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The human side of M&A: Selecting an HRIS delivery model

Part of the *#Tech @the heart of M&A* series
on M&A technology topics

An important priority for organizations engaged in a divestiture is to quickly and cost-effectively start up and deliver human resource (HR) services to enable a smooth employee transition from parent company (RemainCo) to a new organization (NewCo). Many NewCos are accustomed to relying on the RemainCo to provide HR and other back-office processes, services, and systems. Due to this previous dependence on RemainCo and the perceived need to create something new, NewCos may leverage the divestiture as an opportunity to select and tailor their HR Information Systems (HRIS) to their specifications and needs as a new organization. While doing so, they should focus on minimizing cost, mitigating business disruption, and managing a short time-to-close window. It is important, therefore, to select an HR technology strategy and HRIS deployment model that will meet NewCo’s strategic, operational, and employee needs.

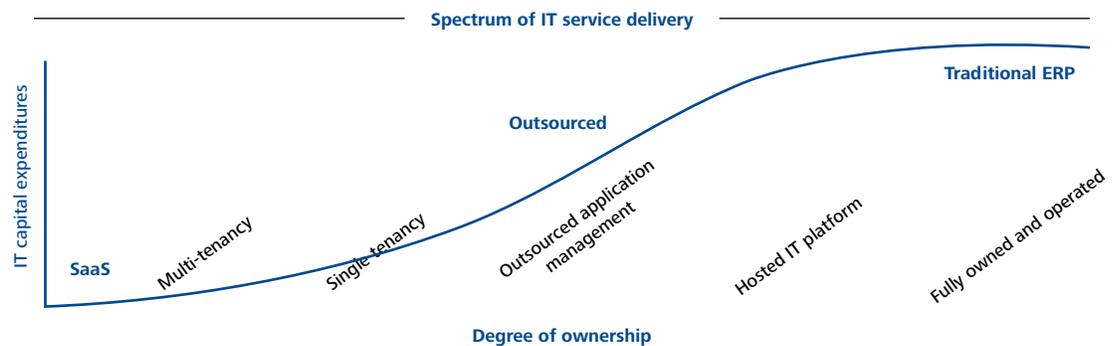
HRIS deployment model options

In addition to client-specific considerations, a divestiture environment has a number of recurring factors that tend

to heavily influence HRIS technology and service delivery model decisions. For example, when defining the HR Service Delivery Model strategy for Day 1 and Day 2, a NewCo should assess its current-state HR operating model and determine which process and technology changes and which deployment approach (local, regional, global) would help optimize the future-state HR organization’s efficiency and effectiveness. This process should be done in tandem with developing NewCo’s overall enterprise IT strategy to align HR and broader technology decisions and enable synergies with vendors around cost, service, and interfaces (for example, general ledger, travel and expense, and financial consolidation processes).

Before analyzing some common HRIS selection considerations in a divestiture environment, it is helpful to understand the differences among the three major HRIS system delivery models: Software as a Service (SaaS), outsourced, and traditional Enterprise Resource Planning (ERP) (figure 1).

Figure 1:



Software as a Service (SaaS): In a SaaS environment, the HRIS solution is fully hosted and managed by a third-party software vendor who is responsible for the application, the infrastructure, and ongoing support. The characteristics of a divestiture have made SaaS platforms a popular choice for companies looking to start up their HR function quickly and cost-effectively. In addition, SaaS platform functionality can be enhanced over time because vendors generally release solution updates two to four times per year.

Outsourced: In an outsourced model, the organization engages a third-party vendor to supply the system software, hardware, and a range of support services (such as payroll processing and HR administration) under a single contract.

Traditional ERP (On premises): In a traditional ERP model, the organization owns and maintains the hardware and infrastructure. Software licenses are purchased outright for a set fee based on employee population and module scope. Software configuration, support, and enhancements are managed, developed, and tested internally; this gives the organizations the highest level of control when customizing the HRIS solution.

More organizations are choosing SaaS and outsourced HRIS models

Industry observations and Deloitte's work with companies engaged in divestitures with 100-8,000 employees have revealed an important trend: Over the past three years, HR technology selections during a divestiture have moved away from ERP models to a fairly even split of SaaS and outsourced solutions. Selection decisions typically hinge upon several recurring considerations (figure 2).

Figure 2:

Consideration	Why it is important	ERP model	SaaS and outsourced models
Transition Services Agreements (TSAs)	RemainCos typically try to minimize TSA services and push for quick exits from TSAs, creating urgency to quickly launch the HRIS solution.	<ul style="list-style-type: none"> • May require longer implementation timeline due to need to set up hardware and infrastructure solutions in addition to configuration/customization 	<ul style="list-style-type: none"> • May require shorter implementation timeline due to use of vendor's existing hardware and infrastructure; focus is on configuration
Time to close	The structure of many divestiture deals includes a short time to close and limited or no post-close RemainCo TSA support.	<ul style="list-style-type: none"> • Generally requires longer implementation timeline, which may not be compatible with a deal structure that includes a short time to close and limited or no post-close TSA support • Requires highly skilled resources that the NewCo may not have in house 	<ul style="list-style-type: none"> • Provide opportunity for single contract for technology and outsourcing services (payroll outsourcing, for example), eliminating the need for the NewCo to build those capabilities in house • Can leverage the third-party provider's established processes, controls, and personnel
Timing of capital expenditure	Newly spun-off companies may not be able to afford directing a large capital investment away from the business, making the payment schedule and the associated cash flow impact an important consideration.	<ul style="list-style-type: none"> • Potentially has higher upfront capital costs for hardware and software licensing • Is typically paid for out of the capital expenditure budget rather than the operating budget 	<ul style="list-style-type: none"> • May require smaller upfront investment; just implementation and subscription costs • Are typically paid for out of the operating budget rather than capital expenditure budget • Payment terms differ by vendor; some begin charging for subscriptions at the time of contracting, not go-live

Consideration	Why it is important	ERP model	SaaS and outsourced models
Total Cost of Ownership (TCO)	There is often pressure on the NewCo to demonstrate value quickly and with fewer resources than the RemainCo has at its disposal.	<ul style="list-style-type: none"> Often has a higher TCO due to cost of infrastructure hosting, data security, and hardware maintenance 	<ul style="list-style-type: none"> Often have a reduced TCO and a continual upgrade model to deliver the latest functionality Transitions responsibility of managing ongoing operations to the vendor, reducing the NewCo's need to maintain a large HRIS service delivery team
HR operating model	The RemainCo may retain the highly skilled and historically scarce technical resources (application developers and database administrators).	<ul style="list-style-type: none"> Generally necessitates a higher level of technical resources to manage, develop, and test configuration and enhancements Depends heavily on IT for functional and technical support 	<ul style="list-style-type: none"> Can reduce dependency on internal IT because vendor manages upgrades, including testing A SaaS model still requires some level of skilled HRIS resources to support vendor upgrades

HRIS system implementation and management challenges

Implementing and managing a SaaS or web-based/outsourced HRIS model are both relatively easy compared with a traditional ERP model; however, organizations still may encounter some pitfalls and challenges.

SaaS delivery model considerations

Contracting and fees: Some vendor contracts stipulate that billing will begin the first time the client accesses the environment. This billing model can be taxing to a NewCo's cash flow when it's trying to mitigate pre-Day 1 expenses. Also, the NewCo HRIS set up may take place before the actual NewCo is legally established, again presenting a cash-flow risk. An organization should clarify the billing process early in the delivery model selection process.

Application integration: A SaaS HR solution likely will have to be interfaced to numerous in-house and third-party applications. An organization should determine which integrations are delivered and supported by the vendor and which tools are available for custom integrations.

Solution roadmap: In a SaaS environment, the product's roadmap is as important—if not more important—than its current capabilities. An organization should verify that its priorities are aligned with the roadmap.

Test environment: SaaS providers tend to limit the number of non-production environments. Multi-phased deployments may present challenges, so an organization should evaluate the testing strategy to determine the correct number of environments.

Release management and post-Day 1 solution management: An organization should proactively plan for new product releases during the HRIS implementation, as these can alter implementation timelines (for example, a release during User Acceptance Testing). To aid solution implementation and ongoing management, employee hires should include individuals with the capabilities to manage solution configuration, integration, and reports. And because many SaaS solutions require annual maintenance services (AMS) to update or deploy new functionality, having knowledgeable in-house staff may mitigate the annual expense of a third-party provider performing these tasks.

Outsourced delivery model considerations
Contracting and service level agreements (SLAs): During the contracting process, it is important to prioritize the negotiating and contracting process for HRIS SLAs, solution governance, and defined escalation path for service challenges. If engaging with multiple third-party vendors for HR services, SLAs should account for cross-functional and cross-services items.

Vendor business and delivery model: Some outsourcing firms position themselves as a “one-stop shop” for a company’s HRIS and HR administration services. However, these services actually may be managed by various vendor teams so it is important to clarify and understand the vendor’s business and delivery model.

Application integration: Similar to SaaS HR solutions, outsourcing models will need to be interfaced to numerous in-house and third-party applications. The organization should determine which integrations are delivered and supported by the vendor and which tools are available for custom integrations.

Business strategy alignment: An organization should communicate its business objectives and outsourcing strategy to all vendors and provide documented processes and workflow to mitigate potential service gaps.

HR services delivery model: During vendor selection and implementation, an organization should define and validate the Day 1 HR service delivery model to enable clear understanding of which services will be retained versus outsourced. If outsourcing a large portion of back-office, core HR services in addition to HRIS, it is important to consider the full spectrum of HR processes (HRIS linkage to payroll, inclusive of payroll administration, tax services, and garnishment payments) to manage cost and drive operational efficiency.

In a typical divestiture, HRIS implementation time frames are short and the NewCo’s capacity for capital expenditures may be limited. After weighing these and other considerations, many organizations are choosing SaaS and outsourced HRIS models to quickly and cost-effectively start up the HR function and focus their employees on the exciting future ahead.

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