

WHITE PAPER

Managed HR: Enabling Growth from Administration to Strategic Function

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IDC OPINION

The managed human resources (HR) market has entered a period of growth that has the potential to change the way businesses provide services to their employees. As a growing market, there are now many managed HR suppliers from which clients can choose. Based on the following considerations, IDC Canada believes that both clients and suppliers are gravitating towards a preferred HR outsourcing business model in which suppliers have strong HR capabilities both in breadth (expertise across all HR functions) and depth (long-standing experience in HR):

- ☒ Spending on HR outsourcing in Canada, excluding HR-related processing services is forecast to increase by more than 13%, on average, every year between 2005 and 2009.
- ☒ This spending estimate demonstrates that Canadian businesses are seriously considering all HR options including vendor managed HR services. IDC Canada research indicates that the standards for demand (buyer criteria) and supply (vendor offerings) in managed HR services are aligning around cost-effective solutions that improve organizational effectiveness through enhanced HR service delivery, allowing buyers to confidently choose the managed HR services option.
- ☒ Managed HR services are flexible and scalable; clients can choose how many (or how few) activities to outsource based on their specialized requirements. As clients grow more comfortable with outsourcing, they can add to the number of activities managed by their vendor/partner. As this occurs, clients of managed HR services must carefully choose a partner that can expertly match these growing needs.
- ☒ The evolution towards managed HR services will require considerably more effort on the part of clients to fully understand their business objectives for HR and the role played by external providers. This is of particular importance for companies that are new-comers to outsourcing.

IN THIS WHITE PAPER

There are few markets as dynamic and compelling as the managed HR services market. In the business process outsourcing (BPO) world, HR is one of the most active based on the number of deals signed in the past 12 to 18 months (a minimum of 8 noteworthy deals in Canada alone since September 2003, see Table 1).

TABLE 1

Notable HR Outsourcing Deals in Canada Since Mid-2003

Customer	Signed Contract Date
City of Montreal	March 2005
BC Ministry of Health	November 2004
BC Ministry of Management Services	November 2004
Hewitt Associates	November 2004
Molson's	July 2004
National Bank of Canada	February 2004
CIBC	November 2003
Calgary Health Authority	September 2003

Source: IDC Canada, 2005

Managed HR services, like HR outsourcing or HR BPO, encompasses value-added client/vendor relationships that involve the transfer of the management and execution of a single HR business process or a group of related HR business processes. Businesses are engaging service providers in a variety of ways ranging from traditional outsourcing contract structures to more advanced transformational relationships. It is this shift towards higher value-added vendor/client relationships that is rapidly becoming the signature of the HR market.

The value of managed HR services is derived from executing on two key business imperatives: **managing risk and enabling growth in strategic capabilities**. The achievement of these objectives is realized by using managed HR services to deliver critical, non-core business functions (such as payroll management and processing and recruiting services) and to support a high-quality HR framework that enhances the working lives of a business' most precious asset: its employees.

The movement towards managed HR services reflects the growing need for businesses to investigate alternative buyer/supplier relationships that bring more value to buyers beyond simple cost savings. In order to extract as much value from these advanced relationships as possible, businesses must chart a roadmap that aligns organizational objectives with supplier capabilities and relationship preferences.

MANAGED HR SERVICES: TRENDS

IDC Canada's projections indicate that spending on HR outsourcing services in Canada will grow from approximately C\$190 million in 2004 to C\$355 million in 2009. This includes functional HR processes and full-scale HR department-level outsourcing, and is based on continuous demand-side and supply-side primary and secondary research in Canada and around the world. The addition of C\$265 million into the market over this five-year period represents an average yearly spending growth estimate of 13.3%. This forecast estimate does not include HR processing services (e.g., payroll processing), a market that currently exceeds C\$1 billion and is projected to surpass C\$2 billion by the end of 2009.

Spending is being driven by businesses intent on improving their organization for the benefit of their customers, shareholders, and employees. Businesses are looking to ensure their competitiveness and increase profitability by reassessing the way they conduct business activities. This search for improved productivity and profitability, among other things, is leading businesses to reconsider their business processes. Efforts to achieve continuous process improvements have led to the development and implementation of programs such as Six Sigma and Total Quality Management (TQM). These programs enable systematic process reviews and help to identify ways of institutionalizing positive changes at all corporate levels.

The search for improved productivity and profitability is leading businesses to reconsider their business processes.

Human resources (HR), as a critical corporate function, is not immune to efforts to achieve continuous process improvement results. The move towards managed HR services aids in the achievement of these goals by facilitating organizational improvements, such as:

- Retaining employees by creating high impact HR services that are of highest importance to employees
- Lowering the expense of providing HR services without lowering the quality of programs provided
- Applying technology solutions to HR processes and activities without incurring upfront and ongoing investment costs
- Gaining access to vendor skills and competencies that are too costly or too specialized to retain in-house
- Focusing on core competencies by re-assigning resources to revenue generating activities

In many cases, the assessment of business processes in the realm of HR has led to the externalization of a variety of processes that are highly standardized and repeatable, most notably perhaps is, payroll processing.

In the payroll context, the standard use of external providers is typically limited to out-tasking processing services. Contact with the vendor performing the task can be sporadic and generally limited to problem resolution or routine updates. Vendors may not proactively engage clients in a dialogue to address process improvements or changes to the business' requirements. Likewise there may be little interest on the

part of clients to transform these processes (payroll in this case), because it is not considered to be a strategic function and the supplier's execution is sufficient.

In any successful and well functioning organization, business processes are fluid and the ability to extract increasingly more difficult sources of value from mature processes separates exceptional companies from the rest. As customer needs have changed, HR outsourcers have added competencies in functions that move beyond standardized activities to include those that remain process-intensive, require significant human intervention, and are customized to the unique requirements of individual businesses.

As a result, providers and buyers are moving from traditional outsourcing approaches to 'transformational' outsourcing approaches. Clients that are not satisfied with their current process can progress in one of two directions:

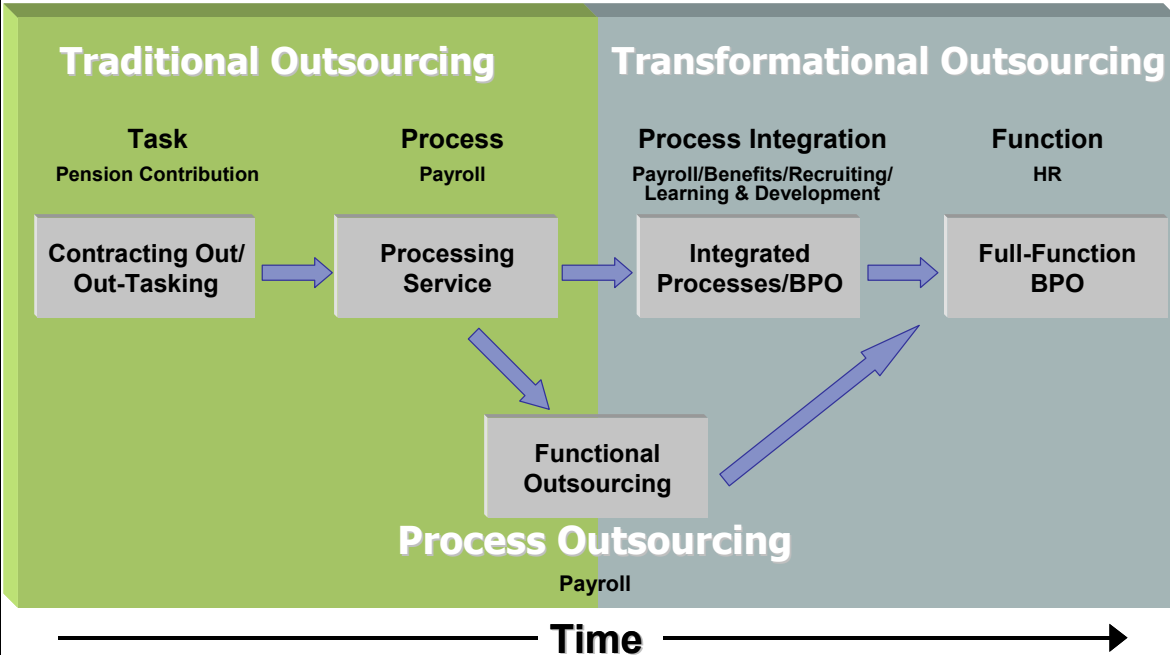
- ☒ They can proceed to transform their HR organization by integrating the various HR processes into a unified or shared services environment that breaks down functional silos. This allows the organization to then consider full-function outsourcing in which outsourcers assume responsibility for the entire HR department.
- ☒ Clients can opt out of the linear progression from internal management to external involvement (out-tasking to outsourcing to BPO) and engage outsourcers in functional outsourcing (as illustrated in Figure 1). Outsourcers will manage and execute discrete business functions within the HR department (e.g., payroll) rather than the entire HR function. Clients can choose to outsource any HR function separately (for example, payroll or recruiting), targeting HR functions according to need. Adding additional functions, to the same provider, over time leads to full-function HR BPO.

Providers and buyers are moving from traditional outsourcing approaches to 'transformational' outsourcing approaches.

Figure 1 illustrates the trend towards HR outsourcing.

FIGURE 1

Evolution of HR Outsourcing

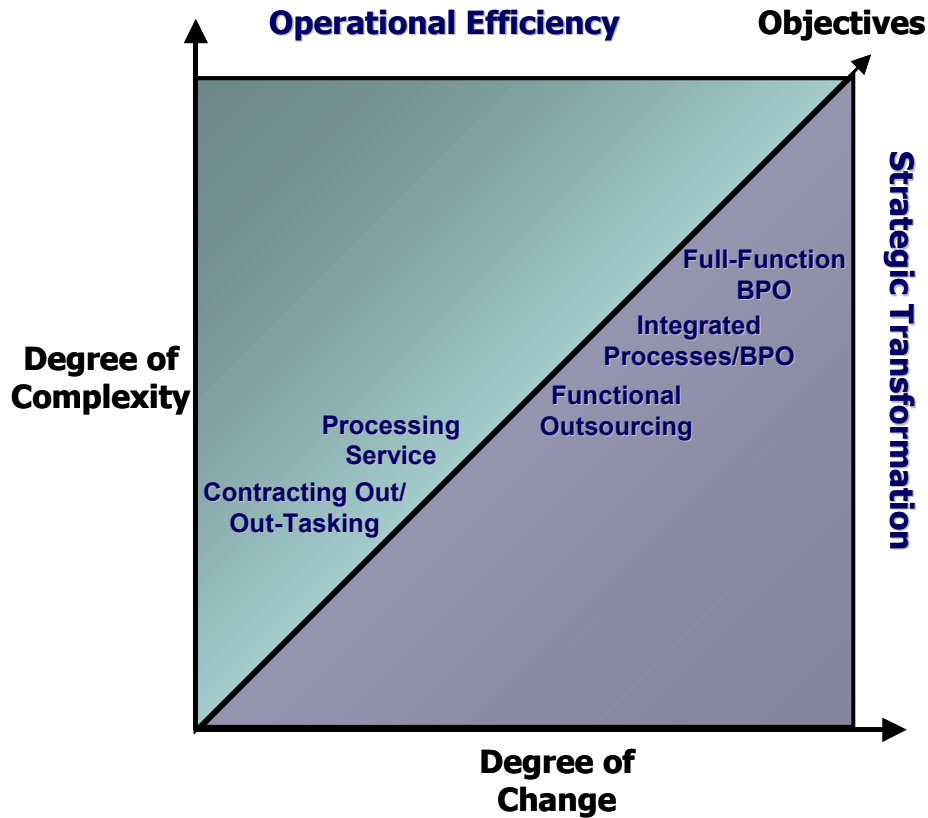


Source: IDC Canada, 2005

The distinction between **traditional** and **transformative** outsourcing becomes clear when plotted along three axes: **complexity**, **change requirements**, and **contract objectives** (operational efficiency or strategic transformation). In varying degrees, functional outsourcing, integrated BPO, and full-function BPO all represent strategic organizational change due to the involvement of the outsourcer in the ongoing success of the client organization. See Figure 2.

FIGURE 2

HR Outsourcing Services Positioning



Source: IDC, 2005

CONSIDERATIONS AROUND MANAGED HR SERVICES

The remainder of this white paper assesses the requirements for customers in the journey towards externalizing HR processes, and the activities and steps required to outsource fully managed HR services successfully. The trend towards HR outsourcing requires prospective clients to undertake a detailed examination of:

- ☒ The state of their HR department in preparation for this transformation;
- ☒ Characteristics and service offerings required for vendors; and,
- ☒ The outcomes the company wants to achieve in outsourcing its HR functions/departments and the means to achieve these objectives.

What follows are the basic building blocks of the requirements and benefits of transforming the HR organization through a fully managed solution:

1. HR Assessment - internal review of all internal HR processes;
2. The review of outsourcing options and the reasons for considering outsourcing rather than maintaining internal control over operations,
3. The processes required to assess managed HR service providers and determining best fit;
4. How the movement towards managed HR will influence the scope of the managed HR services contract and the type of relationship that clients should pursue with suppliers; and,
5. The benefits of fully managed HR solutions and the attributes that vendors should possess to ensure success.

The HR Assessment – Internal Review

In an effort to remain competitive, organizations survey the landscape for opportunities to reduce costs, minimize inefficiencies, and spread best practices to all corporate functions. These endeavors are particularly important for corporate functions that are traditionally defined as "cost centres" where contribution to profitability is, at best, indirect. HR departments generally fall into this category. As a result, organizations must assess the nature and efficacy of HR functions and activities and their impact on revenue, profit, and expense.

IDC research indicates that a significant percentage of senior Canadian executives consider their HR department to be above average as it relates to cost (to the organization) and quality, and that internal HR management is functioning as best as it can given its operational constraints. Research also indicates that there are few stringent measurements that corroborate this perception, and that what was once considered to be amongst the best is no longer good enough.

Achieving improvements in HR delivery requires an examination of individual processes (to assess program effectiveness) and the entire HR portfolio to identify areas of weakness, inefficiency, and redundancy. Undertaking this dual assessment will allow clients to outsource individual processes if there are specific problems, or the entire HR function if the challenges are more general.

Here are some concrete examples of HR functions to examine as part of the assessment, in the areas of payroll, employee information management and recruitment:

- 1) Payroll process: ratio of payroll staff to employees; length of time to process; accuracy rates; cheque-printing and bank reconciliation costs; penalty costs due to missed deadlines for government remittance filing; IT costs; time required to develop reports and the number and quality of those reports

- 2) Employee information management: number of paper processed required to onboard a new employee; number of data entry procedures; personal information benefits management processes; employee service satisfaction rates
- 3) Recruitment: ratio of recruiters to employee base; time-to-hire; job advertising costs; staffing agency costs; hiring success rates; turnover

One of the key determinations of an HR assessment is whether the organization should spend its limited resources on its existing HR department or if those resources should be re-directed to other parts of the business. Given the presence of viable alternatives and the pressure faced in maximizing core business functions for revenue and profit growth, an HR assessment is, perhaps, more important than it has ever been.

The completion of an internal HR department assessment is an important step because it determines the context for the next phase of a comprehensive HR assessment: the review of HR outsourcing options.

Service Provider Advantage: Review of Outsourcing Options

An internal HR department assessment enables internal cost structures and HR programs and processes to be compared against outsourcing organizations whose primary purpose is providing proven and repeatable best practices for HR business functions such as payroll management, recruiting, and hiring. The evaluation of external service providers can be based on three primary sources of differentiation that clients can benefit from:

- Scale**
- Scope**
- Specialization**

Scale

HR outsourcers have a clear advantage based on the size of their operations. For example, an HR outsourcer could use a single payroll professional to manage services for a number of clients, reducing the cost that each client would have incurred to support an internal resource. In the HR department, the absence of scale will often translate into higher relative costs. The use of external HR providers has two primary advantages over internal HR departments:

In the HR department, the absence of scale will often translate into higher relative costs.

- Lower set-up costs.** Clients using managed HR services do not incur up-front costs to enable a process or activity. Consider the advantage of avoiding purchasing an HRIS system and the cost of training users and IT personnel. Managed HR service providers have already made these investments on behalf of their customers.
- Lower input costs.** The use of service provider resources can be based on consumption, lowering ongoing expenses.

Scope

The benefits of economies of scope result when a single entity (i.e., an HR outsourcer) provides **multiple services at a lower cost than when the services are provided by two (or more) separate firms or departments (within HR)**. HR outsourcers can add resource capacity in complementary service areas by exploiting a number of advantages including: a common technology platform and consistent practices and procedures.

The benefits of economies of scope result when a single entity provides multiple services at a lower cost than when the services are provided by two (or more) separate firms or departments.

HR outsourcers can also combine economies of scope and economies of scale when multiple HR offerings are bundled into HR solutions. The benefit to clients lies in the outsourcer's ability to use economies of scale to maintain and expand economies of scope. Lacking the advantages of size, internal HR departments are forced to discontinue or reduce service offerings if business conditions change.

The aggregation of HR functions into one managed HR services contract provides the vendor with more opportunities to reduce redundant operations, rationalize or implement technology components, consolidate dispersed resources, and, identify other areas of potential organizational improvement. Multiple services under contract also allows vendors to lower transactional unit costs by combining various activities such as payroll, benefits administration, and recruiting by lowering overall fixed costs and by recognizing profit margins across a larger base of services.

Specialization

For HR outsourcers, HR functions are not overhead expenses as they are for client organizations. Economies of specialization result from the investment HR outsourcers make in core business offerings including HR information systems and HR best practices. The limiting factor for internal HR departments is that, as a cost centre, its overall size will be limited, impacting the number of services it can provide as well as constraining the depth and breadth of service offerings.

Economies of specialization result from the investment HR outsourcers make in core business offerings including information systems and best practices.

The payroll outsourcing market is a case in point. While many companies still provide payroll services in-house, for a variety of reasons, a large percentage (estimated at 25% in Canada) outsource payroll services to an external provider. This is particularly true for Canadian businesses with more than 100 employees. Approximately two-thirds of companies in this group outsource payroll. Payroll outsourcers have become so proficient at delivering payroll services, for customers of all sizes, that they can provide services at a lower cost. The same result applies to other HR services such as benefits administration, and recruiting. When all of these services are combined, the power of specialization, scale, and scope is clearly evident.

IDC's conception of the HR function in the typical organization is presented below in Figure 3. HR outsourcers are able to leverage economies of scale, scope, and specialization to deliver best-in-class services across the entire value cycle, in a single activity or any combination of activities.

FIGURE 3

IDC's HR Activity Framework



Source: IDC, 2005

Determining the Best Fit for the Organization

There are several questions that clients should address when evaluating the sourcing strategy for HR services, including:

- What is the primary HR outsourcing objective?
- What type of supplier relationship best suits the organization?
- Which component is the organization best served outsourcing (people, processes, technology) and what is the best mix to realize business objectives?
- What would be of greater benefit: outsourcing entire business functions or select parts of a business function?

Objectives

A clear objective for outsourcing HR processes or functions must be present before any action or decision is taken. Outsourcing is a means to achieving a business goal and should not be considered an outcome itself. For a business function like HR, which will remain a strategic corporate function even after its functions are

outsourced, objectives must be well understood and outcomes clearly defined prior to any engagement.

From an objectives standpoint, outsourcing is regularly cited in IDC Canada's research as a means of cutting costs or expenses; accessing skills, technologies or best in class processes not found internally; and, focusing on core competencies. Each of these objectives is unique and requires customized solutions to be fully realized.

The Client/Vendor Relationship

At a basic level, there are three main types of client/vendor relationships which vary according to the complexity of the project and the goals of the organizations that are outsourcing. The relationships span those that are unsophisticated to those whose primary objective is to bring fundamental change to the business and its HR practices.

1. In the first type of relationship, the focus is as follows:

- A. Improving process efficiencies,
- B. Transferring process execution to the vendor, and,
- C. Reducing internal costs.

Payroll processing, in a service bureau model, is an example of a relatively unsophisticated client/vendor relationship. Clients transfer payroll processing execution to the vendor in exchange for cost savings and process improvements based on economies of scale, scope, and specialization. This type of relationship will narrow the choice of vendor to specialist firms.

2. The second, more sophisticated client/vendor relationship addresses the issues of **improving process execution** as well as **optimizing and enhancing HR business processes**. In this type of relationship, business outcomes are the key objective and cost savings are of relatively lesser importance. Process redesign, business analysis, and the application of IT solutions to address process automation will increase the potential for buyers to achieve a modest level of transformation.

Consider another payroll example where the provider not only assumes responsibility for processing the payroll function, but also works with the customer to design and implement a software-based payroll system that allows employees to submit electronic time sheets or invoices. The software could also enable employees to access and maintain their personal records and manage selected HR functions such as updating benefits enrollment information for family members. The extension of the client/vendor relationship can have ancillary benefits that improve productivity for employees both inside and outside the HR department.

3. The attainment of business outcomes through innovation requires **vendors to act as partners**. The goal of this third type of vendor-client relationship is to improve the competitive positioning of the client organization through the redesign of business processes and functions. Clients engage vendors as participants in the transformation

as a means of sharing the risk (and subsequent rewards) of projects that are highly complex and require the full commitment of both parties for success.

In this type of relationship, the vendor can become the 'HR department of record' and assume all the operations of an internal department. Success can be measured in a number of different ways and include objectives such as reducing fees for plan administration or insurance coverage. It could also include identifying and conducting training programs to improve customer service or production management. Clients and vendors can work together to identify required objectives for each HR function, and cooperate to achieve these objectives.

Determining the Best Fit for the Project

The evaluation of the vendor/client relationship structure for managed HR services will help to frame the scope of the project to meet the stated objectives, and it will aid in identifying the required capabilities and skills that vendors will need to possess. In many ways, the scope of the project will influence the scale of the client/vendor relationship. In the HR context there are effectively two fundamental choices:

- ☒ Full-scope (departmental) outsourcing - Vendors assume all HR-related functions in **full-scope HR outsourcing**, becoming the HR department of record. Management and strategic oversight remain with the client organization, however, all HR process execution and support roles and responsibilities are assumed by the vendor. The complexity of these agreements will exclude companies whose primary goal is HR cost reduction.

- ☒ Selective (function/process/activity) outsourcing- In **selective outsourcing**, clients benefit from the external management of HR functions that are under-performing, under-utilized, under-staffed, or (currently) unavailable. The narrower scope of these engagements, in comparison to full-scope outsourcing, limits risk because process expertise can be targeted specifically. Businesses have long benefited from outsourced HR functions such as payroll processing and administration supplied by external vendors such as Ceridian.

In the HR context there are effectively two fundamental choices: full scope and selective outsourcing.

The determination of the ideal outsourcing contract structure will largely depend on the current structure of the HR organization and the value that clients place on improving selective HR processes or introducing innovation through the transformation of the entire HR organization.

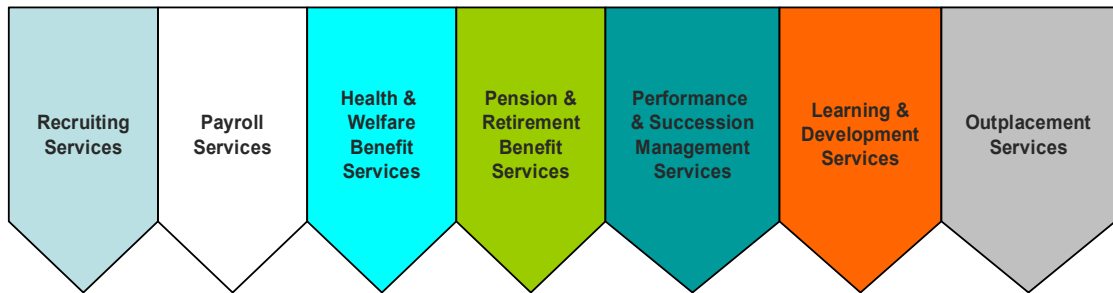
How the Structure of the HR Department Impacts Outsourcing

The typical HR structure is a series of functional hierarchies based on specialized knowledge or competencies, as illustrated in Figure 4. The benefit of structuring an organization in this fashion is that functional silos are often technically-focused requiring specialized knowledge and experience. Payroll is sufficiently different from recruiting, for example, to warrant specialized skill sets and different measurement criteria. Drawbacks to this approach include the inability to realize efficiencies between the functional silos because, quite often, resources are focused on effectively managing their tasks, rather than analyzing and implementing possible efficiencies. Perhaps the most important drawback to structure is that customers (i.e.,

employees) and service quality lose their place of primacy as the silos lose their customer orientation.

FIGURE 4

HR activities in typical functional organization



Source: IDC Canada, 2005

In contrast, an organization oriented by process consistently keeps the consumer in mind. Activities are arranged to allow services or products to flow through the organization (irrespective of functional orientation) to the end consumer. For example, a new employee would work through an orientation process that would span setting up payroll information, benefits and coverage information, materials/equipment procurement, and facilities set-up. Rather than passing through each department individually, the various functions work in concert to fulfill the entire orientation process. From this perspective, any activities (e.g., assigning unnecessary materials/equipment) that do not directly contribute to improving process efficiency or customer satisfaction are more easily identified and dealt with. In the process orientation structure, employees are better able to make process improvement changes and recommendations and the company as a whole can more easily discern which functions add value and those that do not. *This awareness can help the organization identify activities or processes that are well suited to being outsourced.*

The right HR outsourcing vendor would be equally well suited to work within either structure. In the case of functional silos, HR outsourcers can specialize in delivering services for specific HR functions like payroll outsourcing. The process-oriented client is, in some cases, better equipped to identify core business functions and therefore outsource non-core activities. These organizations can also identify the potential for process improvements and transformation and engage external providers accordingly.

Benefits of HR Outsourcing

With clear objectives in mind, assessing the inputs needed to achieve these objectives from external providers becomes less challenging. The following list provides guidance on the types of benefits that HR outsourcing providers can deliver to customers:

- ❑ **Obtain access to (internally) unavailable expertise, skills, technologies.** HR outsourcers have available all of the assets (people, processes, and technology) that may be lacking at the client organization due to cost and resource availability. Obtaining these assets from vendors allows for the implementation, integration, and enablement of services that provide value without the necessary internal investments in equipment, staffing, and ongoing management.
- ❑ **Increased flexibility.** With business in a constant state of flux, adapting quickly to changing conditions can separate competitors. Outsourcing enables flexibility by allowing clients to focus on core competencies and to rely on outsourcing partners to manage non-core functions that divert limited resources. Optimized process efficiencies can result from HR outsourcing relationships where business functions and technologies are continuously refreshed. In a fully managed HR service, the provider is responsible for ensuring its systems reflect the latest requirements. In the HR department, where government regulations change frequently, clients who outsource are no longer responsible for upgrading systems or software to meet new regulations or legislative changes.
- ❑ **Reduce costs/reduce investment.** Outsourcing HR services can provide significant value by reducing direct costs associated with resource expenses (wages, benefits, overhead, IT systems, etc.). Outsourcing can extend beyond these immediate benefits to include future investment costs associated with employee development and training, and new IT hardware and software purchases.
- ❑ **Focus on core competencies.** Resource constraints are issues for almost every organization and one remedy for this condition is identifying, investing in, and enhancing core business competencies rather than non-core competencies. Activities (and resources) focused on non-core competencies are often a distraction and can interfere with critical activities. Outsourcing non-core competencies/activities, allows clients to focus resources on the aspects of their business that drive revenue and profit growth.

What to Look for in an HR Outsourcer

Assessing the optimal outsourcing partner is as much an art as it is science. Its importance is such that numerous firms have developed practices to advise clients in selecting and negotiating with outsourcers.

Clients should carefully consider the attributes of vendors in order to strike the right balance between risk and reward. HR outsourcing is not the same as IT outsourcing.

While there are common technology issues, HR is a people-oriented business function and requires vendors with skills in dealing with employees of every status, handling difficult situations (e.g., termination), and working with third-party providers such as insurance firms. HR outsourcers that bring together these hard and soft skills will be strongly positioned to meet the needs of both the business and its employees.

HR outsourcers that bring together hard and soft skills will be strongly positioned to meet the needs of both the business and its employees.

The following list summarizes some of the key qualifications that should be examined when evaluating the capabilities and partnership potential of outsourcing organizations.

Key supplier qualifications

Experience

- Process expertise.* It is important to choose a provider with a strong, proven track record in managing and administering the selected processes for other clients. HR is process oriented and suppliers that have experience will be a better choice.
- Change management/consulting capabilities.* Businesses cannot afford to remain static. Qualified vendors will be able to assess its clients' business and offer advice and guidance on how to solve problems and improve profitability.
- Best practices approach.* Best practices can come from within an industry or from outside an industry. A provider with a breadth of experience and customers will bring processes and practices to bear that serve to enhance HR operations.
- Strong partnerships/alliances.* Vendors with strong industry relationships can shorten the length of time required to develop and implement solutions by utilizing the intellectual property of trusted partners.
- Global capabilities.* Supporting global businesses is a difficult proposition for a vendor with a limited global footprint. When the clients business spans borders, it is best to have an HR provider that understands the regulatory requirements of each country and the ability to provide services locally, if required. HR vendors such as Ceridian are responding to increasing demands for global services by providing additional product and service offerings in new geographies. A forward-thinking vendor will recognize areas in its offerings that can benefit from integrating the products and services of third-party partners into a single offering that can service clients of any size or global scale.

It is important to engage an outsourcing provider in a field that the outsourcer has established credentials and a proven track record. This is one of the most important ways in which to mitigate the risks associated with partnering with a provider:

Reputation

A positive reputation will ease the fears of employees as the outsourced HR services are transitioned from internal resources to external providers. Engaging a provider that has a reputation for dealing fairly with customers will make this transition less stressful.

☒ **Customer satisfaction**

As an ongoing relationship, HR outsourcing vendors need to be held accountable for customer satisfaction. Maintaining satisfied customers will result in fewer instances of non-compliance.

☒ **Commitment to continuous improvement (Manage contracts according to business outcomes)**

Continuous improvement addresses changes to the client's business and provides scalable capacity that reflects changing requirements. Vendors that manage contracts measured on business outcomes are highly motivated to work with customers to achieve jointly agreed upon service commitments because compensation is directly tied to meeting objectives.

☒ **Cultural fit**

This is one of the most important elements in the outsourcing relationship and one of the most difficult to assess. Partners (buyers and suppliers) that share the same basic attitudes and principles will experience less turmoil based on ongoing operating and management procedures.

☒ **Clear vision**

Outsourcers that have a clear image of how markets are evolving and how they can protect customer interests are committed to their long-term viability and to their customer's long-term success.

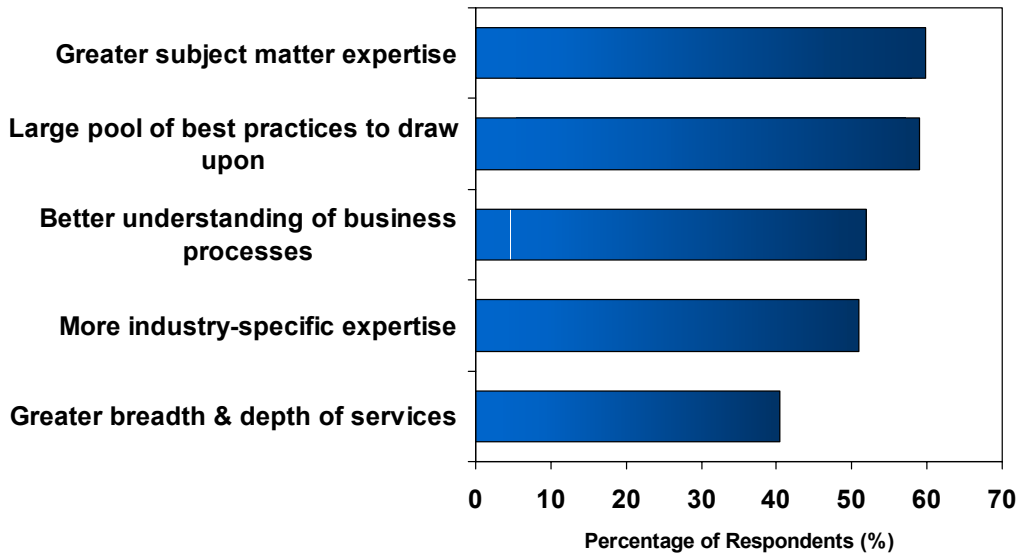
What Defines a Leader in HR Outsourcing?

HR outsourcing leaders are defined as those companies that rate highly in terms of displaying the attributes cited above. They have established credibility in the HR market through long-standing commitments to clients that evolve with their clients' needs, and they build on existing products and services to provide clients with greater resources for leveraging emerging opportunities.

IDC Canada has, through its ongoing research, identified the characteristics of HR service providers that are most important to Canadian businesses. The results are presented below in Figure 5.

FIGURE 5

Expected HR Service Provider Characteristics (Top Five Responses)



N= 153 Canadian businesses

Source: IDC Canada, 2005

The key to assessing leading vendors in the HR outsourcing services market is to evaluate providers according to criteria that are critical to the client's individual requirements. The ideal vendor will demonstrate outstanding capabilities in the areas that are of critical importance to your business and its continued success. HR leaders should be evaluated on their ability to provide end-to-end services as illustrated in Figure 6.

FIGURE 6

HR Outsourcing Vendor Leadership Requirements



Source: IDC Canada, 2005

CONCLUSION

What to Consider When Making the Decision to Outsource Human Resources

Outsourcing HR functions or processes is a viable decision for businesses, particularly those whose internal HR department has reached the limit of its effectiveness; businesses that want to access new programs or services (but don't want to incur the required investment), or those that want to focus on core competencies.

The decision to outsource HR functions should reflect the following steps:

- ☒ Determine how much your organization is willing to outsource and what contract and/or relationship type best typifies these characteristics.
- ☒ Determine which supplier attributes (such as HR process expertise, consulting services, global capabilities, etc.) are top priorities, which attributes are nice to have, and which ones are not important. Use the subsequent rankings to judge vendors accordingly.
- ☒ Always keep the goal of continuous process improvement in mind. This applies to the assessment of functions that are still managed internally as well as those that have already been outsourced. The drive towards continuous improvement applies to internal operations as well as externally-managed functions to fully realize the benefits of best practices in business operations.
- ☒ Focus on the business objectives for the HR organization. Examine HR goals against the overall goals of the organization. Casting a wide net that includes outsourcing options will give the business more sources from which to realize the best strategy to achieve its objectives.
- ☒ Determine where outsourcers can provide value within the HR function and then engage with external providers to achieve outcomes that provide sufficient value for both parties in the relationship.

The drive towards continuous improvement applies to internal operations as well as externally-managed functions

Why Human Resources Outsourcing Should Be Considered

The outsourcing decision is extremely complex and requires significant investment from all corporate stakeholders. This should not, however, be considered as a deterrent for businesses.

IDC Canada believes that the outsourcing of human resources functions has reached a stage where suppliers can provide a compelling service offering that rivals the established capabilities of internally managed HR operations.

HR outsourcers are well positioned to assume the responsibilities of internal HR departments because they have the ability to provide solutions that are difficult for internal HR departments to match. By utilizing the skills and resources of HR

outsourcers, businesses are able to establish best practices in the areas of payroll and compensation, HR administration, staffing, benefits administration, and organizational and employee effectiveness, while aligning themselves to take advantage of emerging opportunities.

Businesses that believe their employees to be a key differentiator should evaluate HR outsourcing as a means of providing HR services that exceed the capabilities of internal HR organizations.

APPENDIX

DEFINITIONS

Business Process Outsourcing (BPO)

BPO involves the transfer of management and execution of one or more complete business processes or entire business functions to an external service provider. The BPO vendor is part of the decision-making structure surrounding the outsourced process or functional area, and performance metrics are primarily tied to customer service and strategic business value. Strategic business value is recognized through such results as increased productivity, new business opportunities, new revenue generation, cost reduction, business transformation, and/or the improvement of shareholders' value.

Processing Services

Processing services involve the transfer of management and execution of activities or single business processes that tend to be high volume and automated to an external service provider. Performance metrics for processing services are primarily tied to accuracy, timeliness, and efficiency of high-volume service capabilities. Processing services are typically standardized and involve little or no customization.

Human Resources Outsourcing (Managed HR)

IDC defines Managed HR services as the outsourced services that support the core HR activities and business processes associated with HR administration, including:

- Payroll and tax administration
- Health and welfare benefits administration
- Pension and retirement benefits administration
- Employee and manager self-service delivery services
- Employee communication design and administration
- Services related to the support of an HR/employee portal

The following two segments make up the relevant HR sub-processes:

- ☒ Benefits. Benefits includes activities related to the tracking and administration of employee health and welfare benefits, defined benefits, and defined contribution pension/retirement benefits, including accounting for funds contributions, electronic funds transfer, and printing and delivering statements.
- ☒ Payroll. Payroll includes activities related to the tracking and administration of employee time and attendance records, withholding calculations, tax filings, electronic funds transfer, and printing and delivering statements.

Methodology

This white paper is based on research conducted as part of IDC's ongoing research into the BPO and HR outsourcing markets, detailed interviews with Canadian organizations in 2004, briefings from Ceridian Canada and other HRO providers.

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