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### **Session 56IF**

#### **Pension Plan Administration: To Outsource or Not?**

**Track:** Pension

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*Summary: New technologies, administrative complexities, and a general desire of companies to focus on their core business activities lead plan sponsors to consider alternative means of providing plan administration. By attending this session you learn about different approaches to outsourcing and the role that actuaries might play in future plan administration.*

**Mr. Anil K. Kohli:** Mr. Fowler is a certified employee benefits specialist and he has been working in this field for over 15 years. He has been on both sides of the fence. He worked for a corporation that outsourced pension administration functions and now he is a member of Wyatt's Outsourcing Group.

**Mr. Scott Fowler:** I worked previously at United Technologies Corporation's corporate office. United Technologies, as you may know, owns Carrier Corporation air conditioning, Sikorski Helicopter, and numerous other large companies. I would say it has advanced far in the area of outsourcing. It has done basically what can be done from an outsourcing perspective. I had a great experience working there, and I was exposed to many different facets of the outsourcing industry.

**Mr. Kohli:** We know that outsourcing is the hottest news in the pension industry right now. We will not be able to cover everything that relates to benefits

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outsourcing because there's not enough time. So we'll be talking about only the issues as they relate to the decision of whether to outsource or not. Mr. Fowler and I will talk briefly about each issue and then get your reactions.

Our agenda is divided into four major topics: the first topic is the environment. The environment is important as this is what is making outsourcing a viable option. In the second topic, we will talk about the solutions available to us. The third topic is about the issues to consider for outsourcing, and the fourth topic is the strategy to be defined, which means the decisions one has to make in outsourcing pension plan administration.

Outsourcing seems to hold many promises. Every day companies are evaluating whether outsourcing is for them or not. But it also has some pitfalls. Outsourcing the complete pension benefit administration is a fairly new thing, and we don't know yet what sort of implications it can have down the road. This is because there are companies that have gotten into the outsourcing business on the premise that they will be able to meet the expectations that are out there.

#### ENVIRONMENT

Let's examine the environment where all this is happening, before we really get into the discussion about the probable solutions and so on. What are the forces that are really creating the demand for the outsourcing? To start with, it is the aging population—baby boomers who are reaching their 50s and are planning for their retirements. They are putting extra demands on the benefits staff to provide more information as circumstances change so that the baby boomers can plan for their retirement years. There is an increased awareness on the part of employees and they would like to control their own retirement funds. This has also caused some companies to change their retirement plans. We see that the traditional defined-benefit plans are being changed into cash-balance plans and defined-contribution plans. Increased competition is putting pressure on companies to minimize the cost of providing these administrative services.

Increased legislation and administrative complexity has increased the cost of providing these services. There's pressure from the investment community to reduce the cost of these functions and to provide a quick return on investment. As you all know, more and more individuals are getting into the stock market. That itself puts pressure on companies and has increased the expectations about what kind of a return investors are looking for from the market.

The availability of advanced technology has provided the tools to reduce the cost of providing these new services in addition to allowing easy information access to employees. Interactive voice response (IVR) is becoming very common. Virtual

service centers are being established by many companies. The Internet and Intranet have provided easy connectivity and accessibility. The year 2000 problem also has caused an extra burden on the available resources, and it has forced companies to consider outsourcing as an option. Many companies are doing process reengineering. Outsourcing pension services is one of the items that comes up during the evaluation of a company's processes and procedures.

There's significant merger and acquisition activity, which has created decentralized administration and multiple and nonintegrated databases. This typically results in increased administration costs. Corporate downsizing has created many open retirement window programs, which in itself puts an extra burden on the pension administration staff.

Companies other than traditional consulting companies are getting into this market. If you look around, you see that investment houses and big banks are thinking of getting into this market. There is a shift in the type of services provided by consulting companies to generate more revenue. Traditionally, consulting companies have handled the valuation work and the needed compliance work and have stayed away from detailed administration work. This has changed as valuation work has become very competitive. I remember 15 years ago outsourcing was just a buzz word. Now it seems it is here to stay. Now the momentum has built up so much that we see that even the big guys with the very deep pockets are getting into this act.

I think these are some of the factors that have created an environment in which outsourcing has become a very viable option. Whether full pension administration outsourcing is going to stay here or not, only time will tell. It is going to depend upon how fast these outsourcing companies can educate themselves and how willing they are to spend millions of dollars to build the infrastructure to have economy of scale and to meet clients' expectations. Just as there are a number of companies today that are still not sure whether they should outsource or not, there are a number of companies that are not sure whether they should be handling outsourcing business. Some are getting into this to protect their current book of business.

**Mr. Fowler:** A couple of comments on a couple of things that you said. There are many benefit service providers suddenly entering the market or trying to enter the market. What they're doing, basically, is throwing a lot of money in technology, and they're raising the bar every time they do that. We're seeing technology advance at incredible rates and everybody is playing catch-up. It's almost become a game of whoever can throw the most money at their technology to get them furthest ahead is going to win. There's only one downside to that, and that's what many

companies are finding out: there's more to outsourcing than throwing a lot of technology at the problem and coming up with solutions that are all technology driven.

You must have consulting expertise; you must have some real bench strength as far as benefit knowledge goes. Some folks feel that customer service representatives (CSRs), for example, are low on the totem pole and they don't really have to train them that much because they have all this nice technology at the desktop and that's going to get them through whatever issue is thrown at them. But they're finding that the knowledge of benefits is just something that you can't grow on a desktop, so to speak. I think that's becoming an issue, as far as keeping all the technology moving ahead and advancing. That's why you just see so many people out there looking at technology and saying, "The guy down the street has got something better." Then the guy further down the street from them has got something even better, and everybody is trying to better that guy.

Many issues are coming up through human resource reengineering. I'm just trying to recap some of the issues that Mr. Kohli has said. I recently talked to somebody who works for, I believe, the state of Michigan. This person was thinking about reengineering the company's human resources (HR) department. The company currently has about 90 people who handle the administration of all the benefit programs and they have absolutely no technology support. It's all done with pen and paper. I couldn't hold back my comment that the company is ripe for outsourcing as far as I'm concerned, because having technology and the correct processes and procedures could really bring it into some tremendous efficiencies and some real customer service.

**Mr. Kohli:** I just want to add that technology is very important because the biggest driving force of outsourcing is really reducing the cost. That's what they are really selling out there. I mean, there are other reasons for which companies have outsourced pension administration. We were involved with one company where cost was not the main issue. The purpose was to reduce the employee count because Wall Street was not looking kindly at that company because of a low revenue-per-employee ratio. The implementation strategy was designed to first outsource those functions that would reduce the employee head count. It is true that the small companies, especially small consulting companies, don't have a chance to get into this business, because they don't have deep pockets like some of the investment houses that can spend millions of dollars on the new technology. At the heart of the outsourcing is the service center and the service center is really driven by technology. You can only make money by applying economies of scale.

We evaluated a number of consulting companies for one very large client, and we learned how hard it is for small- to-medium size benefit-consulting companies to get into outsourcing. These companies were overloading their consultants who also handle the traditional services, by that I mean their regular client work. If a question cannot be answered by the service center, we learned the question ultimately goes to the consultants; these are the same consultants who are also assigned to do other client's work.

**From the Floor:** It would be very helpful to me if you were to put some frame around the use of the word "technology" and about the service center being technology intensive. What are some of the things that are included in the definition of technology for the service center? What are some of the things that you would include? I may be really naive, but I'm trying to understand what you mean when you use the word "technology."

**Mr. Kohli:** Let me answer this the way I understand. The technology we're talking about is, for example, what happens when an employee is handled by a service center. The employee can pick up a phone and dial only one number and can get answers to all of his or her benefits-related questions. If the service center is handling pension, health and welfare, answers to questions related to any of these benefits is through a single phone number, even though the call goes through multiple locations and data centers.

That kind of technology, from an architectural point of view, can become very complex. For example, one of our clients elected to have different vendors handling different types of benefits with a single call center. There are a number of issues that we're going to talk about later on about whether you should go with one vendor or multiple vendors. In this kind of a situation the technology plays a very big role in making the service completely transparent to the employee.

It's not that technology is not available for doing all this. It is there, but it's the implementation and making it work on a ongoing basis that is expensive. Get feeds from multiple data sources and then make sure that it reconciles because everything is on a real-time basis. It's not the valuation type of work where you can get an extract and can run the valuation numbers. Technology is the underlying hardware, software, and communication gear that allows you to meet users' needs by having the service center operator able to easily access all the needed information. We're talking about hypertext, so that an operator can look at the help screen for plan provisions. We're talking about imaging technology that's completely integrated where representatives can view immediately the proper papers signed by the employee. We are talking about online analytical processes that can handle life events or model "what if" scenarios.

**Mr. Fowler:** When I think technology I think there's an infinite number of levels of technology. You can say technology is just going to be a benefits calculator. So somebody can like that and you have to talk about your inputs. Is it going to be a kiosk, is it going to be a phone where they go through an IVR, or is it just going to be a phone with a CSR asking, "What can I do for you? What can I calculate for you?" and things like that. That is one level of technology—we have a benefits calculator helping the CSR. Then you can go to the next level. What if an individual has a question about his or her options upon retiring? Do you want the CSRs to reference a manual or do you want them to have something online where they can start looking at plan specifics and things like that? Then what do you want them to look at? Do you want them to look at a scanned version of a summary plan description (SPD) or do you want them to have an online hypertext-plan help menu selection out there? Then when they go to send out forms that say an individual wants to retire, is that via a click of a button and it's automatically produced and mailed virtually without any human interaction? When it comes back in, is it scanned in and up pops a bunch of boxes that inform somebody that a particular box needs to be filled out in this scanner, and things like that? You just keep raising the bar until you get to the point where a CSR can be in a paperless environment. Or you again go back to the place where you say, "We don't really need that. Our company is not set up for that. Everything is kind of manual, except we have a benefit calculator sitting out there." Again, there's so much new technology coming out as far as the Intranet, the Internet, and new things like that. We're finding that many plan sponsors are very, very interested in Internet technology. Now the bar is starting to go up again. The next question is what's going to happen after Intranet? I'm still waiting to hear that and I'll keep my fingers crossed.

**From the Floor:** Take that a little further. I think what we're going to see at the service end is paper less communication. Why are you paying someone to sit and read a script when you can have IVR technology doing it and when you can have that SPD that is available for your company over Intranet or Internet? Why not only have the CSR do something that actually adds value? If somebody needs their retirement package, there's no reason for them to talk to a representative when they can punch in their ID or their Social Security number and have a retirement packet go out with a bar code on the side and the Social Security number. When the forms come in, they are automatically updated through the scanner and nobody's keying in numbers. That's what we're going to see. Basically work that can be done by the computer will be done by the computer.

**Mr. Kohli:** Excellent. That's absolutely true. I think it's not very far off when you will be able to log on to the Internet, get all these things right from your home, and provide feedback right there.

**Mr. Fowler:** We might almost be there. Getting a retirement package through the mail is totally hands off. You can do that through an IVR. There's no question about it, provided the data will support it. I think there are only two resistances to a totally automated "CSRless" environment. The first is many plan participants don't want to talk to an IVR, they want to talk to somebody. The second is the theoretical issues that people will always have that an IVR just is not going to be able to address. Why does my benefit go down when I select a 50% joint survivor annuity? We could perhaps have an IVR there. I think technology is getting us very quickly to that point.

**From the Floor:** There's another place where we'll have problems with option elections. If we get around it with an ID or Social Security number and a few numbers of the employee, what do you do about the joint survivor issue? So there's going to be some paper until our legislators catch up with technology.

It has been my experience, and the experience of some other people, that different industries are more accessible to outsourcing than other industries. Some industries are very comfortable because many functions are already being handled by outsourcing companies. The cultural issues in certain companies have to be dealt with. Technology is more cultural.

**Mr. Kohli:** Correct. I think what it boils down to is that we don't see any end to where you will stop spending money on the technology improvement. That brings us back to the same question. Can companies spend that kind of money? In my opinion, I think there's going to be a fallout. Everybody will not be able to stay in this business. It will also depend upon the approach that different companies are going to take in defining and implementing the services they will provide. Consulting companies have to make their money by becoming very efficient in providing these kind of services, which may not be true for some other companies such as investment houses. They can throw in all these services for free, as long as they can manage your plan assets. They have bundled up the cost associated with these services. I think we are going to see different kinds of players now. The field is open to all kinds of businesses, not just to the benefits and actuarial consulting companies.

**Mr. Fowler:** Another comment to what you had said. The manufacturing side is a whole different mind-set. When you take away the nice HR department to encourage people to go to someone else with questions, these people start to get really cranky. There are some ways around that are just starting to come into popularity. One is kiosks and another is IVR, but you have to give these people some time to get to a phone because that's another major issue. They're a tougher audience to satisfy. There's no doubt about that.

**Mr. Kohli:** We have investment houses as our clients, and one of them is seriously considering getting into other work such as valuations and pension consulting. That means the valuation side is not going to be limited to consulting companies either.

### **SOLUTION OPTIONS**

The next category is solution options. We are talking about outsourcing, and I presume everybody knows what outsourcing is. It's like having a third party do all or part of your functions that were formally done in-house. But outsourcing doesn't mean that you have to outsource everything. It can be just some of the internal functions that are outsourced. Some may call this as co-sourcing. The options are, first, that either a company can outsource some or all of its current functions. If you really look, most of the valuation work or the regulatory work, even the benefit calculations, are being outsourced to consulting companies. The second option is that not only can you outsource whatever functions you're performing currently, but you are even able to get more of what the vendors are willing to provide. One of the current services that can be outsourced is routing calls from employees and retirees to the service center. If you do that, it means that the data and the data management can still be done in-house. You can benefit from the technology that the vendor has in providing service center accessibility. The vendor can tie into your databases and provide a better service to your employees. Or you can also outsource the maintenance of employee and employer data. There are companies that will maintain the data for you, do all the updates, quality checks, reconciliation, etc., and provide you with access to the data and the programs for you to run in-house. We'll talk about the pluses and minuses of each later on.

It is very common for companies just to outsource the enrollment and eligibility process. You can outsource only pension payroll and administration. Here we're talking about the retiree payment management, which a number of companies have outsourced to banks and trustees. The other function that can be outsourced is pension calculations, both estimates and final benefits. This has been outsourced traditionally to the consulting companies. Then there is the benefit statement production. Companies have gone out and outsourced comprehensive personal statement work because they may not have the capability to pull feeds from the different systems and produce a fancy-looking personal statement.

If you outsource, then you can also give employees the power to really control their decisions. For example, we talked about using IVR to change fund allocations in 401(k)s or to do pension modeling online. You can also have more frequent updates of your data because of the technology that is offered by vendors. You can also provide retirement financial planning online to your employees. You can combine other services such as notices, announcements, etc.



You can also outsource retiree consultation services. This, I feel, is the hardest thing to handle by outsourcing companies. I have not seen any company doing one-on-one counseling; I have seen only group consulting sessions. Large companies have traditionally provided retirement counseling while also providing some financial planning. It can be one-on-one or in a group session. I wonder what happens when a company has provided this and wants the outsourcing company to perform this function as the company has lost all of its staff and experience because of outsourcing.

**Mr. Fowler:** There are some people out there who are for retirement seminars. We want you to go out and do a road show to all of our locations and talk about retirement planning, the 401(k), and the whole three-legged stool type of thing. I've seen that outsourced. I'm not sure I've seen one service center serving all benefit programs through a common CSR.

Another fairly new product that many people are getting into right now is taking all these data—and it could be multiple sources—and coming up with a service center that can pull it all in. It doesn't mean it can come up and consolidate it. It must just pull it all into a common desktop. But now you have a CSR who can answer questions about everything. That's a type of product that many people are exploring. Getting that middle layer to consolidate all that information, at least pull it together, is rather complex and pricey, but I think we might start to see that be more common.

### **ISSUES TO CONSIDER—COST SIDE OF THE EQUATION: FACTORS FAVORING OUTSOURCING**

Let's look at the cost side of the equation. What are the factors favoring outsourcing? Obviously, one factor is the overhead expenditures of providing these services. The major piece comes from personnel cost. The vendors can provide economy of scale because they are providing similar services to a number of clients. The second factor is that HR departments are unable to respond effectively to the growing demands placed on them, which can happen for a number of reasons: limited staff administrative processes that are still manual. It's a very high cost for necessary system modifications and maintaining systems that are adequate.

There can be a delay in evaluating and implementing new initiatives, which means that the company just can't get approvals for new technology fast enough. There can be a high and persistent level of dissatisfaction about the current status quo. It's also possible that the company is unable to keep up with new technology, just because of the cost that is associated with uncoordinated benefits departments, which might happen due to mergers and acquisitions. There is concern about legal liability from poor administration. Some companies feel they just don't have the

staff to perform this function properly. We know of one company that was actually sued for millions of dollars because of poor benefits administration. It just couldn't keep up with the high turnover employee data and it ended up outsourcing the whole function. This company just didn't have enough trust in its own systems and accounting departments to pull it through. The management felt that the best thing was to outsource the whole entire function.

It may be because of the multidivision and multiplan processing difficulties. We've been talking to one prospect who has about 280 different plans. It was asking how much it would cost. It's fairly expensive, even if you have to do these calculations in-house. It also depends on the employee base. We have seen some companies, especially technology companies, put high burdens on their HR staff. Technology companies are more demanding than, say, department stores, where people usually don't ask that often what their benefits are going to be. Sometimes the employees don't even know whether they are eligible for the benefits. Most of employees have a short length of service, and there tends to be high turnover.

There can be plan changes because of negotiations. We have a client who has about 26 plans; every other year at least one plan is modified due to labor negotiations. That means that somebody has to maintain these systems and the changes in it. This can increase the ongoing cost of maintaining these plans. It's possible that the organization wants to focus on its core business and does not want to get distracted by HR functions.

**From the Floor:** I think what you're saying is there's a big push for the HR community to be more strategic rather than administrative, and that's absolutely true.

**Mr. Kohli:** Also, there can be a need for benefit plans to be more compatible with the organization's and employees' needs. We have seen that a number of companies, especially those that are technology related, are changing their plans, to retain young employees. They're changing from the traditional final salary plans to cash balance and equity plans. This also gives companies more control over cost, as final salary plans' cost is hard to estimate due to very steep salary increases in the recent past. It is not true anymore that salaries are going up 3%, 4%, or 5% percent each year. In some industries the salaries have literally doubled within two or three years.

**From the Floor:** I have a question about the cost of technology. I think you were saying outsourcing companies have put many dollars into developing software, but obviously a single employer would not be doing it. They're also starting to have the

plan administration software available to an individual company from outside vendors. Is vendor software not keeping up with these systems that are moving up?

**Mr. Kohli:** This definitely falls into what we do. Most of the software designed to be used by corporations (installed bases) can't be used efficiently for outsourcing. To answer your question, the same software used by outsourcing companies is available to corporations as well. We have seen that there's an increase in demand from the companies that want pension administration software for in-house processing. When companies consider whether they should outsource or not, I think there are other issues that play a role other than just the availability of the software. If it is just the software or technology, then obviously they can get the same technology and install in-house.

Also, do these companies have the staff to maintain these systems? In most companies we have seen, the Human Resources Information Systems department, especially the benefits department, does not get much support from the systems department. The question is: will they be able to maintain these systems and support in-house staff, because, in some sense, you are creating a service center. So the technology availability is there, but I think there are other issues that play a role in addition to the implementation cost that will be paid by a single company as compared to an outsourcing vendor that can spread its cost over many clients.

**From the Floor:** Consulting companies that provide the pension administration software are now doing outsourcing because there's so much demand and not enough providers. They're not willing to take what resources they have and perform the system implementation, because if they can do all the work for a client, they're going to put the people towards doing that work. That's just the impression I have.

**Mr. Kohli:** Yes, you're right. I think there is no free lunch. Many of them have stopped selling software because they didn't make money from it. The software was provided to keep the valuation and the other consulting work, which creates an annuity rather than a one-time payment by selling software.

**Mr. Fowler:** There are many vendors that are going to say, "The only way that we're going to be able to provide you with this service is to totally outsource. We are going to have a system where in the administration we're going to have CSRs and the software. We will give you everything you need to know to do your pension administration." There are firms that will do what we call partial outsourcing; that is "they will run the systems or run the administration," but we're finding that many plan sponsors want their own employees to be CSRs and we recognize that. We say that's something that we definitely must be ready to

provide. And then there's always the total outsourcing, so there's really more than one solution. However, many vendors are not prepared to say that yet.

### **FACTORS AGAINST OUTSOURCING**

What are the factors against outsourcing? One important reason is that you cannot transfer the corporate culture. This is especially true in companies that have been in business for a number of years and have provided this personalized service to their employees. Something like that cannot be done once you outsource, because you are cutting the cost and thereby changing the way the business was handled before.

The other factor is that there is a loss of control and flexibility once you outsource. You really have no control if you have outsourced the whole thing and the vendor is maintaining your data. The only functions the vendor is going to perform for you will be what is in the contract. If you ask for anything new, you may be hit with a high cost, or it's possible the vendor may not be able to schedule those things for you in time. There's very little flexibility here. There's dependency because all the information lies with the vendor. You lost your staff, and with that, the knowledge. Sometimes people think that if they outsource something—that's it, they don't have to do anything to worry about anything, but that's not true. There are many things that an employer still has to do. The employer still has the responsibility of managing the vendor(s), making sure that there is some sort of ongoing evaluations, and that cost control mechanisms are working.

Also, keep in mind that the data still have to come from the employers, so the employer is really not out of it. The employer still has to provide data feeds from either the payroll system or from other systems.

**From the Floor:** If a company is highly decentralized and has many locations, and may have different plans and various data sources, then the cost to get that data may be prohibitive for the company.

**Mr. Kohli:** Absolutely true. Also, the cost may increase over time, because once you outsource the whole thing, it's very, very hard to bring it back. You're basically at the mercy of the vendor from that point onwards. Also, it's possible that gains may not be captured because if the vendor becomes more efficient and reduces the cost, it may not pass those reductions in cost to you. So I think that all these things—the performance bonus, etc.—should be spelled out clearly in the contract. The contract really becomes the key instrument for a successful outsourcing project. You really have to spell out everything so all these things are going to be managed and controlled.

**From the Floor:** It may not be a fair sample but I get many situations where the clients who outsourced administration were quite unhappy with the outcome. I'm sure you have come across such situations. Could one of the reasons for this possibly be that the providers for these services had not matured? In fact, I think from that standpoint, the company has nothing to say about the outsourcing.

**Mr. Kohli:** My experience is that you're absolutely right. When we evaluated a number of companies, we found that this business is not mature enough, and there's going to be a fallout. Also, if it is not planned well and spelled out in the project plan about the transition, conversion, and implementation, chances are that expectations are not going to be met. Just saying that you are ready to outsource and the vendor agreeing that it will take care of it without having a detailed project plan is not prudent. Most companies we talked to were behind in their implementation deadlines partially because the vendors don't have the underlying systems and processes completed and tested.

**From the Floor:** It feels as if another disadvantage could be that there is a loss of contact with employees regarding the plan changes. It seems like one source of information concerning plan design or even kind of minor administrative changes is feedback from employees interacting with the plan's administrator on various things. How does a company that has outsourced administration obtain that information?

**Mr. Kohli:** I think both sides have pluses and minuses. Some people will say, "I can go and talk to Joe Snell in his office," but on the other hand, you can do these things in the privacy of your home. You don't have to tell other things that you may not want to tell to your peers or to a company administrator. If you install a financial planner or the retirement planning tool that employees can access, employees don't have to worry about providing personal information about either getting married or filing for a divorce.

**Mr. Fowler:** Just a point on that. We found that using surveys reveals a lot of information. You'd be amazed at what people say on a survey. Granted, not everybody is going to be very happy about your pension plan because it never pays enough, but they'll certainly never hold back on comments about the level of services at the service center. So I personally am a big proponent of using surveys, and if you're coming from a client side, demand that a vendor use a survey and that you can hold the vendor to performance standards that are actually tied into the results of that survey. I want to get back to your comment on problems with vendors.

I think what you see in the market today is the vendors selling and then returning to the office, and thinking, "How am I going to do all this?" They're always in the mode of customization, they must customize everything they do. You'll likely have to customize outsourcing services for the major firms that you just to. But there's nothing that says that every time you go out and sell something, you have to totally customize your operation. Instead, how about developing your operation first and going out and selling that and saying, "Here's what we have. We know how to do estimates. We know how to do retirements. We know how to do this, that, and the other thing. Here's how we do that. Would you like to buy it?" That cuts down on a lot of customization and the dreaded words—scope creep. Every time you sit down with somebody and say, "Even though we're doing that, we didn't know we were doing that." From the client's side, they assumed you were doing that. That can often be gotten around by just simply sitting down prior to signing the contract and saying, "Here's what we believe you want us to do, are we right? Have we missed anything?" and "Here's how we're going to do it." Those two things, I think, cause some real problems in the marketplace. People just don't sit down at the table and say, "Here's what we're hearing you want us to do. Let's make sure we're on board."

**From the Floor:** Can you comment on how the contract should be structured?

**Mr. Kohli:** I think a contract should be designed in a way so that it has built-in penalties. It should spell out what kind of response time, what kind of performance, etc. is expected. What happens if errors are made? How are corrections going to be handled? If you don't do that, somebody is going to pay ultimately, and there's going to be a bad taste in everybody's mouth. Also, what we learned is that the terminology used should also be clear to both parties. For example, the project plan says that the system will be tested. Different people interpret this differently. Is it unit, system, integration, volume, or user tested? You must spell out what they're going to get, how it's going to be tested, and what we mean by testing. The project plan should be made part of the contract.

I want to get back to the earlier question that if you are doing these functions in-house, then there is more feedback because you're talking to the people. As a matter of fact, the technology can really help you there too because all the calls are channeled through one central place, so it's very easy to capture a lot of information that can be consolidated into meaningful feedback for the employer.

Also, little things like how the company is going to be billed, how the cost is going to be allocated, how the pricing is done, should be covered in the contract. Again, there are a number of ways but it should include the survey results and how many

calls that were made, how many calls were dropped, and how many questions they couldn't respond to, and so on.

### **ISSUES TO CONSIDER—BENEFITS SIDE OF THE EQUATION**

Let's look at the benefits of outsourcing pension administration. First of all, it forces companies to clean up their data. We are seeing even large companies with a great deal of technology that have not kept their employee histories in good shape. Outsourcing doesn't mean it's going to reduce your work. Just like that gentleman said, if it is multiple plans in different locations; it's a big job. Even if your company has just one location, it's a big job. The same people who are providing the current ongoing services are also part of the outsourcing team. They will be asked to train the vendor and do all kinds of discovery processes, training, and conversion. Even for a single plan it can be a big job. I think this forces companies to look at and clean up their data and get everything in shape.

It helps companies to bring in new technology without really investing much money. Some companies just can't afford the kind of expenditures that are associated with IVR, benefit modeling, online up-to-date benefit statements and calculations, and calling one number to get all the answers about benefits. It can also create an opportunity for companies to change their plans, if they want to. It may be more cost effective to communicate plan changes to your employees at the time of outsourcing. You can create a more efficient enrollment process. You can also provide productivity improvements. Again, as we discussed, it must be spelled out very clearly that these kind of improvements will be passed on to the employer.

As far as cost savings are concerned, the word to use is potential cost savings. I made a comment earlier that one of the reasons for pension administration outsourcing is the cost savings. For example, assume you are an employer and your administrative cost is about two million dollars per year. If somebody walks in and tells you that they can perform the same functions for you for half the cost, it will be very hard for you to ignore this as you've been trying to improve the bottom line. But whether these cost reductions are going to be realized or not is a different story. The employer should question themselves that if they cannot do it for two million dollars, what makes another company able to do it for a million dollars? Before signing the contract they should look at that company's processes and how they are executed to provide them with savings. This may not be an issue for some companies that may be outsourcing for other reasons.

Now back to the benefits of outsourcing. Because of the case tracking and reporting ability, there can be better monitoring and control of benefit costs. All the calls are going to go through a single place so you can very easily track these items. You also attain superior interpersonal skills because the people who were hired by these

companies for responding to the employees are better trained in how to handle such questions. There can be an increase in the quality of customer service, because the answers are often consistent. Some of the vendors have created the hypertext from which the operators read. So if somebody calls with the same questions two weeks later, he or she will get the same answer as they did before.

Outsourcing also helps you to understand the administrative costs and where these costs are really coming from. Outsourcing is a very lengthy process and it brings up all the issues. It also helps you to improve your procedures and systems. You must be wondering why we're talking about this if we're going to outsource everything. Again, we are making an assumption that you may not outsource everything, only some of the administrative functions.

Other issues are, if you are outsourcing, you must make sure that the resources are available within your company. As we pointed out, the vendor has to be trained and the conversion process will require your staff whose jobs may be lost after it is all done. In this situation, it becomes hard to keep the morale high during the conversion and implementation process.

You must know whether the organization is ready for this kind of a change. Again, this is a cultural issue. Will the culture allow good people to be let go or not? Because when you do outsourcing you are downsizing, you're letting some people go, and there's always the chance that some of the good people will end up leaving too.

If implementation deadlines are not realistic chances are you may not meet your deadlines. Even though outsourcing companies use a phased approach of implementation with every task defined, these time estimates must be very realistic. And if some company is under pressure and requires certain items to be implemented by a certain date, they must monitor the progress very closely.

The company looking to outsource must do this as a long-term solution; short-term solution outsourcing is not the way to go. Finally, security issues must be addressed if your data are sent via electronic data interchange. The data are copied, if your functions are handled by multivendors. How do you really assure yourself that there are no security leaks?

The ancillary items to be provided by the vendor should be discussed up front as you don't have all the data anymore. Make sure the vendor can provide you with a performance measurement the way you want. If cost has to be broken down by different divisions, then the vendor should be able to provide that. Not only should you verify that the vendor has the tools and processes in place to do pension



administration, but the accounting, billing, and management reporting should also meet your specific requirements. You should also have the resources for the ongoing management, communications, and quality assurance of the services and products provided by vendors.

How many of you have really worked for a company that was in the process of outsourcing its benefits?

**From the Floor:** Well, I have.

**Mr. Kohli:** Was it from the employer side or from the vendor side?

**From the Floor:** Vendor side.

**Mr. Kohli:** Can you tell us about your experience? There were some comments made that company expectations can be very high, and these were not usually met by the vendor.

**From the Floor:** It worked out quite well. It was more favorable than what I heard from others.

**Mr. Kohli:** I think the key is in the communication. Even if you have everything spelled out in the project plan, it doesn't mean that it is going to be played out exactly that way. I think everybody understands that things are going to change, either because the company requested some changes as it learned more about the process or because of a change requested by the vendor. Each party must communicate the change as soon as they are aware of it, especially if it has a material effect on the deliverables.

**Mr. Fowler:** In helping some plan sponsors through the request-for-proposal process, we have found a common denominator on what's driving them to outsourcing.

**From the Floor:** Talking about problems, one of the difficulties is the word "outsourcing." I was a consultant the first time I got involved in outsourcing. To the client, outsourcing meant the vendor was doing everything. The vendor really isn't doing everything. It's really sharing responsibility.

**Mr. Fowler:** It means when you're ready to sign the contract, you must discuss in excruciating detail "here is what we're doing and here's what you're doing" for every possible scenario that could possibly come up within that service center. I'm a firm believer that it's good to address many of those issues up front.

**STRATEGIES TO DEFINE**

**Mr. Kohli:** What are the decisions that a company has to make regarding outsourcing? The first thing is deciding whether to hire a multivendor or a single vendor. Obviously there are different issues to consider.

Do you plan simultaneous or sequential implementation of different functions? It is easier to manage expectations if the implementation is done in stages.

You should talk about systems and/or processes and conversions. This is very important. You have to decide what to keep in-house and what to outsource. There may be some functions and systems that may not be economical to outsource, or there may be very few people affected by these.

Is the vendor going to provide multilocation or single location call centers? Multi location may be good for a backup in case one call center is down. Are you asking for kiosk, Internet or Internet-type of access? Every vendor does not have that, and the Internet is also limited because of the limited capabilities of the browsers.

Regarding data integrity, how are the data links going to be provided? If you have multiple vendors doing different functions, they may be sharing the same data. One vendor may be sending information to another vendor. How do you determine the quality of those data and so on? When we were involved with one very large company, we set up the data clearing house because multivendors were involved. All the data was coming into one place from all sources and vendors, and it was reconciled and then sent back to each vendor. It's similar to a FedEx concept.

You must define a strategy to make sure that quality is maintained. One way to do this is by periodic visits, surveys, etc.

Also, what happens in case of errors and omissions? Who is liable? All this must be spelled out in the contract.

Consider pricing. Is it fixed per employee or is it a cost pass-through? How is the gain sharing going to be handled? Who will manage the implementation process once all functions are outsourced and the staff is gone?