

Hidden Cost of Non-Integrated HR Service Delivery

A Market Research and Thought Leadership Study

Summary of Key Findings

June, 2006



Background on Seams

For most U.S. organizations, HR service delivery has been designed on a process by process basis, with the goal of optimizing the performance of the individual process. Companies may ask, "How do I build the most efficient payroll process?" or "How do I build the most effective health and welfare benefits process?" To respond, a company will assemble a service delivery infrastructure of systems, employees, vendors, outsourcers and business rules. By and large decisions on service delivery infrastructure minimize the issue of having processes interact.

However, Human Resources (HR) processes are interdependent. For example, payroll processes must ensure that Health & Welfare benefit deductions are excluded from paychecks. Similarly, Health & Welfare benefits eligibility processes depend on understanding which employees are "on payroll."

HR service delivery is made less efficient and effective by the complexity of the infrastructure. Companies must develop systems interfaces, manual workarounds, or purchase additional software to address the integration points among processes. We term the inefficiency between two processes as resulting from a "seam" between them.

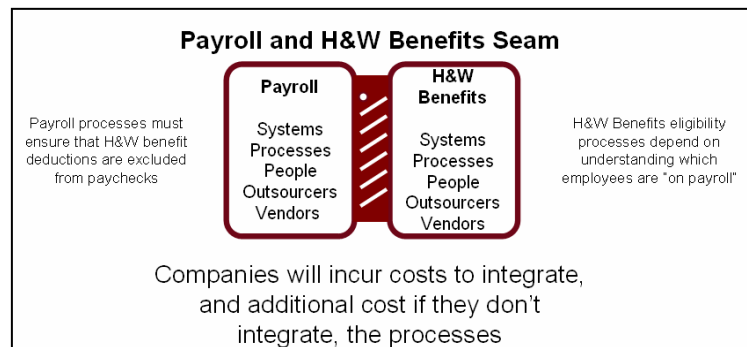
Moreover, company management structures or mergers and acquisitions can produce multiple service delivery infrastructures for a single company or a single process. It is not unusual for a company to have several Time and Labor Management processes and multiple Human Resources Information Systems (HRIS) systems. Also, the advent and growing prominence of outsourcing has given companies the opportunity to perform parts of a process internally and part externally. This generally will result in HR service delivery seams that are more complex and less efficient.

Methodology

In February of 2006, ADP commissioned PricewaterhouseCoopers to conduct a market research and thought leadership study to document the potential "hidden costs" of a non-integrated HR service delivery strategy. ADP believes that non-integrated (multi-vendor or multi-platform) payroll and HR service delivery results in higher costs than a fully integrated service delivery platform because of various cost and service delivery inefficiencies. The diagram below illustrates the Payroll and Health & Welfare Benefits Seam -- how we are defining service delivery, why there are process interdependencies and some potential outcomes of having a seam.

For this study, PwC assessed the existence of and the inefficiencies associated with four different HR service delivery seams:

1. Payroll and HRIS Seam
2. HRIS and Health & Welfare Benefits Seam
3. Payroll and Health & Welfare Benefits Seam
4. Payroll and Time & Labor Management Seam



To analyze the costs and impact of seams, PwC conducted two separate research efforts. First, ten companies identified by the PwC team as having a fully-integrated service delivery platform were interviewed to understand service delivery before and after integration. These "best practice" interviews took place in April and May. The companies interviewed were in different industries and had varying employee sizes.

Second, telephone surveys were conducted between late March and early May 2006 with 141 large organizations (more than 1,000 employees) throughout the United States. Multiple industries were represented in the survey and 60% of organizations had less than 5,000 employees while 40% had more. Nearly half of the respondents were functional managers while 46% were either vice presidents or directors.

The telephone interviews asked roughly 30 questions of all respondents. The questions were customized to a specific seam. All respondents had detailed knowledge of service delivery for that seam. For example, respondents who reported having detailed operational knowledge of Payroll and HRIS were asked questions about the Payroll and HRIS seam while respondents who reported having detailed operational knowledge of HRIS and Health & Welfare Benefits were asked a set of questions on HRIS and Health & Welfare Benefits seam.

Key Findings

The five key findings of this research effort are:

1. There appears to be a tangible cost associated with Non- Integrated HR service delivery integration seams – estimated by respondents to be more than \$100 per employee per year
2. Primary drivers of additional costs appear to be consistent for all HR Service Delivery seams: systems customizations, manual processes (for data integration, reporting, etc.) and additional software
3. There are a surprisingly high number of companies without self service and these companies experience reduced HR service delivery performance, increased dissatisfaction and increased costs

4. Time and Labor Management is decentralized and lacks a formal process owner (making it seem like an organizational orphan) in many organizations.
5. Companies with centralized service delivery strategies (all functions in a shared service center or all functions outsourced to a service provider(s)) state a higher satisfaction with HR service delivery, and fewer expectations of incurring future costs related to the seams

Finding #1: Seams Cost More than \$100 per Employee

Organizations estimated the cost per year that they spend to provide integration among the seams. The cost estimates include labor, software, services and the potential to make substantial erroneous payments as they tried to manage information and processes that cross the seams. Each respondent estimated the costs only for the seam that was the topic of the interview. Results for the four seams that we surveyed are below:

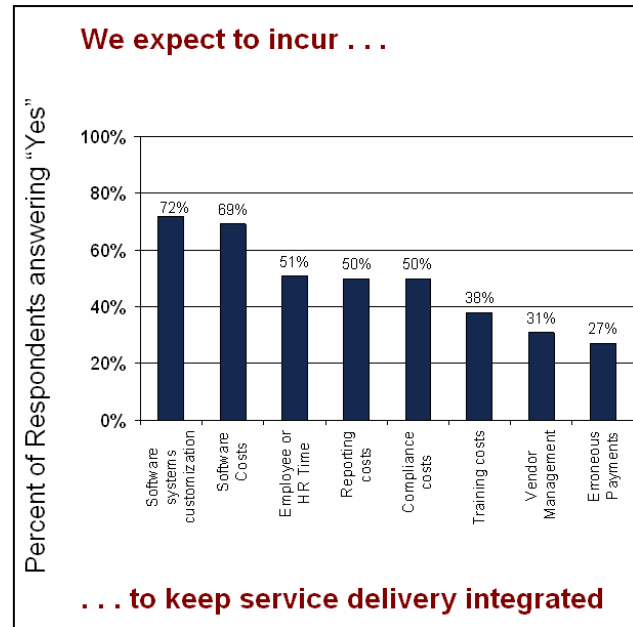
Seam	Additional Cost per Employee
Payroll and HRIS	\$29
Payroll and Health & Welfare Benefits	\$25
Payroll and Time & Labor Management	\$25
HRIS and Health & Welfare Benefits	\$25

A company that has a completely non-integrated approach to all four seams will incur additional costs equal to approximately \$104 per employee per year to integrate service delivery. Taking into consideration Saratoga's independent analysis of HR & payroll budgets, \$104 per employee represents approximately 6% of the total HR & payroll department budgets. Despite being a significant portion of the HR budget, there is a real lack of awareness of the impact of managing information and processes across the seams. In fact, our telephone interviews revealed that many respondents initially believed their organization had an integrated HR delivery solution. When further probed on service delivery, respondents began to recognize that they, in fact, had seams.

While working to reduce or eliminate the impact of these seams may in many instances be motivated by a desire to save money, that is not always the case. In our "best practice" interviews six of the ten companies claimed to have saved money by reducing seams, the other four companies focused on other improvements. The issue for many is one of functionality -- moving from an older system where a lot of money is spent to keep service delivery operating to a newer system where money is spent to drive higher value. The \$104 per employee can be converted into an investment in improved functionality such as better decision making, more robust data & reporting, additional applications, etc.

Finding # 2: Primary Drivers of Seam Inefficiency Are Consistent

Across all four seams examined, respondents identified the same frustrations with seams and the same drivers of future costs. Nearly seven out of ten organizations anticipate having future costs for systems customization or software costs. Over half expect to incur costs related to employee or HR administrative time, reporting and compliance. More than one in four expect to incur erroneous payroll or benefits payments as a result of seams! That is, they expect that the existence of the seam to create potentially costly and unpredictable errors.



According to respondents, most companies expect to take multiple actions to integrate, or eliminate, the seams. The three most common actions organizations report taking to integrate service delivery include:

1. Customizing internal and external systems
2. Employees or vendors undertaking manual steps
3. Adding new systems specifically to integrate existing systems.

It is these actions that drive the \$104 per employee per year cost. Whether the process is automated or manual, significant organizational resources are consumed to manage across the seams. Companies can either strive to eliminate these costs or redeploy their resources to other investments, improving the overall experience.

Organizations report being dissatisfied by seams. Respondents are slightly more satisfied with service delivery basics such as responding to life events and integrating data and least satisfied with the more complex tasks such as integrating employee self service, manager self service, and reporting. Every impact assessed scored less than a 4.0 on a 6.0 point satisfaction scale, and we consider a 4.0 the minimum score for satisfaction.

Finding #3: There are a Surprisingly High Number of Companies without Self Service and These Companies Experience Reduced HR Service Delivery Performance, Increased Dissatisfaction and Increased Costs

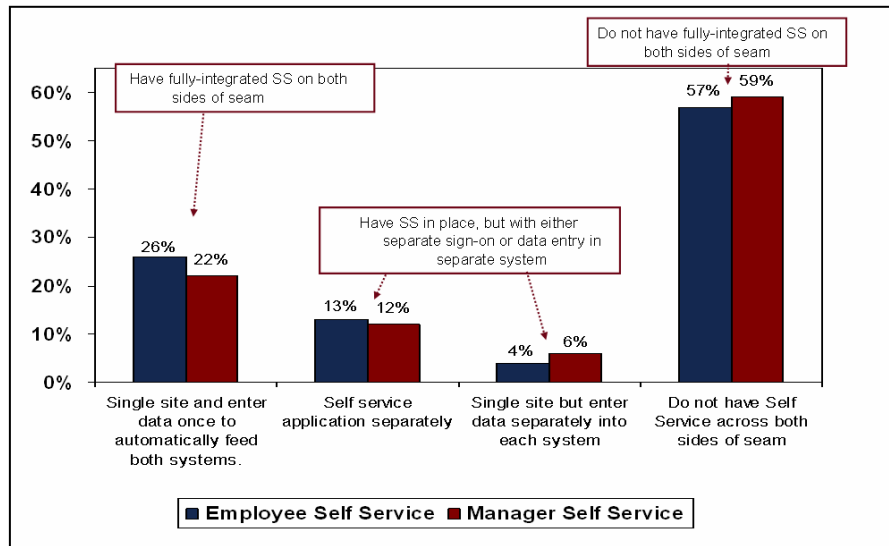
Respondents reported that a surprising lack of self service exists across seams. While most companies have some degree of self service, approximately 60% of respondents did not have self

service on both sides of the seam. This result holds true for both employee and manager self service, as shown in the chart below.

Self service appears to be a source of great dissatisfaction. It is the primary predictor of whether a company will be satisfied with HR service delivery, satisfaction with seam integration (e.g., data, reporting, life events) and whether a company expects to incur future costs related to integrating the seam (software customization, software, etc.). Companies with a single self service site for both access and data entry have higher overall service delivery satisfaction, increased satisfaction with issues impacted by seams and decreased expectations of future seam related costs. The key is that self service is integrated across multiple functions.

In every instance, respondents without self-service expect to incur incremental costs versus

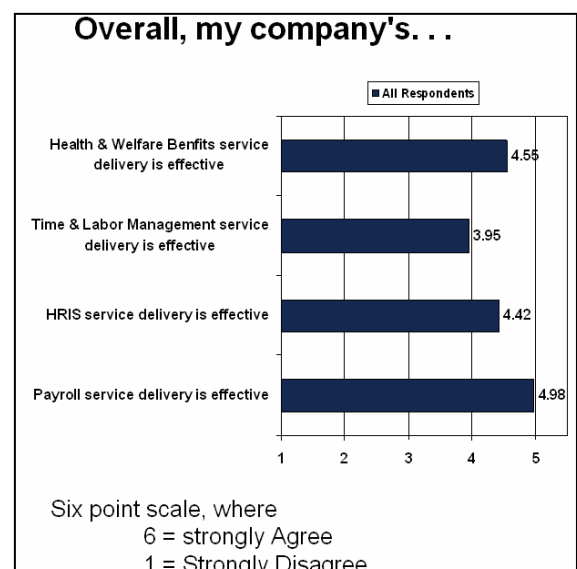
those who do have self-service. Companies that do not have self-service for both sides of the seam are twice as likely to expect to incur additional costs related to reporting. This may not be a direct “cause and effect” relationship and self service itself may not be the cause of satisfaction. However, providing self service that bridges multiple disciplines requires additional back-end integration in order to function as expected, and this integration may be the key to greater satisfaction.



Key Finding #4: Time and Labor Management is an Organizational Orphan

Respondents gave the lowest effectiveness scores to Time and Labor Management (TLM) service delivery. The more senior the level of the survey respondent, the more dissatisfied he or she was with this process.

Perhaps the low effectiveness is due to more limited organization control over the TLM process. Anecdotally, no one appears to be responsible for managing TLM, and none of the respondents in our telephone survey reported being the “head of TLM.” Rather, TLM respondents were typically part of Payroll with split responsibilities to both Payroll and TLM.



Since 80% of “best practice” interviewees reported direct headcount reductions after integration (primarily from manual data entry and timekeeping), non-integrated TLM systems would tend to have higher operating costs, slower processing time and increased likelihood of error than fully integrated TLM systems.

Many TLM systems today are still “black box” systems that are internally developed and / or managed and are difficult to customize. These systems are typically implemented without robust tracking capability, organizational structure codes, or linkage with data warehouses, HRIS, payroll, benefits platforms or enhanced reporting tools

Finding #5: Companies with centralized service delivery strategies (all functions in a shared service center or all functions outsourced to a service provider) state a higher satisfaction with HR service delivery, and fewer expectations of incurring future costs related to the seams

Survey respondents reporting the lowest levels of satisfaction were those that internally deliver HR services, not those that outsource. Companies with a consistently centralized approach to service delivery (whether outsourcing or shared services) show higher degrees of satisfaction with HR service delivery. Respondents at companies that utilize outsourcing believe that executives and line managers are very satisfied.

Those companies with a centralized approach also are more satisfied with data integration and reporting. Fewer of these companies expect to incur future incremental costs. With the exception of vendor management costs, companies that outsource expect to incur lower costs related to seams than companies that do not outsource.

Companies delivering functions internally without a Shared Services Center consistently show the lowest satisfaction with overall HR service delivery. These companies are also least satisfied with the ability to integrate data, reporting, and self service.

	Overall	Centralized	Internal+ Partial
	N 141	53	88
Overall, my company's...			
HR Service Delivery is effective	4.17	4.58	3.93
HR Service Delivery is cost-efficient	4.19	4.41	4.06
HR Service Delivery is timely	4.54	4.65	4.48
Line Managers believe that our HR service delivery is effective	4.13	4.30	4.02
Senior Executives believe that our HR service delivery is effective	4.44	4.67	4.31

Summary

In assessing the existence of HR service delivery seams there is clearly an opportunity to help companies remove inefficiencies. Respondents expect to spend up to \$104 per employee per year (or, we estimate based on Saratoga data, up to 6% of their HR and Payroll budgets) to overcome the inefficiencies associated with HR service delivery seams. To do so, these companies are frequently customizing software, building manual processes for data integration and reporting, and buying additional software. A quarter of respondents even expect that the

seams will cause erroneous payments. Of the four individual processes we assessed, Time and Labor Management appears to be the greatest opportunity for service delivery improvement, yet the costs and drivers of seams are the same across all seams.

It appears that companies can take several courses of action to improve overall HR service delivery satisfaction and mitigate the impact of seams. Companies that have an integrated manager and employee self service infrastructure addressing both sides of a seam demonstrate improved HR Service delivery satisfaction and reduce the impact of the seam. Also, companies that adopt a centralized service delivery approach, including either outsourcing or shared services, show similar improvements.

Despite the impact of HR service delivery seams, there also appears to be a real lack of recognition by respondents that seams are having such an impact. Respondents appear to accept that systems customizations, manual processes and poor self service are "part of life." In fact, many respondents initially believed that they had an integrated service deliver infrastructure (but changed their views after additional probing).

It is appears that companies seek to remove HR service delivery seams, but not always with the intent of reducing costs. While some companies reduce costs, many are looking to drive additional investment, in self service applications, in new HR applications, in better reporting and more. Ultimately, these investments or a similar decision to outsource multiple processes can have a positive impact on the business even though the total cost of operating the systems may be similar to older non-integrated infrastructure.