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HRO Europe: July 2007



## Building on HRO's Cornerstone

*Payroll is the most established domain of HRO, yet only a minority of organizations in Europe outsource it. With compliance pressures mounting and globalization speeding up, is it time to rethink an external solution?*

By Andy Teng

Of all the services that HR undertakes, none is more important than payroll—or as mundane. Employees expect paychecks to be correct each and every time, business leaders only pay attention when there is a problem and complaints are voiced, and investments in upgrading payroll technology are hardly a priority at most organizations. Nevertheless, payroll is a critical responsibility for both HR and finance.

So even as other components of HRO have evolved tremendously during recent years—areas such as recruitment process outsourcing, learning and training, and HRIS have changed markedly since the beginning of the new century—minimal change is occurring today in the outsourced payroll administration market. In fact, many organizations fall into one of two camps: those who will always process payroll internally and those who have embraced some kind of outsourced solution. To say which group has been more successful in maintaining payroll is akin to judging a beauty contest—it's all in the eye of the beholder.

Whether an outsourced payroll solution makes sense depends on a number of factors, such as the global footprint of the employer, the size of the workforce, the complexity of the industry, and a host of other considerations. One thing is clear, however: Payroll has become the cornerstone of multi-domain HRO deals, and employers that outsource payroll now do so in a more integrated fashion than ever before, as they build services around the basic building block of payroll. Their desire to have access to employee data throughout the enterprise is being met by outsourced solutions that enable them to get that information from anywhere around the world. As a result, outsourced payroll solutions are making organizations more transparent than before, providing managers a clearer view of business outcomes.

But even as outsourced solutions offer more advantages to internal services, don't expect the market to suddenly swarm to them. In Europe, outsourced payroll still accounts for a minority of the overall market. According to ADP, the global payroll leader, the percentage of companies outsourcing payroll is well below 50 percent in most European countries, with nations such as the Netherlands and the U.K. leading the charge. Overall, the market penetration rate is between 35 and 40 percent, according to ADP.

Payroll outsourcing is growing slowly throughout Europe, with some markets more accepting of outsourcing than others. In the Dutch market, for instance, ADP estimates that more than 50 percent of mid-sized and large employers outsourced payroll, but it is an anomaly in an otherwise outsourcing-shy EU. The U.K. has aggressively embraced outsourcing, but there is less enthusiasm in countries such as Germany, France, and Belgium. Although predictions are that outsourced payroll will continue to gain market share, it will do so at a snail's pace.

Industrialized, western European nations are likely to see the slowest growth, while emerging markets in Eastern Europe, as well as Russia, have the potential for greater outsourced payroll adoption. In any case, demand for end-to-end HRO contracts including payroll is likely to rise at a faster rate than standalone payroll contracts.

### Integration is Key

"Growth is continuous, but it's slight year after year. There is no big bang," said Marc Bruzzo, senior vice president of sales and marketing with ADP ES Europe. "What is new is what we are doing with GlobalView and what our competitors are doing with their global offerings. Now companies are saying they can buy payroll worldwide. Ten years ago, that was not available."

ADP, whose GlobalView platform allows clients to apply common payroll and HR policies worldwide, view consolidated reports, and leverage local expertise at ADP service centers, developed the solution in response to the changing market. Bruzzo explained that this trend is driven by the larger globalization push. As organizations expand their international presence, they want to better manage their operations on a regional as well as global basis. He explained that within Europe, for example, a French employee might not remain in France throughout his or her career with a particular employer; that worker could be transferred around the EU, and HR wants to have access to the data wherever he or she is. Not only would an outsourced solution with global capabilities offer transparency, but also cost efficiencies can be gained.

Until recently, administering pan-European payroll from a centralized location was still seen as the holy grail of outsourcing pursuits—desirable but highly difficult to achieve. However, providers have rapidly enhanced their capabilities to give buyers more tools to reach this goal, including technology such as employee and manager self-service. By helping employers address their payroll issues in a host of countries, payroll service providers are sweetening their value proposition while growing their revenue base. It's also an imperative to staying competitive in the marketplace.



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"It's the cross-border integration that becomes an advantage," said Paul Knowles, the engagement director in Europe for sourcing advisor Everest Group. Knowles noted that unlike the U.S., the European payroll market is driven by a different set of forces. He cited compliance as the No. 1 reason for companies choosing to outsource a pan-European deal. Considerations such as lack of commonality in data, complexity in the legislative environment, and workforce mobility all complicate payroll administration. These concerns are especially relevant for U.S.-based public companies expanding into the European market. With Sarbanes-Oxley regulations still fresh in the minds of C-suite leaders, ensuring payroll accuracy is high on the list of corporate mandates.

He added that while other drivers affecting the HRO movement are also important, some have become de rigueur in doing business. For instance, payroll processing costs have come down so much that it's become a commodity service in markets such as the U.K. For a provider to compete in this sector, it must have a highly efficient payroll engine. Quality of service is another must-have, as companies that typically transition from an internal service model to an outsourced one will expect outstanding service. The HR and/or finance leader championing outsourcing will certainly not want to jeopardize his or her career on poor payroll service delivery.

"In HR, there is an amount of money to be saved by focusing on cost reduction here, but the missed-opportunity costs if anything goes wrong...could cost much more than could ever be saved," said Marcel de Brauwier, director of HRO for Netherlands-based Randstad, a European payroll provider that recently won the largest payroll contract ever in that country with a deal with Philips Netherlands for €80 million.

He contended that while cost savings have been the initial driver behind many HRO deals, buyers today are less concerned with costs for several reasons. For one, when organizations first considered savings as a reason to outsource, they were lured by promises of savings of 30 percent. Now that many organizations have undergone internal transformation efforts, the opportunity to trim fat is lessened. In the Philips deal, he added, the buyer was more concerned with maintaining quality of payroll services than with cost savings. He explained that because it had undergone a number of spin-offs, Philips executives grew concerned that with fewer internal resources, it would not be able to continue to deliver the same high-quality service to its employees. Outsourcing was viewed as the solution.

#### **Expanding functionality**

If quality of payroll service is at the forefront of European buyers' priorities, then improving functionality may run a close second. That's because some companies have realized that outsourcing gives them access to best practices and new technology. For instance, European organizations continue to gingerly roll out employee and manager self-service, hesitant to make sudden changes in payroll practices. Although they realize that self-service can eventually help reduce costs, improve accuracy, and expand functionality, many are cautiously weighing self-service in their own organizations, even in markets where outsourcing is flourishing.

"Self-service is not yet significant in Europe; it's the same as in the U.S. It's being rolled out slowly. This is partly price-related, but also for payroll, there is a limited amount of self-service that users can carry out other than bank details, address, and downloading pay slips," said Martin Stockton, vice president for global business development at payroll provider Patersons.

Nevertheless, payroll providers are making self-service available so clients can adopt it when they eventually grow comfortable with it. Take the instance of Northgate, which recently acquired Brussels-based ARINSO. The global HRO provider, which is also one of the biggest payroll providers in Europe, is putting a lot of effort into making its self-service offering as user-friendly as possible, said Kobe Verdonck, Northgate's regional executive director for EMEA, Latin America, and Canada. In fact, he pointed out, Northgate has an entire development team working on improving the self-service experience for customers.

"Outsourcing is not only about quality and getting rid of non-core business and making sure you are compliant—it's about saving money, of course. Self-service is one of the drivers behind this," he said.

Verdonck said self-service functionality would be one of the cornerstones of the company's EuHReka 2.0 platform, a pre-configured SAP HR system soon to be available in 40 countries. His views mirror those of other HR leaders in the industry—that self-service can be one of the key tools for gaining great efficiencies, cost savings, and a better customer experience. After all, employee information is the foundation for all HR data, and what better way to reduce administrative overhead and improve accuracy than to directly charge the managers and employees with maintaining their own records.

What remains uncertain, however, is how quickly organizations adopt self-service. While Northgate's clients might be migrating to self-service, many other payroll service providers report that rollout has been minimal in the marketplace. Even in the U.S., the track record has been spotty.

By beginning with payroll, European organizations are finding that HRO can be rolled out in stages and doesn't need to occur in one fell swoop. Making sure that outsourced payroll works well in their organizations, new adopters are laying the groundwork for outsourcing additional services in areas such as recruitment and learning and training. That's why getting payroll right is often a critical precursor to end-to-end HRO engagement. For many growing companies, outsourcing payroll is also an efficient way for them to ensure compliance without all the internal investments. And in an era of rapid globalization, overcoming market hurdles is key to keeping up with the market shifts.

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