



When Small Businesses Outsource Payroll

**Time to build, time to improve,
time to spare.**

This white paper is an overview of how a professional payroll provider can help smaller businesses concentrate on the critical areas of their operations while meeting important regulatory requirements.

Executive Summary

Like most tasks in a small business, there is more than one way to produce payroll each period. This white paper analyzes three options for payroll processing—manual bookkeeping, using in-house bookkeeping or payroll software, and hiring a professional payroll provider.

Many firms choose to handle the payroll function manually in house, typically for cost, cash-flow flexibility, or control purposes. Yet, as this paper outlines, there are a number of drawbacks to this approach, including lost productivity, errors, and security and storage risks.

Payroll software gives businesses the convenience and sophistication of software entry, along with some of the hands-on control of manual processing. Yet, it still takes time to input the data correctly, report and remit taxes to government agencies, maintain the software, and keep up to date with the latest government requirements.

These disadvantages are why over 85 percent of certified public accountants recommend that small businesses employ the expertise of professional payroll providers. Specialized payroll-processing companies provide secure and accurate payroll for small businesses, and often offer additional human resources services that help manage workforces of any size.

Ultimately, outsourcing helps management put more time into what they really do best and into more productive tasks that directly affect the bottom line. Business owners can even use the additional time for strategic improvements of the business, or for hobbies, friends, and family.

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Payroll Is a Major Function

Success lies in the details, and so many of the details of establishing and running a small business fall on energetic entrepreneurs. Eventually, the thrill of starting a business turns into the day-to-day administration of back-office functions in addition to delivering products and services to customers and clients. Paying the rent and arranging for a carpet cleaner can take a few minutes. Taking care of payroll involves painstaking detail—pay period after pay period—whether there are three or 300 employees in the organization.

Fortunately for business owners and managers, there are alternatives to consider for the demanding tasks of payroll processing. Each has its own strengths and level of time commitment and must be judged on its own merits. There is no single answer that fits every enterprise.

Payroll Options for Small Businesses

Entrepreneurs typically start out by calculating their own payroll, and they are often reluctant to assign the task elsewhere. In some cases it may be desirable for the business owner to remain on that task, but more often than not it simply is not a good use of their time.

Once a business owner decides to delegate responsibility for payroll processing and unload the burdensome paperwork, there are three main alternatives:

- Assign it to an employee
- Use bookkeeping software
- Partner with a payroll-processing organization

Your Own Payroll “Department”

Some business owners decide to keep payroll responsibilities or make it an assignment for one or more employees. It could be an add-on task for an office manager or bookkeeper, for example, or even someone hired specifically with payroll and related tasks in mind. Most owners who operate this way believe that it's not a difficult task, and that they will save money by keeping payroll processing inside the organization. They think that assigning payroll processing to a trusted employee is the answer. However, there are risks to this approach, ranging from data safety and security to business productivity and payroll accuracy.

A critical question business owners need to answer is whether they are comfortable allowing employees to access sensitive, private information. Risks include identity theft, embezzlement of company funds, and the unauthorized altering of company records for favors or personal gain.

Some business owners also underestimate the complexity of payroll processing. Each paycheck requires multiple calculations, and the average small business will file 32 tax deposits and 16 returns each year. What's more, it's nearly impossible for a business owner to stay up to date on the frequently changing rules and regulations for employment taxes.

In addition to the complexity involved, small-business owners should be concerned about the risk of misreporting or failure to report employment taxes to federal and state government agencies. Errors can result in costly penalties, which are never anticipated in small-business budgets.

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Most of all, it is the prospect of greater productivity that drives so many decisions by small-business owners. Using working hours to calculate and process payroll does not flow to the bottom line of a business, and owners should ask themselves, “Is this a good use of my time compared with other possibilities?” Since payroll is a necessary task but not one that advances the goals of the organization, owners often conclude that they need to search for a better method.

The Computer Solution

For computer-savvy managers who like to enter data and watch the numbers flow, bookkeeping software is an option to consider. This tool streamlines and partly automates their payroll each pay period. In addition, it can help integrate payroll with the rest of the company’s financials, and program aids typically help novice users navigate their way through the process of setting up employees in the system, entering their wage levels and hours, and accurately calculating the required payrolls. Most programs contain forms for reporting employment taxes to federal and state government agencies.

This do-it-yourself method must also be used with some caution and an understanding of its limitations. Like the previous in-house method, relying on software doesn’t guarantee that the latest government rules and regulations are in place when needed. The onus for compliance remains with the business owner, not the software producer. Outdated tax rates aren’t the only potential problem. There’s a familiar refrain among computer programmers— “Garbage in, garbage out”—which simply means that incorrect input by computer operators inevitably yields an incorrect result.

Using software to process payroll does not eliminate some of the other problems associated with manual calculation. Still present are concerns about the time needed to gather the required information and ensure error-free data entry, the safety and security of payroll data on the company’s computers or network, and using a system that can adjust as the company’s needs change.

Payroll Outsourcing

In addition to removing the payroll burden from business owners and employees, professional payroll providers can provide both obvious and hidden advantages. On the downside, some business owners may perceive that payroll providers are costly and intrusive, but a closer look could dispel those concerns.

Small-business owners who outsource their payroll immediately gain time that they can apply to their long list of daily tasks. They use it to give more attention to key clients or customers, to get started on new projects, to reenergize their competitive efforts, or to simply reclaim some time for relaxation.

Outsourcing delivers the talents of professionals who are expert in the nuances of payroll, payroll taxes, and reporting and remitting to the appropriate government agencies.

Professional payroll providers make the process easy. Employers only need to communicate to their customer service representative once each pay period. With employee pay levels and deductions set up in the system, calculations are handled automatically and all current rules and regulations are applied.

Harried business owners or managers who calculate their own payroll can spend considerable time searching for keying errors. With a professional provider, trained customer service representatives handle the process, and records are available for review online or on paper.

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For business owners who prefer software, online solutions may offer hidden advantages they are not aware of. These offer many of the same features as software but offset some of the disadvantages. For example, online payroll typically requires no software to install, and upgrades apply to all users at the same time.

There is also a convenience factor in allowing key individuals such as accounting professionals and tax-preparers access the company's online payroll account for their work. It reduces or eliminates locating, faxing, or mailing documentation. It also saves time and allows third-party advisors to access or import information so it can be managed faster and more accurately.

Online payroll solutions provide a safe haven for company payroll data through multiple, backup server locations. As long as each user safeguards their password, the data will be locally secure as well.

Data security from a national, publicly traded payroll company provides the kind of scheduled, redundant backup that is beyond the capabilities or initiative of many businesses. The large-scale security budgets of professional payroll outsourcers enable them to invest in state-of-the-art solutions for storing and protecting sensitive data. Their reputations are on the line, and their clients enjoy the resulting benefit that brings peace of mind.

Any decision on a business process should include at least an informal time and cost analysis. At minimum, a cost comparison to outsourcing should include the time it takes business owners or managers to calculate payroll each pay period, the time needed to prepare and remit payroll taxes to government agencies, and the time required to generate reports for in-house and accountant use. An extended examination should include the time and expense involved with associated tasks. For example, what does check stock cost? How much time does it require to print, sign, and distribute checks or pay stubs? How much time is spent researching answers to employee questions about pay when payroll reports have not been run? How much would the business suffer if a fine were imposed for a delinquent payroll tax payment?

Business owners may be surprised at just how affordable a full-service provider can be, especially when evaluated on a per-payroll-period or monthly basis. For example, the cost may be comparable to the monthly expenditure for a mobile phone.

Accounting Professionals Recommend Outsourcing

An Actionable Research survey revealed that more than 85 percent of CPAs who serve small businesses said they recommend a payroll provider over all other methods (such as manual or software processing or even outsourcing to accounting firms). The reasons they cited included greatest accuracy, lowest risk for compliance issues, and reports that are in the most readable formats for accounting professionals.

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Making the Decision

Small-business owners should choose a payroll provider that can offer the right level of service and reliability. Here are the top five questions that owners should ask:

1. Is it a national provider (which helps ensure security, continuity, and quality control standards are in place) with local or regional representatives?
2. Can businesses submit payroll information by phone, fax, or over the Web?
3. Are there multiple data and operating locations in place that enable the provider to keep data secure and serve all clients continuously, even in the event of a natural disaster or other service interruption?
4. Is the provider able to integrate payroll with other business operations that rely on payroll data—employee benefits such as 401(k) retirement accounts and insurance benefits such as workers' compensation and disability insurance?
5. Does the provider offer a wide range of human resource services for small businesses, such as personalized 401(k) retirement plans that easily integrate with payroll and up-to-date solutions for tracking employee time and attendance?

This is a partial list, but it's a good place to start. Armed with the right information on payroll options, small-business owners can feel their payroll pain fade away while they find new opportunities to focus their energy and intelligence on making their businesses more successful.

About Paychex

Founded in 1971, Paychex, Inc. is a leading provider of payroll, human resource, and benefits outsourcing solutions for small- to medium-sized businesses. The company has more than 100 offices and serves over a half million payroll clients nationwide.

The company offers comprehensive payroll services, including payroll processing, payroll tax administration, and employee pay services like direct deposit and check signing. Human resource services include 401(k) plan recordkeeping, employee handbooks, job descriptions, workers' compensation administration, section 125 plans, time and attendance applications, administrative services organization solutions, and other administrative services for business.

Professional employer organization options are available from Paychex Business Solutions, Inc. (PBS).

Paychex Insurance Agency, Inc. makes a full range of business insurance options available, including group health insurance from more than 150 highly rated carriers.

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