

## Payroll: it's a challenge, in or out

**Once a core function of the human resources department, these days payroll is just as likely to be handled by the finance team – or by a completely separate external organisation. Is it possible to balance the desire for outsourcing payroll with the push towards creating an integrated view of all HR functions? And how can HR work with finance and IT departments to ensure maximum efficiency in payroll? Angus Kidman investigates in the first of our special two-part series on payroll**

For employees, a successful payroll system is one of the most visible measures of a successful HR technology strategy. Staff may be willing to forgive the occasional dodgy manager or delayed group certificate, but if their money doesn't go into the bank account accurately and on-time, they'll quickly express their displeasure.

For the typical HR manager, however, payroll often falls into the category of a necessary evil. While it's essential that it's done and done well, it's much harder to add real strategic value to the business simply through upgrading the payroll systems.

That explains why many organisations have increasingly looked to outsourcing as a means of providing their payroll function. The age of many payroll systems is also another factor; faced with purchasing a whole new package, moving the problem to an outsourcer can often be a viable solution.

Outsourced or otherwise, payroll software remains big business. IDC estimates that the global market for HR management and payroll processing software will grow at 5.6 per cent each year through to 2007. That will see a rise in overall market value from \$US4.3(\$5.5) billion in 2002 to \$US5.7 (\$7.2) billion in 2007.

Part of that opportunity arises because many smaller businesses haven't automated their payroll at all. A survey of 500 businesses conducted by AMR Interactive for MYOB last year found that amongst businesses with four or less employees, 47 per cent had a paper-based payroll process. While that's not altogether surprising, what is more striking is that 37 per cent of businesses with five to 19 employees continue to work with a paper system, despite the obvious benefits of moving to an electronic environment.

For these businesses, simply introducing an electronic payroll process can create huge benefits. For better-established companies with larger workforces, however, creating a business case that purely addresses payroll can be more difficult.

### **The NSW Teachers Credit Union**

Changes to payroll software can thus often come about as a result of broader strategic plans within an organisation. In the case of the NSW Teachers Credit Union, a recent upgrade to its payroll distribution system was part of a broader shift to develop a company-wide intranet-based knowledge management strategy.

The credit union, which has 250 employees spread over two locations, has been using MicrOpay to manage its payroll since 1987. In December last year, it rolled out MicrOpay's ConnX employee self-service (ESS) module, but the path to that changeover had actually begun much earlier.

Human resources manager Helen O'Reilly had first begun considering adding ESS to the payroll system five years ago, but held off because of technology issues. "MicrOpay didn't have an employee self-service module at that time, and to move to another system was going to cost an enormous amount of money," she says.

One year ago, O'Reilly learnt of the planned release of the ConnX module. By that time, the credit union had begun planning to roll out an intranet as the centre of a knowledge management strategy. "We wanted to create a knowledge culture at the credit union," says O'Reilly, noting that more than 60 per cent of current staff have been with the organisation for 10 years or more and thus had a wealth of valuable business knowledge that hasn't been captured. "We felt that an intranet would allow us to share as much information as possible with staff."

ConnX's arrival was timely given the overall plan. "It's basic, but it was going to meet our requirements, which was to minimise paper distribution," O'Reilly says. "When we looked at paper distribution, a lot of it was linked to payroll and leave applications."

As well as simplifying the distribution of pay advice and the processing of leave applications, adding payroll to the intranet served a broader goal. "It was probably used as a carrot for people to use the intranet. We needed to have something on there that would encourage people to go there." In turn, the plan to roll out an intranet made it easier to justify the cost of the new ConnX module.

O'Reilly served on the intranet planning committee along with the general manager for finance and administration, who is also in charge of IT implementations. This ensured that the project met the goals required by all three functions.

After a trial period where both paper and electronic pay advices were distributed, the credit union has now moved to a completely electronic system. O'Reilly is very pleased with the results. "Acceptance from the staff has been

overwhelming. People think it's fantastic. It has been a very successful project."

One factor where the credit union was lucky was in being able to co-ordinate the approach of the finance, IT and HR teams. While this was simplified by the fact that these functions only encompassed two line managers, the same strategy has generally proven successful in much larger organisations. However, integrating the payroll components with other applications can remain a difficult task.

### **The problems with payroll**

Richard Downing of Star Accounting Services traces current problems in this area back to the mid-1990s trend to add overseas-developed payroll modules into broader HR management systems.

"At the time, we were happy on the surface to integrate payroll in," he says. "But in the later 1990s, we saw a huge frustration as people realised the cost of integration."

Despite that, integration remains desirable. "There's been a trend towards total HRM, and you can't do that with outsourcing," says Downing, who worked with local accounting software provider Greentree when their software was moved onto a full Windows base in the late 1990s.

Of course, if your payroll system has been outsourced, achieving any kind of integration can be trickier still, despite the fact that the notion of farming out payroll is not itself a new one. As Downing notes: "Payroll is one of the few bureau computing functions that has remained on the market," notes Downing, outlasting similar implementations in other areas that date back to the 1970s.

So why has outsourcing remained popular? "Payroll is hard, so outsourced payroll happened for two reasons: confidentiality and staffing," says Downing. While confidentiality can be overstated – even if you farm everything out, someone will still have to transmit details of pay and position changes – the desire to add to a low headcount can be a good argument.

"Even in a sizeable organisation, there's often not many pay officers," says Downing.

Budgeting is always an important consideration. "Outsourced payroll does get expensive, because it is usually charged per pay packet," Downing points out, while software normally but not always has an upfront cost. If contract-based calculations are involved, the problem can be even more pronounced (see sidebox 'The contract challenge'). These are the kind of discussion points which need to be considered by a CFO and CIO as well as the HR team.

Ideally, it should be possible to balance the desire to shift a non-competitive function (payroll) with the differing needs of those three departments. "Today's market conditions, characterised by volatility and uncertainty, are driving many companies to seek ways to reduce costs as well as to adapt to the evolving marketplace," says Cap Gemini Ernst & Young business process service analyst Bill Frech.

Teamwork thus becomes an essential component. "The capacity to anticipate, accommodate and address change as a team is a critical component of successful outsourcing engagements," states Frech. "Flexibility is simply a requirement, not only in the contract, but in how both teams communicate, solve problems, and achieve strategic goals."

### **The contract challenge**

Managing payroll can be even more challenging if you have to deal with contract employees rather than permanent staff. "Companies of all sizes have historically struggled to effectively administer the full contract worker employment cycle, from engagement to daily management to termination," Gartner research director Jim Holincheck noted last year.

Greentree's Downing points to the example of Whitney Marine Industries, one of Australia's most prominent boat builders. Whitney originally had its payroll outsourced, but used an in-house accounting system for other functions.

While this eliminated the need for dedicated payroll staff, it didn't fundamentally match with the cost accounting needed in the boat-building industry, which is project based. Keeping track of staffing costs was essential: "A large part of the costs of their production were labour," Downing says.

Up to 10 new jobs needed to be entered into the system each week, and pay data had to be costed back against jobs in the accounting system. At the same time, that pay data also had to be entered separately by the outsourcer. "The bureaus force double-handling of the labour inputs," says Downing.

In Whitney's case, the best solution proved to be shifting back to an integrated package (Greentree) which eliminated the need for double-handling. Most businesses will face challenges of this type, and they need to be carefully considered when planning any outsourcing arrangement.