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Outsourcing Payroll

Panacea or Pay-Per-View?

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Aided by the success of Timothy Ferriss's book, [The 4-Hour Workweek](#), and fueled by limited internal resources and an abundance of service providers, we have become a nation of outsourcers. It's not hard to understand the attraction. Who wouldn't love to hand off their least favorite chore to someone else? But when it comes to payroll, we might be kidding ourselves about both the benefits and the true costs of outsourcing. (Draw your own conclusions about that 4-hour workweek.)

The promise of payroll outsourcing is that the payroll service provider will assume all of the hassle of paying employees, leaving employers free to pursue more value-added activities. This arrangement sounds like a no-brainer. In cases where the burden comes from the sheer number of payroll checks or the number of taxing authorities expecting payment, an employer might actually succeed in shifting a portion of their pain to a service provider. But in many other cases, companies who outsource end up trading one set of burdens and irritations for another. These employers encounter inflexible reporting, limited options and hidden charges, and don't succeed in substantially reducing the demands on their staff. And what's worse for today's businesses, they end up having limited insight into their labor costs – which are an increasingly important driver of overall profitability.

Contracting with a payroll service provider is like subscribing to cable. As employers, we're no different from the excited boxing fan who signs up for the premium sporting channel with its 24/7 access to all the best events. Imagine our surprise, on the evening of the big bout, when we discover that the big event is "pay-per-view" requiring payment of an additional charge on top of the monthly fee. There's a reason no one loves their cable company but you needn't let your payroll service provider hit you with a left hook in the form of unexpected charges.

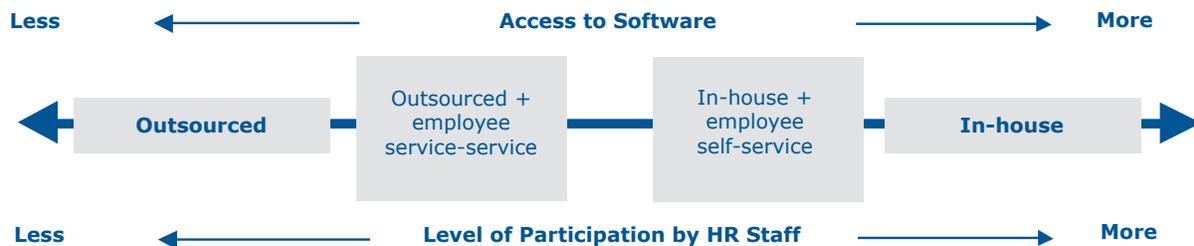
Outsourcing can be a good solution, but the decision to outsource is hardly cut and dried. Before you decide on a payroll management solution for your company, it's important to take a moment to learn about your choices and the advantages and disadvantages of each option. In this whitepaper, we'll compare in-house payroll solutions with outsourced solutions to help you make an informed decision.

Two Ends of the Spectrum...and Lots In Between

There are two main ways to address your payroll needs: manage the process yourself or outsource payroll management to a service provider. These options are at opposite ends of the payroll management spectrum. At one end, there is potentially lower staff and technology involvement, while at the opposite end there is both more staff time and more direct software use. The ideal solution usually lies somewhere in between.

With a completely outsourced solution, you might capture all payroll information on printed forms and transmit it to your payroll provider via fax. Your company would have no direct access to the underlying application or calculations and would receive finished paychecks. The outsourced provider would manage data entry, calculations, payroll check processing and all other steps.

With a traditional in-house payroll management solution, on the other hand, you might have a desktop system that is accessed by members of your payroll department. You would capture all employee information on paper forms before entering them in your system. Your in-house payroll team would manage the entire process, from data entry and calculations to funding and remittance.



Most payroll management solutions fall somewhere in the middle of this continuum. The range of solutions has expanded thanks to greater sophistication, and a new feature called “employee self-service.” This feature gives employees direct access to a subset of their data – generally contact information, beneficiary designations, and other basic information. As changes are needed, rather than filling out a form that goes to HR, employees can directly access the system to update their own information. Regardless of the solution, this feature saves everyone time and effort by putting appropriate tasks in the hands of employees.

| Payroll Management Solutions | |
|--|---|
| Responsibility | Type of solution |
| HR/PR Staff | In-house desktop software. |
| HR/PR staff and employee | In-house desktop software with employee self-service access. |
| HR/PR Staff and employee | Hosted dedicated application accessed via the Internet. |
| HR/PR Staff, outsourced provider, employee | Outsourced payroll service with access to data entry screens via Internet, employee self-service. |
| HR/PR Staff and outsourced provider | Outsourced payroll (information processed via a “black box”) data is submitted and completed items are returned to the company. The application in the middle is invisible to the employer. |

The (real) Cost of Doing Payroll

Now that we've reviewed the various payroll management solutions, let's review each step of the payroll cycle to identify the challenges, how they're addressed by in-house and outsourced solutions, and the "pay-per-view" costs that could be incurred.

Hiring

The payroll cycle begins when a new employee comes on board. Once the offer letter is signed and the employee is hired, there are a myriad of forms to fill out, elections to make, and data to enter. The hassles of adding an employee to a system are generally shared by the new employee and the Human Resource (HR) staff. On the first day on the job, the employee must fill out forms indicating his preferences regarding both taxation and benefits. The HR person must set up a new record, review documentation, get approvals, and complete more forms. Finally, all of this information has to get into the payroll system. Whether that system resides inside the company or with a service provider, the same amount of employee effort is required.

Fortunately, both outsourced and in-house solutions can be set up to allow an employee to enter much of his contact information via self-service access, so whether the system is online or on-premise, handled in-house or by an outsourced service provider, the time needed to enter basic employee information is roughly the same.

| Step | Activity | Worker | |
|-----------------|-----------------------------------|---------------------|-------------------|
| | | Outsourced Solution | In-house Solution |
| HIRING | | | |
| Add an employee | Gather forms | HR/PR | HR/PR |
| | Make copies of required documents | HR/PR | HR/PR |
| | Record salary | HR/PR | HR/PR |
| | Specify payment method | HR/PR | HR/PR |
| | Record allowances | Self-Service | Self-Service |
| | Record benefit elections | Self-Service | Self-Service |
| | Record marital status | Self-Service | Self-Service |

New employee hires involve a significant amount of paperwork and processing time for an HR staff person. Regardless of the system used, it takes time to get information from the new employee to that system. While the effort is equal, you can expect to pay additional charges if you opt for an outsourced service provider

Potential "pay-per-view" charges

- Per employee set-up fees which can often vary based on withholding and benefits required

Paying

Capturing, recording and reviewing time for hourly employees can be a lengthy, error-filled process. Fortunately, there are a number of automated time keeping and time card systems that can be integrated with either on-premise or outsourced payroll applications. The more complex your work environment and the more detailed your tracking requirements, the greater the need to integrate your time keeping and payroll systems. With proper integration tools, both outsourced and on-premise applications can help reduce the burden of getting your hourly employees paid correctly.

Paying salaried employees is usually less time consuming than paying hourly workers. Salaried employees generally have fewer changes to their pay, although they make more frequent changes to their withholding and benefit elections. Salaried payroll should be exception based so that entries are only required for paid time off, special situations or commission/expense reimbursements. In addition, most comprehensive payroll solutions allow you to enter changes that don't take effect until some future date. Look for an effective date feature in any solution you are considering, whether in-house or outsourced.

When it comes to piece-rate workers, you will need to capture and record per piece data and enter it in your payroll system. You might pull the data via an automated feed or re-key it in your payroll system. Either way, you need to know if your payroll system is equipped to manage this form of payment, and if so, what additional charges are involved for integration.

| Step | Activity | Worker | |
|--|---------------------------------|---------------------|-------------------|
| | | Outsourced Solution | In-house Solution |
| PAYING | | | |
| Pay an hourly employee | Record hours | HR/PR | HR/PR |
| | Calculate payroll | Provider | HR/PR |
| | Print paycheck | Provider | HR/PR |
| Pay a salaried employee | Enter exceptions to regular pay | HR/PR | HR/PR |
| | Calculate payroll | Provider | HR/PR |
| | Print paycheck | Provider | HR/PR |
| Pay by the piece or other unique methods | Capture and record data | HR/PR | HR/PR |

Regardless of payment method, payroll processing requires the time and attention of an HR or Payroll employee. While minor adjustments to benefits or elections can be entered by an employee via a self-service solution, changes to hours worked, rates and salaries, or piece rates have to be managed by authorized staff members. Once captured, the changes must then be communicated to the payroll system. Only then is the payroll solution or service provider able to process payroll, generate checks, and capture transaction details.

Both outsourced and in-house solutions require equal amounts of time and effort to ensure that employees are paid the correct wages each pay period.

Potential "pay-per-view" charges

- Fees for non-standard payment methods (like piece rates)
- Integration fees
- Individual employee information change fees such as number of exemptions, marital status or changes in benefit plans

Funding

When it comes to funding payroll, no solution will remove the biggest hassle — coming up with the money. But beyond that, both in-house and outsourced solutions can help you determine how much to fund and reduce the burden of getting the correct amounts to the proper authorities. The more options you offer for employee benefits, garnishments, bank account types and the like, the more complex the funding process will be. When you use an outsourced payroll provider, however, these additional options can result in additional charges.

| Step | Activity | Worker | |
|------------------|---|---------------------|-------------------|
| | | Outsourced Solution | In-house Solution |
| FUNDING | | | |
| Fund the payroll | Transfer funds to cover payroll (done a few days earlier when outsourced) | HR/PR | HR/PR |

The type of payroll option you choose will have a direct impact on your cash flow. For most outsourced solutions, you are required to calculate and fund the full gross payroll in advance of the pay date. For in-house solutions, you can generally transfer funds for the net pay amount on the pay date and then make additional transfers to cover tax and benefit payments when due.

Outsourced solutions generally involve a single funds transfer, while in-house solutions support multiple transfers of funds, but only when payments are due.

Potential "pay-per-view" charges

- Fees for multiple banks
- Fees for direct deposits to non-checking bank accounts or multiple bank accounts for a single employee
- Time value of money

Remitting

After the employees are paid, it is time to get any withheld amounts to the proper authorities. Outsourced service providers will normally manage remittances to federal and state (or provincial) authorities. But they may not automatically make payments to your benefit providers, credit unions, or specific vendors (e.g. auto loan companies). Many in-house solutions will automatically create payroll-related remittances for use in making payments from your accounts payable system. You will then need to produce checks and mail the payments or send payments via your online banking system.

| Step | Activity | Worker | |
|-----------------------------|---|----------------------|-------------------|
| | | Outsourced Solution | In-house Solution |
| REMITTING | | | |
| Remit withholding and taxes | Make tax deposits Make other benefit payments to providers | Provider Provider | HR/PR HR/PR |

Both in-house and outsourced payroll solutions can help you capture amounts withheld and payable. Depending on the way you structure your arrangement with an outsourced payroll provider, they can also manage your remittance directly, thus reducing the effort needed to generate checks. In-house solutions generally require additional steps to print checks and then mail them to the appropriate payee.

Potential "pay-per-view" charges

- Fees by the payee
- Limitations on number of providers
- Extra charges for remittances to local banks or credit unions

Filing

Compared to figuring out how much to pay and getting remittances to the right place, tax returns are a cinch. By the time the returns are due, all of the supporting information has been accumulated in your application of choice. The service provider or in-house team member runs a report or prints a form and then sends it to the appropriate authority.

| Step | Activity | Worker | |
|---------------|---|---------------------|-------------------|
| | | Outsourced Solution | In-house Solution |
| FILING | | | |
| File returns | Prepare and remit quarterly returns and amounts due | Provider | HR/PR |

Other than keeping track of due dates, which becomes the responsibility of the provider in an outsourced solution, there is little difference between the amount of work required under either method.

Potential "pay-per-view" charges

- Additional number of states or local tax authorities
- Amended return charges

Recording

Labor charges typically represent a large chunk of operating costs. The next step is to get those costs from your payroll system into your general ledger so they can be properly reflected on your financial statements.

Most outsourced payroll solutions offer limited integration capabilities via a file transfer. In other cases, they provide you with a printed list of transactions by GL account number. Your team must then make manual journal entries to update your system. There are normally limits on the level of detail provided and on the number of departments that are supported.

Using an in-house system, transactions automatically flow to your general ledger. You have control over the level of detail to record and have the option to create as many categories of costs as you need. You also have the benefit of timely updates and integration with a job costing system, if needed.

| Step | Activity | Worker | |
|----------------------------|--|---------------------|-------------------|
| | | Outsourced Solution | In-house Solution |
| RECORDING | | | |
| Record payroll tax entries | Post activity to General Ledger Distribute cost details to projects or jobs | HR/PR HR/PR | HR/PR HR/PR |

An in-house payroll solution will simplify the process of getting transactions from payroll to your general ledger

Potential "pay-per-view" charges

- Integration development
- Additional departments
- Changes to categories or level of detail

Analyzing

When you come right down to it, after getting your employees paid, the main purpose of any payroll system is to capture information that helps you manage your business. You might need to analyze your labor costs by product, department, or location. You might want to compare costs by week or charges by employee. You could be watching your benefit costs or staying on top of worker's compensation insurance. Whatever your issue of the day, week, or month, having full access to your payroll details via an in-house solution can make the difference between being in control of your labor costs and having a bottom line that is out of control. While available with an outsourced service provider, additional information typically involves additional charges and more hassle.

| Step | Activity | Worker | |
|------------------|---------------------|---------------------|-------------------|
| | | Outsourced Solution | In-house Solution |
| ANALYZING | | | |
| Reporting | Analyze labor costs | HR/PR | HR/PR |

An in-house payroll solution can help eliminate the hassle of managing your labor costs.

Potential "pay-per-view" charges

- Frequency of reports
- Report customization costs
- Detail versus summary reporting
- Ad hoc additional individual employee requested reports

Before You Decide...

Outsourcing certainly has its benefits, but before you decide to hand off your payroll hassles to an outsourced solution provider, stop and consider not only your company needs, but also the potential pay-per-view costs you might encounter along the way. Which steps in the payroll process cause you the most pain? Are you willing to pay for the convenience of outsourcing them? Will outsourcing truly shift the burden? And are you ready to hand over some (or all) of the control of your valuable information? Can you live with level of detail provided by a service provider or do you need more insight into your labor costs? Use Appendix A to help determine whether an outsourced solution is best for your company.

Appendix A

The true cost of payroll outsourcing.

Use this worksheet to calculate the true cost of an outsourced payroll solution.

| Item | Quantity | Qty cap for quoted price | Estimated Cost from Outsourced Provider | Total Cost |
|---|----------|--------------------------|--|------------|
| Countries in which reporting | | | \$ _____ per _____ | |
| Avg number of new hires per year | | | \$ _____ per _____ | |
| Avg number of terminations per year | | | \$ _____ per _____ | |
| Employees | | | \$ _____ per _____ | |
| Hourly/Salaried | | | \$ _____ per _____ | |
| Type of pay | | | \$ _____ per _____ | |
| Frequency of pay | | | | |
| <input type="checkbox"/> Hourly | | | \$ _____ per _____ | |
| <input type="checkbox"/> Salaried | | | \$ _____ per _____ | |
| <input type="checkbox"/> Piece rate wages? | | | \$ _____ per _____ | |
| Benefits- number of options/ plans provided | | | \$ _____ per _____ | |
| Garnishments? List number of creditors | | | \$ _____ per _____ | |
| Other special withholding | | | \$ _____ per _____ | |
| Payment methods <input type="checkbox"/> Direct deposit to checking only <input type="checkbox"/> Direct deposit to multiple accounts <input type="checkbox"/> Paper checks <input type="checkbox"/> Other | | | \$ _____ per _____ \$ _____ per _____ \$ _____ per _____ \$ _____ per _____ | |
| Number of states/provinces in which filing | | | \$ _____ per _____ | |
| Number of days in advance of pay date to fund payroll | | | _____ days X 2.5% /365 X _____ dollars of payroll = _____ | |
| System integrations needed? | | | \$ _____ per _____ | |
| Number of custom reports needed? | | | \$ _____ per _____ | |
| Union employee or pay structure functionality? | | | \$ _____ per _____ | |
| Grand Total | | | | |

About Serenic Software

Serenic Software develops and delivers mission-critical ERP software solutions for public service organizations including: K-12 school districts/boards, public sector, nonprofits (NPOs), and international non-governmental organizations (NGOs). Serenic is a Gold ERP and ISV vendor and a development partner for Microsoft. Serenic public service solutions are trusted by over 1,000 organizations around the globe. You can learn more about Serenic Software at www.serenic.com.

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