At What Cost?

## The Impact of Benefits Outsourcing on the Total Cost of Ownership

BY GREG SECORD

Driving down costs, providing exceptional service to customers and employees, ensuring quality, and minimizing risk—these are key actions that not only impact executives, but also payroll and human resources (HR) professionals.

In fact, many of today's payroll and HR departments are required to provide an evaluation of their performance as it relates to these initiatives, most specifically cost effectiveness. Health and welfare benefits administration is no exception. Many HR managers compare their performance to industry benchmarks or seek a calculation model from return on investment (ROI) calculators or total cost of ownership (TCO) studies.

While such studies have documented the financial impact of companies providing health care to their employees, none have evaluated the costs associated with administration of these benefits. And while benchmarking can be a useful tool, the results may not be accurate, as many companies don't use the same methodology for measuring benefits administration costs, nor do they categorize these functions and their corresponding expenses in the same way.

To fill this void, Sourcing Analytics Inc., an independent consulting firm specializing in HR service delivery evaluation, conducted the first benefit services TCO study, focusing on the costs of health and welfare benefits administration. Commissioned by ADP, a provider of outsourced payroll, HR, and benefits administration services, the study compared the costs of in-house administration to the costs of outsourcing.
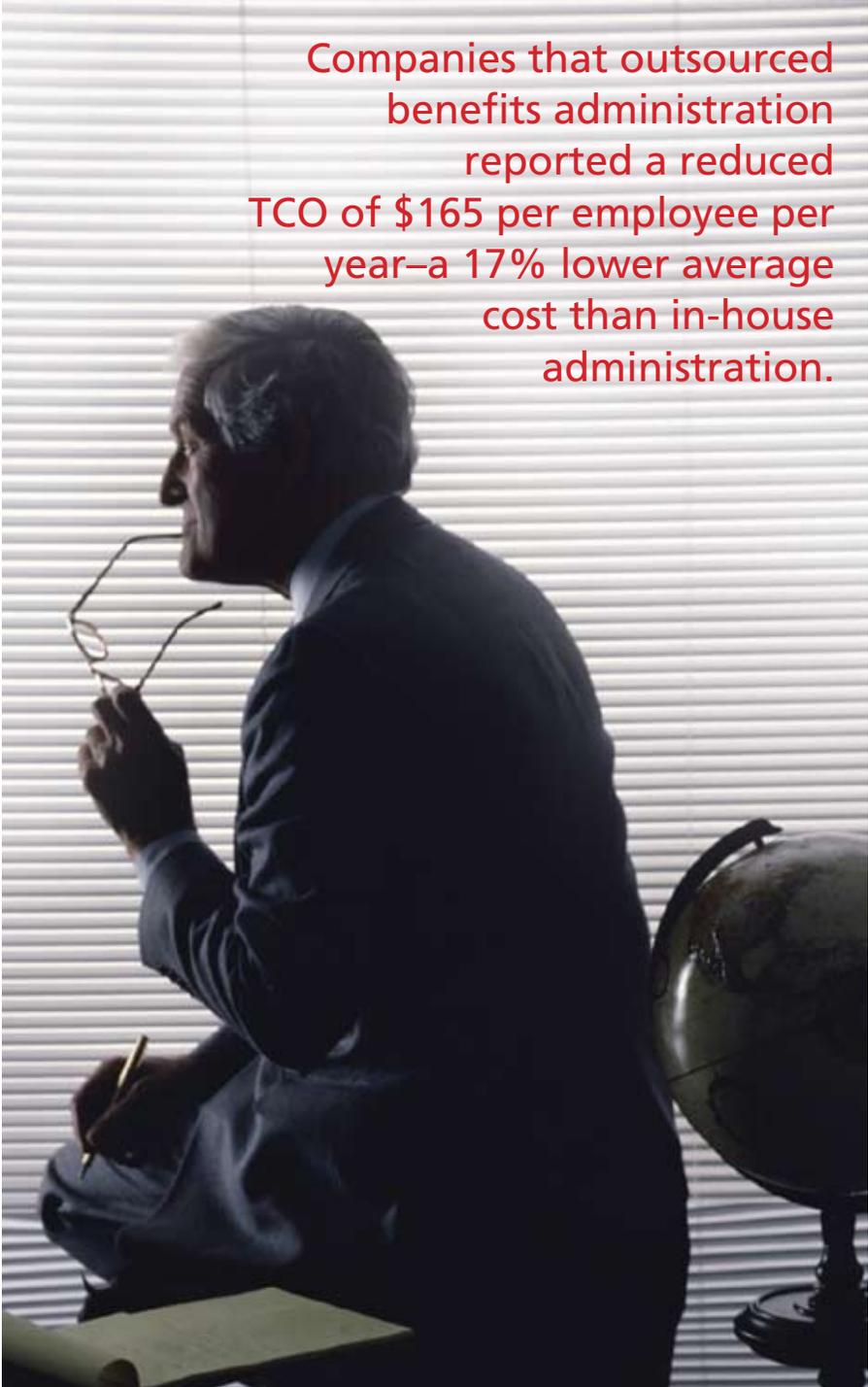
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Methodology

The survey was designed to analyze all costs, regardless of the administration delivery mode. This included in-house costs combined with external costs, whether for outsourcing, consulting, system implementation and/or maintenance, etc. The result was TCO calculations that were consistent across the survey group, which consisted of 36 companies with an average of 5,700 employees.

With no industry benchmark for how to measure the cost of health and welfare benefits administration, it was important to define TCO in a way that every organization could understand and follow.

For the purposes of this study, TCO of health and welfare benefits administration was defined as:

• Determining eligibility for a set of benefit plan types;
• Communicating eligibility and plan options to employees;
• Managing enrollment for benefits at hire, upon a change in status, and during annual enrollment;
• Managing the flow of data to the network of carriers/benefit providers; and
• Managing the flow of benefit deduction information to the payroll system(s).

The types of benefit plans considered included: medical, dental, vision/hearing, basic employee life insurance, short-term disability (STD), supplemental STD, long-term disability (LTD), supplemental life insurance (employee, spouse, dependant), supplemental LTD, accidental death and dismemberment, personal liability, flexible spending accounts (FSAs), commuter benefits, long-term care, and voluntary benefits (homeowners, auto, pre-paid legal, pet insurance).

Study Results

The study results showed that the average TCO for in-house benefits administration was $199 per employee per year. But companies that outsourced benefits administration reported a reduced TCO of $165 per employee per year—a 17% lower average cost than in-house administration. Additionally, the study found that employers experience economies of scale when using multiple outsourced services from a single provider.

Companies that included call-center support services in their benefits outsourcing arrangement experienced a 24% lower average TCO than companies outsourcing without call center support. The average TCO results were $183 versus $151, respectively.

Additional study results showed that organizations that administer benefits in-house could not quantify their costs related to Sarbanes-Oxley. In some cases, companywide costs for regulatory compliance were gathered, but the organizations were not able to segregate expenses related solely to benefits administration. Those that outsourced could mitigate compliance costs with a Type II SAS 70 review performed by an independent audit—a service often provided through the outsourcing arrangement.

A Closer Look at TCO

It is a common belief that outsourcing is more efficient for large companies, in regards to health and welfare benefits administration. However, when the study participants were grouped by benefit-eligible employees in ranges of 1,000 to 1,999; 2,000 to 4,999; and 5,000 or more, the study revealed that the cost relationship between in-house and outsourcing remained the same.

The study also evaluated whether cost changed due to the level of complexity within an organization's benefit program. Complexity refers to the number of plans in a benefit program and the number of data exchanges required to report to carriers, employees, etc.

Generally, one would believe that the more complex a benefit program, the more difficult and expensive it is to administer. That assumption is accurate for those who administer benefits in-house, but not for those who outsource. Employers who outsource do not directly provide the high level of employee assistance required by more complex benefit plans.

In many cases, this allows employers to offer a more comprehensive program. On average, the outsourcing study participants had a 38% more complex benefit package than those who administered the benefit program in-house, enabling them to provide value-add services, such as Web-based solutions for enrollment and ongoing benefits management.

An Individual Decision

Regardless of a company's size or benefit program complexity, outsourcing benefits administration appears to lower costs. Enterprisewide change management often starts with evaluating options and the associated costs. With this knowledge comes the power to drive targeted process improvements that help to decrease costs, improve service, and ensure quality across the organization.

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