcount reductions that was solicited from the divisions. The headcount savings of 81.6 recommended here is derived from the extension of Div E’s process mapping and analyses. These results are much more specifically associated with the value of installing the XYZ system.
# Cost/Benefit Analysis

## Hard Dollar Savings Projection

<table>
<thead>
<tr>
<th>Division</th>
<th>Headcount</th>
<th>Annual Value (loaded salary)</th>
<th>Legacy Savings</th>
<th>Annual Total Savings</th>
<th>H.R.</th>
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<tbody>
<tr>
<td>ABC0.7</td>
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<td>$48,048</td>
<td>$0</td>
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<tr>
<td>Div A</td>
<td>0.9</td>
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<tr>
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<tr>
<td>Div C</td>
<td>22.4</td>
<td>$1,537,536</td>
<td>$990,000</td>
<td>$2,527,536</td>
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<tr>
<td>Div D</td>
<td>9.8</td>
<td>$672,672</td>
<td>$32,500</td>
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<tr>
<td>Div E</td>
<td>22.0</td>
<td>$1,510,080</td>
<td>$0</td>
<td>$1,510,080</td>
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<tr>
<td>Div F</td>
<td>8.6</td>
<td>$590,304</td>
<td>$585,000</td>
<td>$1,175,304</td>
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<tr>
<td><strong>Total ABC</strong></td>
<td><strong>81.6</strong></td>
<td><strong>$5,601,024</strong></td>
<td><strong>$1,322,500</strong></td>
<td><strong>$7,208,524</strong></td>
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</tr>
</tbody>
</table>

* Source: Div E’s process improvement savings assumptions and calculations with loaded average salary of $55,000 plus 33% for benefits.

** Legacy savings for Div D are associated with legacy system maintenance, licenses, software, etc. and Div F’s with avoidance of budgeted training system and legacy savings.
Cost/Benefit Analysis

Total cost is estimated to be $11,214,730 and involves:

- Installation of XYZ for (division’s) and ABC.
- Construction of a ABC Data Warehouse for common reporting,
- Training System development, and
- Severance costs that are incorporated in the #### restructuring charges.
## Cost/Benefit Analysis
### Cost and Allocations for XYZ

<table>
<thead>
<tr>
<th>COSTS</th>
<th>Budget</th>
<th>Allocation</th>
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</thead>
<tbody>
<tr>
<td>One-time start-up costs</td>
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<tr>
<td>ABC</td>
<td>$200,000</td>
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<tr>
<td>Div A</td>
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<td>Div B</td>
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<td>Data Warehouse</td>
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<tr>
<td>Training System</td>
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</tbody>
</table>

* Covered under a separate appropriation

Total: $11,214,730
Cost/Benefit Analysis

Payback Period for XYZ
25 months

Months

Cumulative Costs
Cumulative Savings

Payback point
Business Case Components
Non-Financial Analysis

- Describe the non financial reasons for change
- Risk management – more important since Sarbanes/Oxley
- Service levels
- Corporate agility
- Catalyst for change
- Core competencies
- Fixed and determinable cost
- Leveraging technology

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Business Case Components
Recommendation

- Now that all of the analysis is complete, what is the recommended course of action?
- Where in the business case should this be?