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Barbara Schaefer,
Union Pacific senior VP,
human resources

PULLING THE PLUG

A gloomy
forecast
for HRMS?

LESSON PLAN

Business
supports
after-school
programs

Pulling *the* plug

The complexity of **INSTALLING AND MAINTAINING HUMAN RESOURCES MANAGEMENT SYSTEMS** is prompting many companies to **BYPASS THEM ALTOGETHER**. *Software companies could find themselves endangered, and are* **WORKING HARD TO LOCK UP CONTRACTS** *with outsourcing giants.*

By Samuel Greengard

I'T'S NOT EVERY DAY THAT YOU JUNK a human resources management system and hand more than half your staff their walking papers. But three years ago, Regus Americas, the U.S. branch of a 2,000-employee firm that provides fully furnished executive suites to companies in 50 countries, embraced the strategy without hesitation. With 4,000 business centers scattered across the globe, managing technology and administrative tasks was expensive and inefficient. What's more, it required more IT staff than the firm could muster.

Regus decided to outsource virtually all human resources activities, including payroll, training, benefits administration and personnel administration. However, during the vendor-selection process, the HRMS platform itself wasn't a consideration. "We really weren't concerned with the specific platform or vendor for the HRMS," says Matt Dean, a vice president at Regus Americas. "We were only interested in a system that could address our specific needs."

A dagger to the heart of HRMS providers? Perhaps. A complete upheaval that's threatening to shake up the industry and leave major software providers scrambling? Most definitely. Boston market research firm Yankee Group reports that human resources business process outsourcing—which involves outsourcing of entire business processes rather than isolated IT tasks—will grow from 17 percent of the U.S. human resources market today to 30 percent by 2008. Gartner Dataquest projects that HR outsourcing will be a $37.8 million business by 2007.

Driving this trend is a very simple fact: "It is becoming extremely complicated to put together and sustain a state-of-the-art HR delivery system," says Naomi Bloom, managing partner at Bloom & Wallace, a consulting firm in Fort Myers, Florida. "Handling all the different aspects—software, system integration and maintenance, call

> *"It is becoming extremely complicated to put together and sustain a state-of-the-art HR delivery system."*
> ◀ **Naomi Bloom, managing partner at Bloom & Wallace**

centers and more—requires tremendous resources. It's more than a lot of companies can handle."

While organizations have long turned to service providers to address niche needs in payroll and benefits administration, only recently have many begun using a comprehensive outsourcing strategy. Some, such as Regus, are scrapping internal systems altogether. Others, particularly small and medium-sized firms that haven't previously relied on a major HRMS package, are leapfrogging directly to first-tier systems in the same way that countries like China and Kenya have skipped land-line communications and headed directly to cellular.

The fallout is enormous. In a shrinking market for HRMS—a trend that's expected to continue until at least 2005—vendors are jostling to set up arrangements with services firms such as Accenture, ADP, Ceridian, Convergys, EDS, Fidelity, Genesys, HRAmerica, IBM, TriNet and Hewitt Associates, which has just acquired Exult. Yet the finances for these deals might not be enough to keep all the HRMS vendors in the black. Bloom, for one, sees stormy weather on the horizon.

THE RUSH TO BPO

THE FOLLOWING DYNAMICS are the main contributors to the enormous growth in human resources business process outsourcing.

COSTS: Naomi Bloom, managing partner at consulting firm Bloom & Wallace, says that the goal is to slash costs directly and, when possible, make them predictable and variable with business activity. Outsourcing offers an opportunity to "generate revenues [cost savings] from what was a cost center."

EXPERTISE: Business process outsourcing offers organizations an opportunity to gain access to potentially best-in-class HRM consulting, products and programs as well as human resources management delivery systems.

TIME TO MARKET: Companies want to see improvements in human resources management and boost service levels. However, as Bloom puts it: "Be careful what you wish for. You don't want to make poor hiring decisions faster and more cheaply."

REDUCTION OR MITIGATION OF RISK: Today's complex web of laws, restrictions and regulatory requirements can prove taxing for many organizations. There are also security concerns and international data-privacy issues to manage. Outsourcing can reduce, if not eliminate, many of the challenges and risks associated with today's business environment.

FOCUS: Human resources business process outsourcing helps organizations focus on key strategic issues rather than a mountain of administrative tasks. It allows workforce-management executives to become decision-makers and even partners in the operation of the business.

OUTCOMES: The effective use of BPO can improve human resources management practices and lead to better use of internal capabilities, including human capital. Advanced analytics can provide insights into trends, challenges and opportunities. —S.G.

"Those selling software directly to companies should be concerned," she says. "If they do not wind up on the platform of key HR outsourcing providers, they could find themselves endangered."

At the same time, companies large and small are finding that by outsourcing, they're able to trim staffing levels and retain only the executives and managers who contribute to the bottom line. "The vast majority of HR functions within any given company provide little or no strategic value," says Steve Larson, a regional practice leader at Watson Wyatt Worldwide. Ultimately, "it's all about core competencies and dollars."

CORE CONSIDERATIONS

Last April at a conference in Las Vegas for human resources executives sponsored by Oracle, Bloom stood in front of an audience of about 80 key decision-makers and had the audacity to announce that the outlook for software providers—and many professionals in the workforce-management arena—is gloomy and getting gloomier. "Senior management has had it with one more business case on why HR needs more time, more money, more vendors and more consultants just to sustain the HRM delivery system," she said.

When Bloom talks, people listen. Since the 1960s, she has commanded the attention of top corporate executives and has helped guide them through the dizzying world of information technology. What's more, she has played an instrumental role in helping ERP and HRMS providers define and design their commercial products for a fast-changing marketplace. At once engaging and self-aggrandizing ("There's nobody in this space that I haven't worked as a consultant with," she boasts), Bloom is not ready to fade away.

"The top vendors will swear that business process outsourcing is not affecting them, but they know that it's impacting their business in a big way," Bloom says. Over the last decade, these software firms have discovered that they must churn out a constant stream of upgrades, patches and new platforms. In today's ultra-competitive business environment, a company's image is every bit as important as its offerings. Although many features in a typical application go unused or underused, no ERP or HRMS vendor can afford to gain a reputation as a laggard.

Managing these systems is often a nightmare. Every couple of years, most companies find themselves grappling with a major upgrade. In addition, many organizations struggle with adding niche best-of-breed applications to the mix to create the specific function they desire. In the end, the complexity of choosing applications, assembling them and getting the software to work efficiently often proves overwhelming to management and IT. "Many companies do not manage infrastructure well," Watson Wyatt's Larson says.

Yet BPO isn't only about hardware and software. After all, an organization can turn to an application service provider to manage information technology and get the software it wants. Today, virtually all major ERP vendors,

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including SAP, PeopleSoft and Oracle, offer hosted solutions directly through outside providers. A BPO relationship encompasses the actual work that an organization typically handles itself, including payroll processing, applicant tracking, training and benefits administration.

The end game is to manage all the processes transparently while presenting an appealing and functional Web interface or phone system for workers. "As an employee, I'm not interested in dialing into four 800 numbers, coping with three different online protocols and sign-in procedures and navigating several Web sites. I want everything presented in a uniform and seamless way," Bloom says. To be sure, companies that find themselves juggling internal software and systems, outside service providers and piecemeal outsourcing are growing increasingly frustrated. "They're viewing comprehensive outsourcing as an attractive concept," Bloom notes.

OUTSIDE IN

The list of companies that have turned to human resources BPO is growing by leaps and bounds. Exult, which earned $480 million in 2003, brings clients Bank of America, BP, International Paper, Circuit City Stores and Prudential Financial to its merger with Hewitt. Accenture claims BT (formerly British Telecom) and Borden Chemical. IBM has grabbed Procter & Gamble. And smaller providers such as TriNet, in San Leandro, California, are signing up medium-sized and small firms that couldn't previously afford first-tier applications.

BPO firms claim that they can cut costs by 15 percent to 25 percent while streamlining and improving business processes. Diane Shelgren, chief operating officer for North America Accenture HR services, points out another key factor: "It's possible to gain a level of business and technical expertise that most organizations cannot afford. Hiring specialists or developing internal knowledge and expertise is an expensive and challenging task."

Although each offers a different wrinkle (some, like IBM and EDS, have migrated from the IT world into human resources; others, such as Ceridian and Accenture, are expanding out from their roots in human resources), the general concept is pretty much the same. "The whole point is to consolidate multiple relationships into a single relationship," says Martin Babinec, president and CEO of TriNet. "It is a way to free up internal resources so that management can stay more focused on big-impact issues."

At Regus, that is clearly the goal. Since the company's inception in 1989, it had relied on internal systems to deal with workforce-management matters. A centralized human resources department handled tasks for all of its global locations. Then the company expanded to the United States in 1999. Three years later, Regus turned to human resources BPO through TriNet. As a result, it was able to slash its staffing within human resources by approximately 60 percent and trim its overall administrative expenses. The only human resources function it continues to handle in-house is recruiting. A human resources staff of two now manages its entire U.S. operation.

Dean hasn't looked back. "Because we have so many different locations in so many places—all with different state requirements and varying workers' compensation laws—administering HR is a huge challenge," he says. "Outsourcing saved us from hiring a huge staff to understand all the rules and regulations for 30 plus states. It has helped us ensure that we are in compliance with federal and state tax regulations." He believes that the company would also require a 40 percent larger IT staff if it handled everything internally.

But the biggest benefit, Dean says, is avoiding multiple applications, intranet sites and scattered data. "Everything that takes place—upgrades, patches, security fixes and changes to the tax code or state labor laws—is completely transparent (invisible) to us," he says. "The only thing we're involved with is the selection of benefits providers, such as health care and life insurance." Employees access data through a Web-based portal at work or from home.

Another company that has embraced human resources BPO is Procter & Gamble. In September 2003, it signed a 10-year, $400 million global agreement with IBM Business Consulting Services for payroll processing, benefits administration, compensation planning, expatriate and relocation services, travel and expense management, and human resources data management. IBM also provides application development and management of P&G's human resources systems, including an SAP HRMS and employee portal. About 800 P&G employees were offered jobs at IBM as it took over shared services centers in San José, Costa Rica; Newcastle, England; and Manila, Philippines.

Jim Holincheck, a research director at Gartner Inc., says that executives are no longer hesitating to hand over various applications and processes to an outside provider. "For years, many companies have used service providers and outsourcers in niche areas, and they have discovered that it works. They are beginning to grow comfortable with the idea. The question now is whether we will see companies migrate to a total HR business process outsourcing model. That is the next frontier."

The way Bloom sees it, human resources BPO is part of the natural evolution of the workplace and IT. In the 1960s, companies typically wrote their own software code and built their own systems. At the time, shrink-wrapped commercial software was almost as abstract an
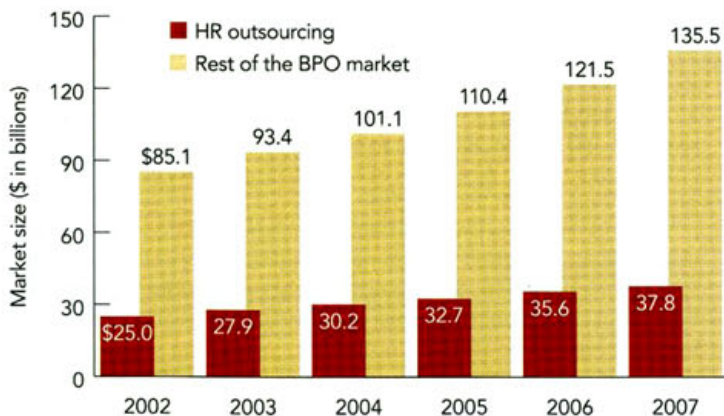
Diane Shelgren

Jim Holincheck

Worldwide BPO Market Size and Forecast, 2002 to 2007

The business process outsourcing market is poised for rapid growth over the next few years. HR outsourcing is following suit.

Market size ($ in billions)

Year	HR outsourcing	Rest of the BPO market
2002	$25.0	$85.1
2003	27.9	93.4
2004	30.2	101.1
2005	32.7	110.4
2006	35.6	121.5
2007	37.8	135.5

Source: Gartner Dataquest (July 2003)

idea as e-mail and Web pages. During the 1980s, as personal computers became an office mainstay, off-the-shelf applications began to appear. Then in the mid-1980s, the use of commercial software finally surpassed homegrown applications. "A survey of executives in 1980 would have found a widespread belief that commercial software wasn't good enough and would take years to reach mainstream adoption," Bloom says. "They couldn't have been more wrong."

Bloom's point, of course, is that adoption rates almost always exceed expectations. Now the same thing is happening in the HRMS space, she says. Market research firms like Gartner, Yankee Group and IDC, while predicting steady growth in the BPO space, don't see the tsunami-like wave that's forming. "The problem is that they interview people who reflect past and current attitudes rather than the dynamics of the marketplace."

If Bloom has her finger on the pulse of the situation—and she's known for doing just that—the ERP and HRMS marketplace could see plenty of turmoil in the coming months. "The heyday is gone," she says. "The good news for vendors is that if you're a global provider, there are still a lot of underdeveloped countries left to sell your products to. Already, the Big Three [SAP, PeopleSoft and Oracle] are scrambling to tap into markets in China, India, Africa and South America. The bad news is that the U.S. market is heavily penetrated and there isn't going to be significant growth."

FITTING IN WITH BPO

THE HUMAN RESOURCES BUSINESS process outsourcing model is based on a very simple concept: an outside provider that specializes in management and delivery of HRMS and other systems can do the job more efficiently than the company contracting with it. "Economies of scale and a core focus serve as a key advantage," says Jim Holincheck, a research director at consulting firm Gartner Inc.

Yet putting the theory into practice requires an emphasis in several key areas. Naomi Bloom, managing partner at consulting firm Bloom & Wallace, says that a BPO provider must find clients that fit its business model. It should replace the client's workforce and facilities with consolidated, lower-cost facilities and staff; operate from low-cost, high-quality service locations; find professional, highly trained staff; optimize its own cost structure and human resources management techniques; and use technology and lower-cost tools, such as Linux and grid computing, to provide better service at a profit.

In most cases, human resources BPO providers build such a model through a one-to-many approach, Bloom says. They are able to standardize on a single technology platform that offers entrée to an array of capabilities. Essentially, a buyer checks off the features required, and they're switched on and available through an enterprise or employee portal. When new releases and upgrades occur, the BPO provider simply adds the information.

Yet in order to succeed, it is often necessary for a company using these services to adjust its underlying business processes and rules. Part of the payoff from BPO systems is that users presumably benefit from efficiencies built into the provider's own highly automated business processes. This can include subcontracting and relying on third-party outsourcing. "The goal is for client organizations to adopt a best-practices approach," Bloom says. —S.G.

The recent spike in merger and acquisition activity within the software industry supports Bloom's argument. Facing an increasingly saturated marketplace, software providers now are confronting the prospect of selling their products directly to BPO providers. The economics of the business model and licensing agreements translates into lower revenues, she says. Those that fail to forge deals with major BPO providers could find themselves squeezed out of business. Already, SAP, PeopleSoft, Oracle and Lawson have begun to pursue BPO providers with maniacal fervor.

Exult had exclusive arrangements in place with SAP and PeopleSoft, while Hewitt uses PeopleSoft alone. Nevertheless, clients of the merging companies will see no changes in their HRMS platforms "for the foreseeable future," a Hewitt spokeswoman says. ADP has begun offering mySAP ERP Human Capital Management and SAP NetWeaver products in its BPO. HR America uses Ultimate Software to power its underlying HRMS. Some industry observers, such as Philip Fersht, a senior analyst for business process outsourcing at Yankee Group, believe that too many new players and a lack of focus on market segments equals market saturation and turmoil within the next year or so.

PROCESSING THE FUTURE

For organizations eyeing human resources BPO, the current state of affairs can produce high anxiety. Costs and ROI are only part of the equation. Moving terabytes of data from one HRMS software application to another—even one that an outside company is managing—can torpedo productivity, costs and even daily operations. What's more, signing a 5- to 10-year deal is not for the faint of heart. That's because companies migrating to a human resources BPO model must often change practices to take advantage of the technical capabilities of the service provider. "Outsourcing doesn't replace solid business processes and good decision-making," Holincheck says. Understanding the intricacies of the business model—including whom a BPO provider does business with—is essential, he says. The contract firm might outsource operations to India or the Philippines, which may or may not be acceptable. The specifics, he says, should be defined in an ironclad service-level agreement.

Bloom and others say there's no turning back. Organizations increasingly are questioning the money they're spending on in-house HRMS. They also recognize that there is a need to stay focused on critical strategic areas, including benefits, performance management, leadership development and knowledge management and that these tasks demand far more attention and resources than they can handle on their own. The basic trend is clear. "It's difficult to find a company that doesn't cringe at the prospect of upgrading its HRMS and managing the entire infrastructure to support human resources," Larson says. "The idea of handing off administrative tasks to another company is incredibly appealing. Like it or not, it's part of the future of the 21st-century enterprise." **wfm**

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