

HR OUTSOURCING: A PERFORMANCE EVALUATION

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Sharon Taylor, Senior Vice President, Corporate Human Resources, Prudential Financial, and Chairwoman of the Human Resources Outsourcing Association, was the keynote speaker at the recent HRO World™ conferences in California and New York. In her presentation, Sharon shared her views on the promise and potential of HR outsourcing, and conducted a performance appraisal as only a seasoned HR professional can do. Sharon was kind enough to share her presentation with the HROA; the following article is her presentation, in her own words.

When I first heard about this topic – whether HR outsourcing has grown up and is living up to its promise and potential – I thought it was an intriguing angle. When we come together as an outsourcing stakeholder community, we usually cover tactical issues like establishing key performance measures and building successful partnerships. No question that these are important subjects; however, given our day-to-day pressures and accountabilities, it's less often that we have a chance to step back and assess, on a macro level, where we are and how we're doing with the overall outsourcing model. So I thought this was a perfect opportunity to do just that.

Performance and potential – these are certainly familiar terms to those of us in HR. In fact our whole talent management model is rooted in these concepts. We put talented people into positions based on their track record of past performance and their potential for growth. And we have some very structured tools to establish requirements and measure progress throughout the performance lifecycle including:

- The want ad
- The candidate resume
- The performance review
- 360-degree feedback
- The development plan

If we were to apply these tools to the Outsourcing Model, what would the outcome be? How would it rate compared to expectations? What would be the strengths and soft spots? And what would we advise as a strategy for further advancement?

A Bit of HR History

Before taking the Outsourcing Model through a performance assessment process, let's consider where HR organizations were at the point that multi-process outsourcing first came onto the scene in the late 1990s. This was a time when large companies were confronting the realities of the New Economy in a big way. HR was being asked to rise to two huge challenges:

1. To help their organizations stay competitive by becoming more agile and innovative
2. To cut expenses to help bring the corporate cost structure in line with leaner e-commerce firms.

A 1999 essay on the challenge of the New Economy by The Corporate Leadership Council put it this way:

HR is in a difficult situation. On the one hand, it must develop its capacity to take on a range of strategic activities in order to help the organization navigate the rougher seas of e-commerce. Those same pressures, however, are squeezing the resources available to HR to accomplish these critical tasks. The price of managing the migration poorly is likely to be steep.

HR organizations slow to cut out costs and streamline traditional services are likely to have their budgets cut for them by the CEO. Instead of managing strategic initiatives, they will be left managing a dwindling set of administrative and transactional functions, while the most interesting human capital management activities will be farmed out to other parties.

Without intervention, after a decade of ceaseless chipping away, HR will be left a smaller, less effective version of its current self.

WOW! In other words, HR functions faced extinction if we didn't change and change fast. As the CLC study underscores, our experience was the norm in many large companies. So clearly, 10 years ago HR realized that it needed help in a big way.

"Help Wanted"

We needed to become faster, leaner and more focused. To do that, we needed to find a way to get out from under the burdensome administrative load that took up a good deal of our time and energy. This, in turn, forced us to fundamentally rethink our service delivery model.

It was based on this need that large-scale, multi-process HR outsourcing emerged as a solution. Certainly at that point individual processes like payroll and benefits administration had been outsourced successfully for some time. But not unlike a high potential but junior person who comes forward and says, "I can do more," HR business process outsourcing (HR BPO) offered a thin but compelling resume that was an attractive fit with HR's need.

Outsourcing offered the promise of:

- Quickly and decisively solving for the issue of how to get out from under our administrative load
- Doing it in a way that would
 - Decrease costs
 - Maintain or improve the quality of our processes and
 - Free up HR to be a strategic partner to the business

Further, outsourcing offered access to some things in areas where HR did not have in-house depth.:

- IT capability that would allow companies to keep pace with the rapid evolution of HR technology
- Service delivery architecture that would enable us to leverage web-based self service as part of the solution to off loading administrative tasks
- Variable people resources that offered a solution to the quandary of how to size down the function while retaining access to expert skills and the additional manpower required for special projects and peak volume periods

It was an unproven concept but many of us were willing to take the calculated risk.

Now, as we approach the 10-year anniversary of that leap, what might the Outsourcing Model's performance review look like?

The HR Outsourcing Model Performance Review

I am going to put on my Organizational Development hat for a moment. A good performance review starts with clearly stated objectives – the things you agree at the outset will be achieved.

In the case of HR BPO, I am going to focus on three objectives that are fundamental to the model:

1. Reducing expenses
2. Improving processes
3. Fully realizing a strategic HR function

I'll review what HR Outsourcing set out to achieve in each area and what the major accomplishments have been. I'll also give my perspective on areas for continued improvement and share some 360-degree feedback, if you will, from various surveys and thought leaders. And I'll end with an overall rating and development plan for the industry.

Expense Reduction Competency

Fundamental to the outsourcing model is the idea that buyers were going to drive down their costs. The plan was that this was going to happen in several ways:

- Through a variable cost model
- Via guaranteed savings
- By reducing the capital outlay required for technology upgrades and maintenance

By most accounts outsourcing has performed well against this objective.

According to the Towers Perrin 2005 Study of HRO Effectiveness, fully 88 percent of companies reported some or complete success in cutting short-term costs, and 92 percent reported long-term savings. Reductions in process costs to deliver HR services were equally impressive.

Buyers have also been able to reduce the capital costs associated with the ownership and maintenance of complex software and technology, while vendors have been able to leverage efficiencies by spreading investments across multiple customers. And the very nature of the outsourced contract facilitates predictability of costs. You know your annual spend for in-scope functions and the pricing for add-ons associated with additional services. This has allowed buyers to better prioritize and budget for projects and process changes.

At Prudential, for example, since the commencement of our contract we've realized substantial savings. These are guaranteed savings and savings resulting from reduced volumes. We had a baseline headcount reduction of over 280 employees. All in, we have met our financial business case. We have also seen a change in behavior around the demand for HR services from internal corporate customers. People tend to get much more focused and disciplined around what they ask for when there is a price tag attached.

Of course, there is still opportunity within the model to drive down costs. For example, providers haven't cracked the code on how to leverage the full possibilities of economies of scale in a way that is attractive to buyers. Offshoring, where it makes sense, is another opportunity area.

I'll also temper my comments on costs by saying that from a provider perspective the results may be more mixed. Not all deals are moneymakers, and the economics of the model are still evolving.

However overall, the area of cost savings is a strong one for outsourcing. It has met and often exceeded expectations. I'd rate it a "4" out of "5" on our performance rating scale.

Process Improvement Competency

Of course cost is just one dimension. While studies show that it may have been a large driver in the initial adoption of outsourcing, quality of service is also a critical component of overall performance. For example, according to Hewitt Associates' 2006 Survey of U.S. Trends and Insights for Outsourcing, 58 percent of respondents ranked improved service quality in the top two drivers of the decision to outsource. The outsourcing model promised not only seamless continuity of service delivery, but also the opportunity for process improvements, with the web as a primary delivery channel.

On this dimension, which I would characterize as a shared responsibility between the client company and outsourcing provider, the evaluation is more mixed. Core employee processes like payroll administration and retirement have transitioned consistently well and demonstrated quality improvements post outsourcing. We know this because these processes have well established service level agreements and are generally measuring positively against them.

Core processes also adapt well to the self-service environment and outsourcing has been an enabler in this regard. I don't think that many organizations would have had the momentum to move to self-service as quickly as they did had they not shifted to the outsourced model. So that's an example of outsourcing as a catalyst for change.

In the area of governance, I think most early adopters would say that they have devoted considerably more resources to oversight than they anticipated. We quickly realized that we needed not only to track performance, but also to monitor the vendor's controls and compliance to our corporate and other regulatory policies. This was against the backdrop of dramatic changes in the regulatory environment over the last few years including Sarbanes Oxley, GLB and Privacy.

While this has been an admittedly bumpy area for many, outsourcing has pushed both buyers and vendors to accelerate the development of our risk programs and incorporate control consciousness into our operating models. All in all, I would put this in the win category.

Results have been mixed for the less transactional HR processes such as learning and staffing. One of the issues is that performance in these high touch services is not black and white like, for example, systems availability, where you either meet the standard or you don't. That's easy to monitor, report on and fix if there are problems.

Rather, there are nuances in the customer experience that make it much more difficult to measure and set standards because they are about quality rather than quantity. Outsourced recruiting, in particular, has been an area where performance has been problematic. For example, in the Towers Effectiveness Survey that I cited earlier, satisfaction for outsourced recruiting was just 69 percent compared with 90 percent satisfaction for the low touch process of DC retirement administration.

I think there are several reasons for this. One is that the labor market has changed dramatically in the past few years. Many of the early outsourcing deals were put in place in the early 2000s when hiring was flat. In the years since then many companies have moved into a growth mode, unemployment is at an all time low, and the demand for specialized skills is increasing. This is putting intense pressure on outsourced providers and has exposed vulnerabilities in their recruiting processes that may have been masked during the period of low activity.

A second issue is that, frankly, many companies are not very good at workforce planning. The challenge is that if you aren't providing good data on your expected staffing needs to your outsourced provider they can't adequately prepare to support those needs. Further, many of the early deals offered recruiting as a bundled offering – as if it is a single process. However the reality is that talent acquisition involves a whole series of linked activities, some quite complex and strategic and others highly administrative.

Part of the answer is to take a fresh look at the discreet processes that roll up to recruiting and figure out which aspects can be outsourced in a given arrangement in a cost effective and high quality way. That "sweet spot" is going to vary depending on the size, culture, core competencies and goals of each unique organization.

So broadly, the delivery of high touch services needs attention. Providers have to offer better solutions for the less standard and more judgment intensive processes that buyers are interested in. At the same time, buyers need to be realistic about the need for exceptions within these processes and build that realism into their expectations and measures. Until we improve performance in the area of high touch, I don't think most buyers will consider outsourcing additional, sensitive, judgment intensive functions like employee relations. Frankly, the jury is out on whether certain areas can ever be viable candidates for outsourcing, given how deeply they are baked into organizational culture.

There is also continued work to be done in the area of self service. Many employees and managers have not embraced the do-it-yourself mindset. This is partly because the self-service tools are often not that intuitive or easy to navigate. Again, issues are more likely to come up with more complex, infrequent functions like leave processing.

This confusion usually results in calls for help landing with the HR Generalists – the very people who were supposed to be relieved of the administrative burden. It's one of the things that hold HR Generalists back from spending time on more strategic work – the focus of our last objective, which I'll get to in a minute.

But first, let's give a rating to process improvement. On balance, considering the clear wins and the gaps, I would say that we met expectations but still have a number of things to work on to exceed them. So I would rate this area a solid "3" out of "5".

Strategic HR

One of the most alluring promises of HR Outsourcing was that it would be an enabler to HR becoming more strategic. The premise was that once HR handed over all of those transactional, high volume functions we would quickly turn our focus to value added, consultative services, which we would be well equipped to deliver. Our internal business clients would immediately recognize us as the strategic partner we were meant to be, and welcome us with open arms to the proverbial "table."

The reality has been much more complex than that. And while we have made some headway, there are still significant challenges to HR fully realizing the strategic role. Some of these challenges are tied to outsourcing and some are not.

One hurdle, which many of us didn't anticipate, was how much time and attention we would need to devote to designing the model for the retained HR function in the period immediately after outsourcing. I've already talked about challenges in setting the structure for governance and vendor management. Beyond that, companies have also had to define the optimal set-up for the rest of the retained HR organization in the post-outsourcing world. Specifically:

- What roles remain in corporate center HR?
- What is the core work of HR Generalists?
- What are the reporting relationships?
- What are the appropriate job descriptions, levels, and headcounts for each?

It's been a long haul with some missteps, but I think that most early adopters have finally landed on a retained HR structure that sets the stage for their organizations to be strategic.

We also had to rethink the skills and competencies needed by HR professionals to take on the strategic role. Financial acumen, operational understanding, analytical and consulting skills have become much more critical in a post-outsourced HR function. Those skills weren't part of the traditional profile for HR and, frankly, many otherwise talented people didn't survive the transition. But among those who did, as well as those new to HR since outsourcing, there is an increased level of business literacy. Again, this is a positive step toward HR being equipped to be a strategic partner.

Providers, too, have become more realistic in how they are positioning outsourcing. There is less hype around transformation and more emphasis on what they can reasonably deliver in terms of cost and quality. That's largely because both buyers and providers now recognize that outsourcing is not the silver bullet we had hoped for in unleashing HR to be strategic.

Transition has been particularly challenging for HR Generalists – the people who sit in the business and advise on people issues. In fact, according to the Towers Effectiveness Survey, 23 percent of organizations report little or no success in reshaping the generalist role post outsourcing. Part of the problem is that HR is reluctant to move outside its comfort zone. Administration, processing, putting out fires are what many of our clients have come to expect and value from us. Another issue is basic skills. Fully 62 percent of respondents to that same Towers survey felt that their retained HR Generalists had competency gaps in key areas like project management, strategic thinking and change management.

So we need to get serious about defining what we expect from the generalist role. And we need to more aggressively address generalists' skill gaps through training and redeployment.

More broadly, the HR function needs to do a better job defining what it really means to be strategic within our organizations – to stop throwing around a vague cliché. We need to be clear about where we fit in to the overall structure of our companies and how we add value. In effect, we need to rewrite our mission and vision statements.

Providers also have work to do in fully supporting strategic HR. Delivering consistently superior service with no distracting surprises is a part of the equation. Beyond that, the wealth of information collected as part of the administrative process has tremendous untapped potential. It would be wonderful to mine that data for trends and patterns of behavior that could inform our strategic thinking. Few of us are doing that.

And so, on balance, while there is some progress, I have to conclude that the goal of Strategic HR has only partially been achieved since outsourcing. I would rate it a "2" out of "5".

360-Degree Feedback

I've given you some of my impressions, but what do the other experts say about the outcomes of outsourcing? Let's take a moment and look at what some of the major surveys and thought leaders have to say.

When you look at the major surveys on outsourcing, you see a pattern of general satisfaction:

- PricewaterhouseCoopers' 2005 "Trendsetter Barometer" indicates that 81 percent of CEOs involved in HR Outsourcing say their experience has met or exceeded expectations
- In Hewitt's 2006 survey of HR Outsourcing Trends & Insights, 65 percent of HR Executives are satisfied or very satisfied with their current HR outsourcing arrangement
- Towers Perrin's 2005 Survey of HRO Effectiveness shows a similar result – 64 percent of companies with "mature" HR outsourcing deals somewhat or very satisfied.

Drilling deeper, the HR BPO Buyers Advisory Board looked at satisfaction levels by process in a 2006 survey and concluded that self-service, DB retirement and Stock Option Administration were the most favorably rated, while services like staffing, learning administration and HRIS were the lowest.

Thought leaders also offer qualified optimism: According to University of Southern California professor Ed Lawlor:

"Maybe our expectations weren't all met, maybe the cost savings weren't as great as we hoped, but there is no evidence that the concept is wrong or that the HR administration outsourcing industry isn't going to continue to grow at 25 percent a year."

I tend to agree. When we consider the benefits and challenges associated with HR outsourcing, and when we look back with reasonable expectations I would say that the model has met, but is not yet exceeding expectations. I would rate it a solid "3" out of "5".

Development Plan

So what's the development plan? How do we move this model to exceed expectations and unleash its full potential? Here are my thoughts, many of which we have already touched on:

- We need to either raise the service and satisfaction levels for high-touch services or revise our expectations about what is a suitable candidate for outsourcing.
- In line with that goal we need to find the "sweet spot" for outsourced recruiting, recognizing that the ideal is likely going to fall along a continuum that will vary from company to company.
- We need to fully leverage the possibilities of self service by making it more intuitive and user friendly. At the same time we need to push back on the pockets of resistance to self service within the corporate culture and stop enabling behaviors within HR.
- We need to develop more universal performance standards and benchmarks so that we are comparing apples to apples across industries.
- We need to figure out how to incorporate new, innovative process improvements without destabilizing services or unfairly penalizing vendors.



- We need to equip those in HR, particularly HR Generalists, with the proper tools and training to be truly strategic (and we need to make the tough decisions on those who are not suited to the role), and
- Finally, we need to share our best practices and lessons learned so that we can duplicate successes and avoid pitfalls as the industry matures.

If we can fully leverage that potential, and drive strong performance, I believe HR outsourcing has a bright future ahead.