

# Measuring the Middle:

The Buyers' Perspective of Mid-Market HRO

HROA Research Report  
October 2008

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## INTRODUCTION

In August 2007 the HROA established the HROA Mid-Market Special Interest Group (SIG) to address the needs and specific areas of interest to the mid-market buyer of HR outsourcing services. Within the SIG, a Research and Tools subcommittee was formed with a mandate of establishing a base of mid-market relevant data and information. As part of that mandate, the sub-committee undertook a survey, the results of which are included in the subsequent sections.

## SURVEY METHODOLOGY

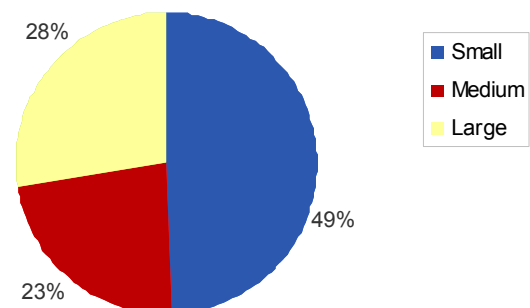
In developing the survey, one of the sub-committee's early objectives was to structure the survey in a manner to permit comparability to other, broader buyer surveys. That said, the sub-committee was careful to include in the survey questions addressing areas that might be of particular interest to the mid-market buyer.

The survey was distributed to roughly 5,000 potential respondents. Due to practical issues, this distribution list included respondents from other market segments. The survey was released in June 2008, with the response period closing in mid-August 2008.

In characterizing the respondents, we defined the market segments (Figure 1) as follows:

- Large market – over 15,000 employees
- Mid-market – over 3,000 employees but less than 15,000 employees
- Small market – under 3,000 employees

**FIGURE 1: Company Size: Number of Employees**



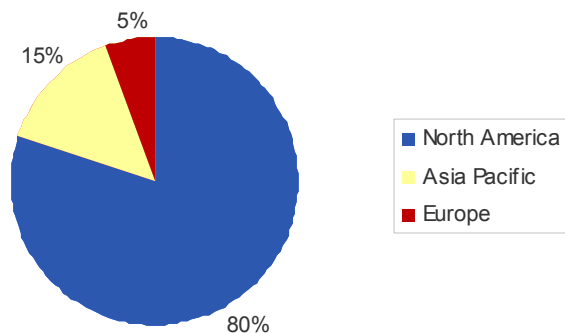
## Survey Methodology

We received 87 responses. Please note that, while issues and trends reported in our report were clear from the data, this is a limited sample set so readers should be careful in projecting conclusions across the mid-market segment. It is important to note that at the current time this may be the least clearly defined market segment. True to the sub-committee’s mandate, the results of this survey are the beginning of understanding this market, and we are not yet at a definitive point in identifying market trends.

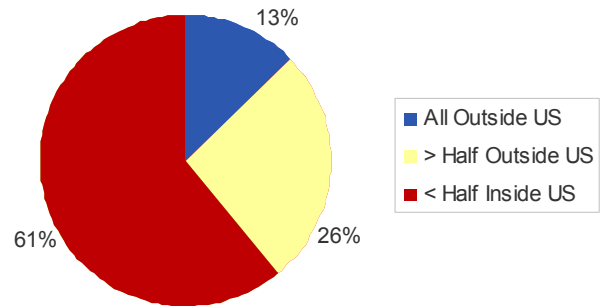
Interestingly enough, the single largest group of respondents was below our target group. Again this response reinforces the point that survey results, conclusions and perspective will warrant further research to better calibrate our market segment.

An additional interesting dynamic of our respondents was that while the preponderance are US based (Figure 2), they also represented a significant global perspective, in that they had material populations of employees outside of the United States (Figure 3).

**FIGURE 2: Headquarters Location**



**FIGURE 3: Employee Locations**



As a final point, note that roughly two thirds of respondents characterized themselves as HR professionals. This indicates that we have strong representation from the functional experts and those most likely making the key service delivery strategy and corresponding buying decisions.

## EXECUTIVE SUMMARY

The survey findings are summarized below; detailed findings are presented in the subsequent section.

### Market Penetration

Almost three quarters of respondents indicated that they engaged in some HR outsourcing. There was a clear correlation between size of organization and level of outsourcing. The larger the organization, the more likely to be outsourcing, including a higher likelihood of more comprehensive (or multi-process) outsourcing.

### Customer Satisfaction

While it appeared that a number of relationships had experienced initiation or stabilization periods, general satisfaction levels indicated that outsourcing undertaken to date has been largely successful. While re-alignment of an existing contract was normal, actual repatriation of services (i.e. taking an outsourced service and returning it to an in-house delivery organization) was relatively rare.

### Outsourcing Market Penetration

There were diverging points of view on the practicality of outsourcing of certain HR processes. Some of these perspectives were consistent with perspectives that exist in the large market segment; however, results did indicate that the small and the mid-market market buyers were generally not as well informed regarding the current state of the provider market and what opportunities there might be for a buyer to leverage provider capability.

### Market Standardization

A common belief in the provider community is that the mid-market segment is ideally suited for “one-to-many” service delivery (where providers use the same

infrastructure, processes, technology and people to deliver like services to multiple clients). The concept is that this market represents a leverage opportunity for a provider, which should positively impact the price the mid-market buyer has to pay.

In reviewing the survey results, the validity of this perception was called into question. Certain responses indicated dissatisfaction with the level of flexibility available from providers. There are at least two interpretations of the results. Firstly, this may reflect a perceived lack of flexibility in the relationship between the parties, so that when business conditions change, providers are not as nimble as an internal organization might have been to accommodate that change. Secondly, this may be more of a tactical issue where clients are frustrated by providers attempting to operate a one-to-many model and are therefore less able to adapt to specific or unique business requirements.

This is a fundamental question that warrants further study.

### Summary Conclusions

The mid-market does appear to be an active but still relatively untapped market. Buyers are not well informed on what the providers have to offer. And the providers may not be well informed on buyer requirements.

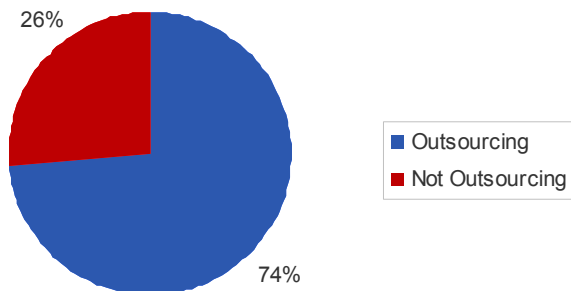
Clearly it is in the best interest of all market participants to ensure that the demand or buy-side of the market and the supply or provider-side of the market are better aligned. The HROA is uniquely positioned to help foster a higher level of dialogue to foster the greater alignment.

## DETAILED RESEARCH FINDINGS

### Penetration of HRO into the Marketplace

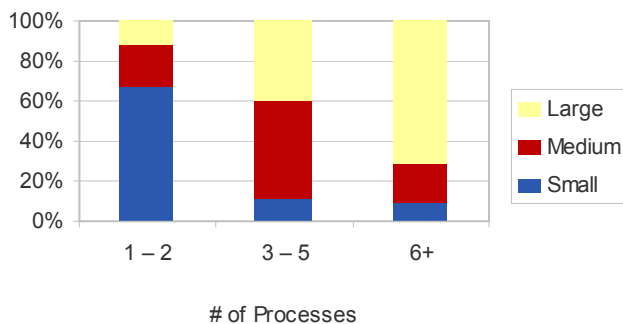
Various forms of outsourcing are quite common. Arrangements run the gamut from single process or niche outsourcing, to transactions that appear to be of a broader scope, including multi-process outsourcing.

**FIGURE 4: Use of Outsourcing**



In stratifying the responses by size, there was a clear trend correlating size of the buyer, and likelihood of a more broadly scoped HR outsourcing (Figure 5). While our survey was aimed at the mid-market, the demographics of our respondents allowed us to get a perspective on outsourcing across a number of the market segments.

**FIGURE 5: # of Processes Outsourced & Size of Organization**



Of note across the segments is that, although not as striking as in the large market, there is strong trend towards multi-process outsourcing in the mid-market, as evidenced by the roughly 55% of mid-market buyers who indicated they are outsourcing more than three processes.

Outsourcing as a business strategy appears to be proven in the mid-market segment; however, it continues to be on a smaller scale (when measured as number of processes). This finding indicates that there is greater opportunity still available in the mid-market. Buyers should consider what other market alternatives exist, while providers should examine their capabilities and go-to-market strategies in the context of the mid-market buyer's requirement profile.

### Setting and Attaining Objectives

Just over three quarters of respondents indicated that outsourcing was driven by a larger transformation effort. Responses indicated that outsourcing was frequently used as a tactic to deliver the transformation strategy. This is a perspective shared by the large market.

In reviewing responses regarding the setting of objectives, more than half of the respondents identified the following main HRO objectives:

#### HR service quality improvements

The single strongest objective (72% of respondents) confirmed that making HR service quality better was a key objective. This reflects a need to tactically "fix" service delivery performance and shows outsourcing as a tool to pragmatically address delivery issues.

## Detailed Research Findings

### Cost savings

About two-thirds (62%) of respondents confirmed that economics help to drive their decision making. Like any other buyer, this confirms that costs, and using outsourcing to drive costs out of the business, was an important lever.

### Focus HR on more strategic work

This was the highest rated “strategic” objective (at 60%). While the previously identified objectives tend to be more tactical, this objective is clearly about positioning HR differently in the organization and moving its role from processing of data and guardian of policy to a value-added contributor driving the business forward. While in HRO circles this objective is regularly referenced, the results confirmed that this is part of the dialogue for mid-market buyers as well.

### Standardized HR processes throughout the business

This was the last objective identified by at least half the respondents (at 52%) and again represented a very pragmatic challenge. It appears that companies in the mid-market are challenged as well by the issue of standardization and the implied benefits it represents (consistent and equitable business practices at lower costs). It is interesting to note that buyers saw outsourcing as an opportunity to deliver standardization.

Of interest as well was an objective relating to the acceptance of HR by the business as a strategic partner. This objective was rated by only 12% of the respondents. This may indicate that in smaller organizations expectations of HR becoming that strategic partner are less, and they are viewed more as a utility supporting the business. Considering that mid-market buyers are at least as challenged by staffing issues –

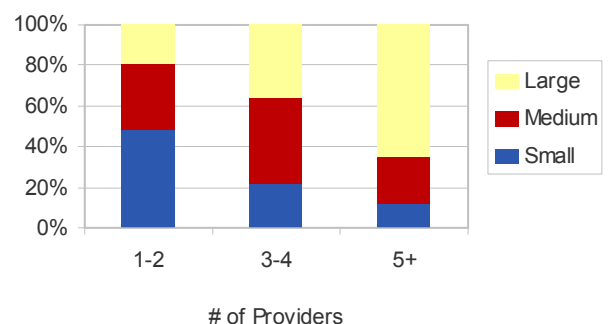
retention, talent management, etc. – and may not have the financial resources that larger organizations might have, this market may be the right place for HR to more aggressively push that agenda. Perhaps outsourcing is one of the levers to help achieve that goal.

Once set, objectives have generally been met. Rankings ranged from 80%-95% for having met the objectives (combining those rated “successful” and “neutral”). And while these objectives included cost savings objectives, a consistent trend indicated that, while cost savings were accrued, they were consistently below what had been factored into a business case. The responses show *planned* levels of savings tended to be in the 15%-25% range, while *actual* savings ranged from 5%-15%.

### **Service and Relationship Model**

Another clear correlation coming out of the survey was that smaller firms tend to use fewer suppliers (Figure 6). This may result from the realities of scale (where larger organizations by virtue of scale and geography would naturally have more providers) or sourcing strategies – larger organizations mandating multiple providers.

**FIGURE 6: Smaller Organizations Engage Fewer Providers**



## Detailed Research Findings

Provider selection criteria tended to focus most on issues of contractual terms, quality/expertise of staff, service level commitments and costs (in particular, implementation costs).

Also in the upper range of criteria was flexibility to meet specific needs. The evaluation of this response posed at least two considerations:

- Buyers are interested in flexible relationships with providers to better accommodate the impacts of changing business requirements – and those changes may be more strongly felt by smaller companies. The implication is that outsourcing may result in a less nimble delivery capability as there is now a contractual aspect and business agreement requirement to incorporate any changes (as compared to internally provided services which can be changed unilaterally); or
- As in the large market, buyers want flexibility at the very tactical or service delivery level in the definition of requirements and how those requirements are met. If this is the case, it calls into question a widely accepted belief across the provider community – that the big opportunity in the mid-market is delivering in a one-to-many (one provider delivering like services to a multiplicity of clients) model allowing providers to truly deliver scale advantages not only to the market but to their shareholders as well. This is a fundamental issue to be vetted in the marketplace as mid-market buyers position themselves to pursue outsourcing, and by providers as they position themselves to capture the market opportunity.

Issues such as transformative capabilities, cultural match and ability to service employees working outside the home country were ranked low.

Again this indicates a strong tactical orientation of mid-market buyers.

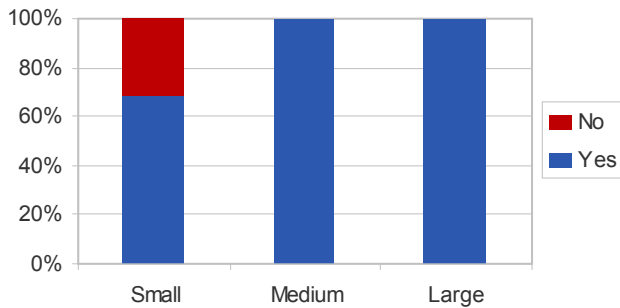
In constructing transactions there was another direct correlation across market segments considering:

- Use of Service Levels – where the qualitative aspects of service expectations are well defined and agreed upon;
- Fees at Risk – where the provider commits to penalties for service non-performance; and
- Formal governance – where people, processes and tools are in place to formally manage the service relationship.

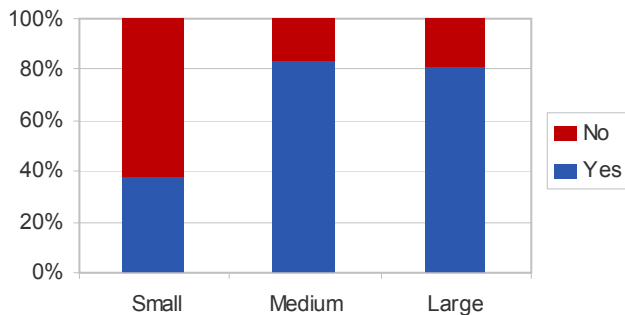
Mid-market and large market companies were clearly more developed than small market buyers in applying these mechanisms. It would likely be in the best interest of small market buyers to quickly progress their understanding of these concepts and begin to incorporate them into transactions going forward where they create value through enhanced service delivery and service delivery oversight. Well applied, they can be in the best interest of both parties and are underpinnings in establishing a sustainable service relationship (Figures 7, 8, and 9).

## Detailed Research Findings

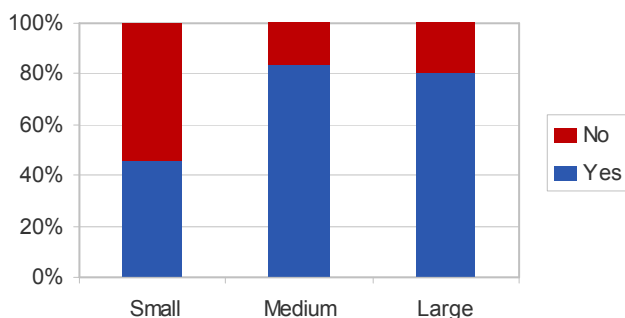
**FIGURE 7: Use of Service Level Agreements**



**FIGURE 8: Fees at Risk**



**FIGURE 9: Formal Governance in Place**



With regard to trends in outsourcing particular functions, mid-market responses confirmed common trends seen in the large market segment. Specifically, across the continuum of HR practices where one end of the continuum is defined as transactional processes and the other end as more consultative processes, outsourcing is much more common in the transactionally oriented processes, and tends to be more on an exception basis for the consultative items. For example, those most commonly outsourced processes include:

- Health & Welfare Administration
- Payroll processing & Tax filing
- Retiree services (pension & healthcare)
- Self-service and contact center
- HR information systems

Outsourcing processes such as Compensation, Expatriate Administration and Employee Relations are relatively rare.

It was interesting to note surprisingly large numbers of respondents (although well below the majority) indicated the absence of availability in the market of certain transactional processes; buyers felt that the market did not have the capability to deliver these services. This issue points to the need for better education of a broader spectrum of buyers so that buyers can make more informed decisions.

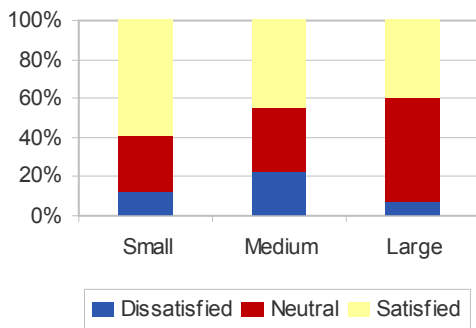
Offshore service delivery (in the context of this report, that means services delivered usually from Asia into the United States) was reported less than half the time. The use of offshoring increased, however, for more technology or office-based processing.

## Detailed Research Findings

### Satisfaction Levels

In an interesting twist, the small and large segments indicated the highest levels of satisfaction with outsourcing (Figure 10). In managing satisfaction it is always important to manage not only service performance but also expectation levels. Conjecture is that smaller organizations are (a) more likely to be receiving a standard service (one-to-many model); and (b) more likely to be able to manage their expectations.

**FIGURE 10: Satisfaction with HRO Varies by Organization Size**



Larger organizations are more likely to have the wherewithal to purchase a more customized solution matching their requirements more specifically while also being able to invest more in formally managing their internal customers. It may be that mid-market companies find themselves caught between having to buy the standardized solution while being less able to manage expectations, resulting in the lower satisfaction levels.

This situation does create challenges in the mid-market segment for both buyers and sellers. For buyers the challenge may be in managing their own organizations through the realities of an outsourcing transaction, while for providers it may be in better optimizing standard solutions, with perhaps broader configuration (as opposed to customization) options.

Also, current satisfaction levels notwithstanding, there continue to be issues in the buyer experience. The most common raised were:

- Concern about internal HR staff capability – generally manifesting itself in expressed concerns of the capability of internal HR staff to transition to new roles following outsourcing;
- Underestimating resources – buyers consistently “round down” the expectations of their internal organization when they launch an outsourcing initiative, which creates implementation issues during the transition/transformation stage; and
- Difficulty in building a business case – where buyers are not able to “afford” an outsourcing solution, frequently because the up-front investment required (which is largely a period expense), swamps the business case.

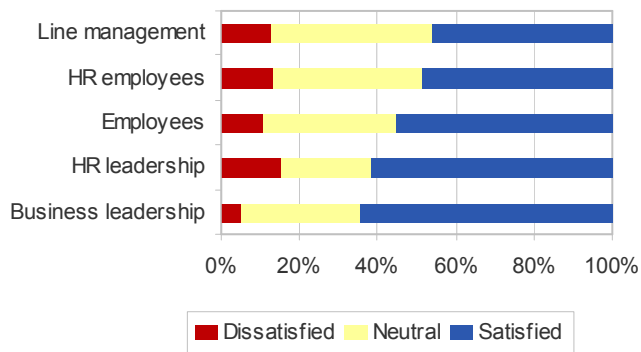
Repatriation of services (i.e. returning an outsourced function back into the buyer’s internal organization) is rare, reported in fewer than 10% of relationships. That being said, fewer than 60% of respondents were prepared to be references for their current providers and fully 23% considered repatriation or moving to another provider due to service issues. So while there are many success stories out there, it is not an unblemished record, and buyers need to ensure appropriate governance processes are in place to manage the downside risk.

As a final note on satisfaction, the highest levels of satisfaction tended to be with senior management and

## Detailed Research Findings

HR leadership. At the same time, while more than 60% of HR leadership is satisfied, it must be noted that fully 15% are dissatisfied. Service “consumer” levels ranked lower (Figure 11).

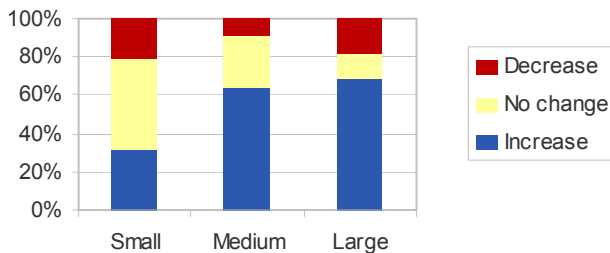
**FIGURE 11: Satisfaction with HRO Varies by Staff Type**



### Spending Levels

Despite current economic conditions, the general consensus was that spend levels would increase or not change in each market segment. This view tended to be more bullish the larger the organization (Figure 12).

**FIGURE 12: HRO Spending to Remain Healthy in Middle and Large Organizations**



## About the HROA Mid-Market Special Interest Group

The Mid-Market Special Interest Group is a global special interest group of the HROA geared toward anyone who is involved in HR outsourcing in the mid-market – defined as outsourcing three or more HR processes with an employee size generally ranging from 3,000 to 15,000. The group brings together consumers, providers and other mid-market stakeholders focusing solely on human resource outsourcing as a subcomponent of multi-tower business process outsourcing (BPO).

The HRO Mid-Market Special Interest Group's objective is to provide a platform for all HRO mid-market stakeholders to contribute research, data, and tools to make informed decisions related to the evaluation, purchase, implementation and management of HR process outsourcing. The group's purpose is to establish, evolve and continuously improve the industry standards and practices for middle market HRO.

Membership is open to any organization or individual who is a member of the HROA in good standing. The group's membership is broad, including buyers, advisors and providers.

For additional information about the Mid-Market Special Interest Group or to join, visit [www.hroa.org](http://www.hroa.org) or contact Adam Bleifeld at [info@hroa.org](mailto:info@hroa.org) or at +1 202 905 0351.

## HROA Mid-Market SIG Research & Standards Committee

Thank you to the following members of the HROA Mid-Market SIG Research and Standards Committee, who helped in the preparation of this report.



## About the HROA

The HROA is the definitive independent organization for all those who purchase, provide, or participate in HR transformation and outsourcing. Our membership encompasses over 7,500 HR executives, including the largest 50 buyers, the top 30 providers, the leading sourcing advisors and attorneys, and the best thought leaders in HR Transformation. The HROA brings its diverse membership together to set standards and practices, provide peer networking, and maintain a robust curriculum.

For additional information about the HROA or to join, visit [www.hroa.org](http://www.hroa.org) or contact Adam Bleifeld at [info@hroa.org](mailto:info@hroa.org) or at +1 202 905 0351.