

MDF HR
Consulting



FECA

Balancing Benefits

Unlocking the Toolbox

September 2011

Who Am I

- 20+ years professional Human Resources Experience
- Full time consultant for 14 years
 - Sample Clients
 - Internal Revenue Service
 - Department of Defense
 - US Customs Service
 - UK Ministry of Defense
 - Cooperatives Nationwide for the last decade

Cooperative Perspective

States where we have provided solutions.



Topics

- History & Context
- Assessing your Package
- Benefit Trends
- Cost Containment
- Design Enhancement

History of Benefits

- Wage Freezes during World War II
- Benefits to attract employees
- Been Stuck With them since

Benefits Costs as a Percentage of Payroll

- When first offered in the 40's
 - Benefits were insignificant cost
- Until recently
 - Averaged 30-50% of base salary
- Recent trends
 - 50-75% of payroll
- If trend continues
 - Benefits may outstrip base salaries

Why Offer

- Benefits are a tool, in your Total Compensation Toolbox
 - Has the lock on your toolbox rusted shut?
- They contribute to three strategic objectives
 - Attract Employees
 - Retain Employees
 - Motivate Employees

Attracting Employees

- MetLife 9th Annual Study of Benefit Trends Found:
 - 61% Of employees state benefits were an important reason for accepting a Job

Retaining Employees

- 69% Of employees report benefits are an important reason they remain at their current job

Turnover in a Recession

- Recession does not guarantee low turnover
- MetLife study indicates 1 in 3 employees hopes to be working somewhere else in 12 months.
- For the last two years, voluntary quits have been near or exceeded involuntary

Reporting Period	Involuntary	Voluntary
July 2010	49%	44%
July 2011	43%	50%

BLS Job Openings and Labor Turnover Summary (Sept 7, 2011)

Motivating Employee

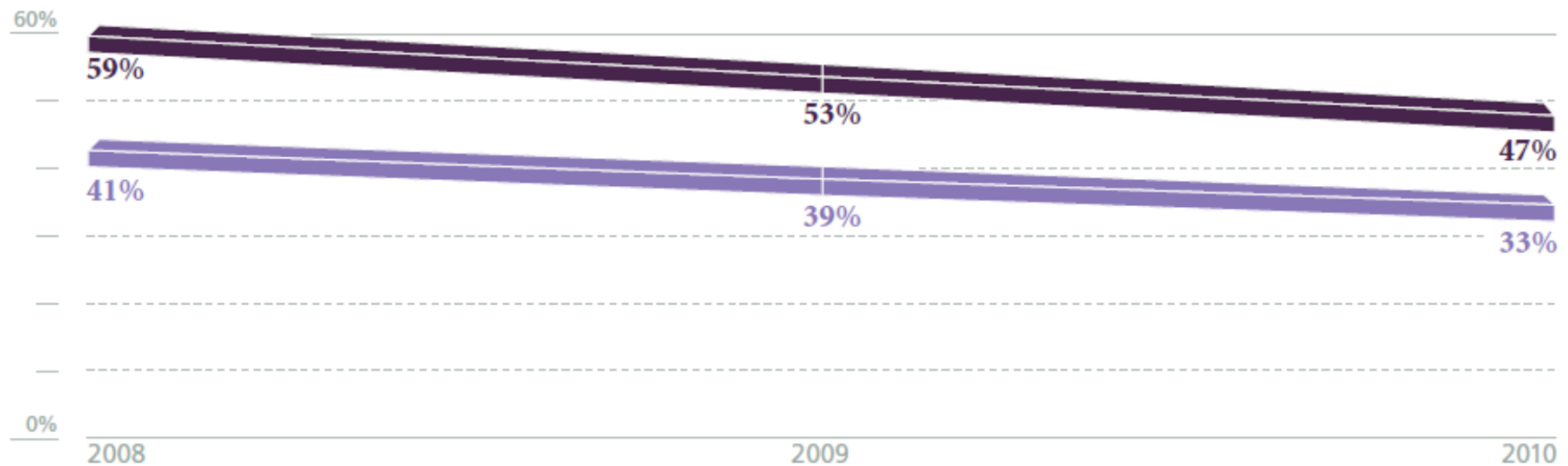
- Job satisfaction aligns with benefits satisfaction
- Of workers satisfied with benefits
 - 81% Satisfied with current job
- Of workers unsatisfied with benefits
 - Only 23% satisfied with job

Loyalty Gap- Employee

Employees and employers have different views of loyalty

Employees who feel:

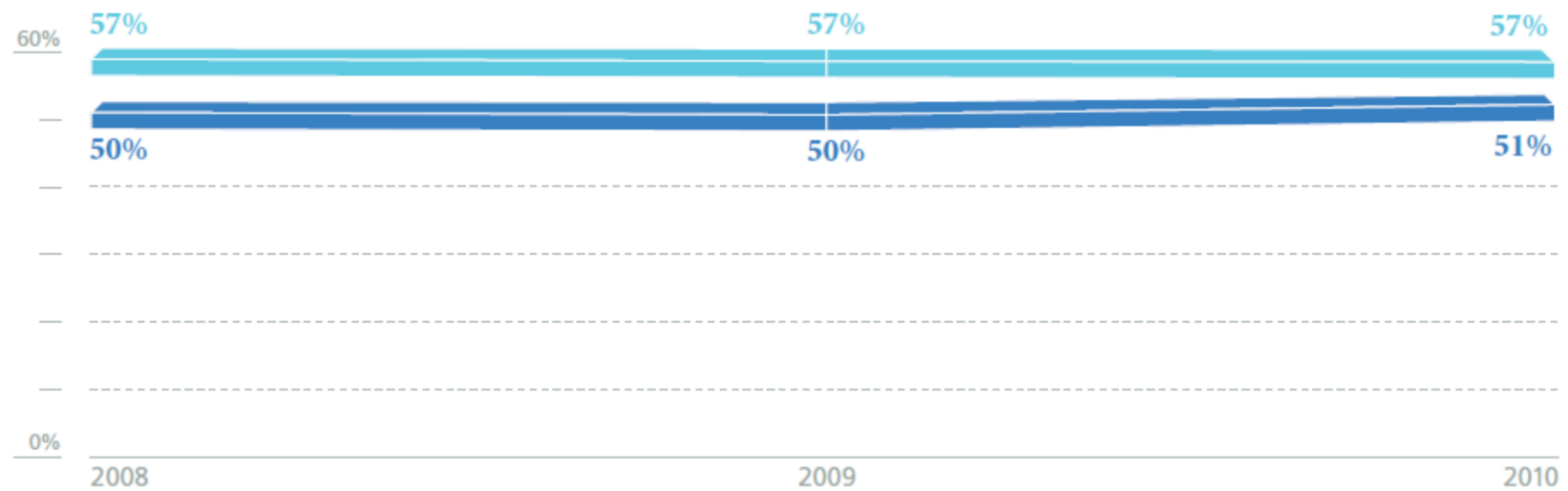
- A very strong sense of loyalty to their employer
- Their company has a very strong sense of loyalty to them



Loyalty Gap - Employer

Employers who feel:

- A very strong sense of loyalty to their employees
- Employees have a very strong sense of loyalty to the company



Business Objectives

Most employers ranked cost control as their most important benefits objective

Employers identified their top objectives and then ranked these in order of priority



Bridging the Loyalty Gap

Factors considered extremely important to loyalty

Factors considered extremely important to loyalty	EMPLOYERS	EMPLOYEES
Salary/wages	70%	79%
Health benefits	58%	74%
Company culture	52%	44%
Advancement opportunities	46%	51%
Retirement benefits	38%	64%
All other benefits (dental, disability, vision, life, etc.)	37%	59%
Programs that help create work-life balance	32%	43%
Health and wellness programs	26%	35%
A choice of voluntary benefits	21%	36%

High-Value Benefits
Employees place much higher value on non-health and retirement benefits than many employers realize.

Benefit Satisfaction & Loyalty

Satisfaction with benefits is associated with greater employee loyalty



Employees who are highly satisfied with their benefits



Employees who are highly dissatisfied with their benefits

Topics

- History & Context
- Assessing your Package
- Benefit Trends
- Cost Containment
- Design Enhancement

Strategic Analysis

- Every Human Resources program you spend time and money on should be subjected to three “Strategic” tests
- Programs include but not limited too:
 - Each piece of your benefit package
 - Base compensation
 - Scheduling practices
 - Recruiting Procedures
 - Performance Management

Test One: Legally Required

- Are you legally required to have it?
 - Minimum Wage
 - Worker's Compensation
 - Equal Employment Opportunity
 - Paid Leave (Mandatory in some localities)
- If yes
 - Make sure you are in compliance
 - Compliance done in the most cost effective manner

Test Two: Support of Objectives

- Does this program help us
 - Attract
 - Retain
 - Motivate Employees
- Does it support an operational objective
- Keep it and figure out how to make it even more efficient in it's support

Test Three: Not Doing Either

- Does it meet either of the first two tests?
- If no, why do we still do it
 - If it's not legally required
 - Employees don't want it
 - Not supporting an operational objective
- Stop wasting time and money on it

Environmental Scan

- Who do you compete with for labor?
 - What do they offer for benefits?
- What do your employee's spouses get for benefits?
- Sources of information
 - Benefit Surveys
 - Do your own survey

Competitive Analysis

- How does your package stand up to others
- Do we have the right mix of “Total Compensation”
 - With “Lexus” benefits, you may be able to afford “Hyundai” base pay.
 - If you have “Yugo” benefits
 - Trade up somewhere

Internal Analysis

- How do your employees perceive your benefits
 - Have you asked them
- Ask them
 - Find it valuable
 - Perceive it as competitive
 - Willing to pay more for it
 - Still want it even if they had to pay for it

Generational Concerns

- Gen Y Age 21-29
- Gen x Age 30-45
- Young Boomers Age 46-54
- Older Boomers Age 55 and Over

Generation Y

- Hardest hit by job market freeze
- More anxious to leave
- More dissatisfied
- Benefits not a big retention factor
- They do recognize the value
- Effective benefit communications most important to this group

Generation X

- Value benefits more than Gen Y, but tend to be less satisfied with benefits
 - Increases flight risk
- Benefits are strong retention driver
- Reinforce with them
 - Income protection
 - Building financial security

Young Boomers

- Not generally a serious flight risk
- Dissatisfaction may cause reduced engagement
 - ROAD Warrior
 - Retired On Active Duty
- Reinforce benefits that help with financial issues
 - Defined Benefit Retirement
 - Supplemental Insurance
 - Long Term Care

Older Boomers

- Generally satisfied with job, unlikely to leave
- Major challenge
 - Financially unprepared for retirement
- 62% of employers expect older employees to remain beyond normal retirement
- Provide
 - Financial planning tools
 - Wellness & disease management

Topics

- History & Context
- Assessing your Package
- Benefit Trends
- Cost Containment
- Design Enhancement

Benefit Trends

- Incentives / Penalties for Healthy / Unhealthy Behavior
- Higher Out of Pocket Costs
- Full Coverage for Preventative Care
- Health Coaches / On Site Health Centers
- More Choices to meet Individual Needs
- More Communication / More Tools
- More HSA's, Fewer Plan Options
- Scrutiny of Spousal Dependant Coverage

Incentives / Penalties for Healthy / Unhealthy Behavior

- Financial incentives for healthy behavior
- Full Coverage for Preventative Care
- Company Contributions to HSA for
 - Participation in Health Screening
 - Smoking Cessation
 - Supervised Weight Loss
- Penalties for unhealthy behavior
 - Higher premiums for Smokers

Higher Out of Pocket Costs

- More than 40% of employers indicate plans to raise deductibles, co-payments, and out of pocket maximums.

Full Coverage for Preventative Care

- No Co-Pay Deductible for:
 - Preventative drugs
 - Vaccinations
 - Screenings
 - Flu Shots

Health Coaches / On Site Health Centers

- Access to health coaches / and advocates
 - Individual advise to workers on health care needs
- On site health care beginning to come back

More Choices to meet Individual Needs

- Increased number of voluntary benefits available through employer
 - Auto
 - Homeowners
 - Supplemental Life
 - Long Term Care
 - Vision Discounts
 - Massage Therapy
 - Fitness Club Memberships
 - Tax preparation services

More Communication / More Tools

- On Line Tools
- More than just open enrollment
- More information
 - More tools for managing personal healthcare

More HSA's, Fewer Plan Options

- HSA's continue to gain popularity
 - Driven by more Consumer Driven Plan
- HSA:
 - Employee / Employer Contribution
 - Tax Exempt
 - Funds can "Roll Over"
- Many employers continue to reduce the number of plans available
- Reduced premium may assisting in avoidance of "Cadillac Plan Tax"

Scrutiny of Spousal Dependant Coverage

- Are all the dependants you are covering really eligible?
- Average cost per year for a cooperative \$2,000-\$5,000

Topics

- History & Context
- Assessing your Package
- Benefit Trends
- Cost Containment
- Design Enhancement

Cost Containment

- Take it seriously
- Is this an acceptable statement from your finance folks:
“Sorry, we seem to have lost \$250,000 in the fog of accounting”

Cost Containment

- But this happens all the time, and we don't give it a second thought.

“Sorry, our health plan expenses will increase by another \$250,000 this year,. We're told this is competitive with the overall market”

Cost Containment Strategies

- Consumer Driven Plans
- DB VS 401(k)
- Dependant Eligibility Audits
- Wellness Incentive Programs
- Tiered Drug Programs
- Workforce Structure
- Tiered Contribution

Consumer Driven Plans

- Healthcare Reform has increased popularity
- Higher “Up Front” cost for employees
- Higher Deductibles and Co-Pays
- Offset with Flexible Spending Accounts and Healthcare Spending Accounts
 - May have company match and/or contribution
- Intended to drive employees to better be better “consumers” of health care

Consumer Driven Plans Research

~~CIGNA Insurance Internal Study~~

- Cost Trends
 - Less than half the trend for HMOs and PPOs.
 - First-year Cigna CDHP members were
 - More than 12 percent lower relative to Cigna HMO and PPH
 - 4.4 % CDHP
 - 9.8% traditional-plan members.

Consumer Driven Plans Research

- Out of Pocket Costs
 - Member out-of-pocket costs were similar.
 - Not including the additional cost benefit of lower premiums
 - Typically 10 percent to 20 percent lower for consumer-driven plans, according to Cigna.

Consumer Driven Plans Research

- Use of preventive care increased.
 - First-year member preventive visits increased and second-year member visits were significantly higher than those among traditional-plan members.
 - Recommended care compliance remained constant. Cigna CDHP members continued to receive recommended care at similar compliance rates as traditional-plan members.
 - Medication compliance improved, while costs decreased.
 - Use of maintenance medications that support chronic conditions increased while costs decreased over the period for Cigna CDHP members.

Cost Containment Strategies

- Consumer Driven Plans
- DB VS 401(k)
- Dependant Eligibility Audits
- Wellness Incentive Programs
- Tiered Drug Programs
- Workforce Structure
- Tiered Contribution

DB VS 401(k)

Strategic Issues Facing Employers

- Traditional DB retirement plans present a number of challenges, including:
 - Plans are neither understood nor valued by employees.
 - Plans are passive and so do not prod employees to better prepare for their retirement, nor give them a framework to measure their success.
 - Plans are perceived as more costly and more difficult to budget than DC plans.
 - Recent significant premium increases make drive this home
 - Plans might not align with the overall HR philosophy (e.g., to reward current employees, including younger workers).

DB VS 401(k) Strategic Issues

Yet DB retirement plans can offer advantages in workforce management, including:

- Providing early retirement windows.
- Retiring older employees with dignity.
- Serving as a collective bargaining tool

Alternative No. 1

No DB Plan Design Change, but Communicate Value to Participants

- Increase participant services, including by offering access to information via the web and phone.
 - Provide combined statements showing DB and DC plan information.
 - Provide retirement planning tools that include the DB plan.
 - Provide retirement workshops that answer the question.
 - “What is a defined benefit plan, and why should I care?”

Alternative No. 2

DB Plan Closure

- No participants enter the defined benefit plan after a certain date.
 - Existing participants continue to accrue benefits.
 - New participants have bigger contributions within a defined contribution plan.
- Issues:
 - No winners or losers.
 - No ERISA 204(h) benefits cutback notice.
 - Two-tiered benefits for workforce.
 - Possible nondiscrimination testing issues.
 - Cost control is deferred to the long-term future.
 - FAS 158 financial statement impact is virtually the same as with an active plan.
 - Plan investment policy should be reviewed but is not likely to change—for now.

Alternative No. 3

Partial DB Plan Freeze

- Freeze pension benefits of workers under certain age, or service, or age plus service.
- Provide bigger contributions to workers subject to freeze in the 401(k) plans.
- **Issues:**
 - Benefit cutback for younger employees.
 - ERISA 204(h) notice required for young employees.
 - Complies with the Age Discrimination in Employment Act.
 - Simple—no choices, understandable changes.
 - Somewhat better cost control, still mostly deferred to the long-term future.
 - Two-tiered benefit structure within workforce.
 - FAS 158 financial statement impact is improved. Difference between the accumulated benefit obligation (ABO) and projected benefit obligation (PBO) decreases.
 - Financial statements will show a one-time gain or loss as a result of the curtailment of future benefits for the young employees.
 - Plan investment policy should be reviewed as more of the plan's liability becomes fixed.
 - Changes to investment policy may be desirable.

Alternative No. 4

Full DB Plan Freeze

- Freeze pension benefits of all workers.
- Provide bigger contributions to workers over age 40 in the 401(k) plan.
- Issues:
 - Benefit cutback for all employees.
 - ERISA 204(h) notice for all employees required.
 - Complies with the Age Discrimination in Employment Act.
 - Simple—no choices, understandable changes.
 - FAS 158 financial statements impact is improved; difference between PBO and ABO is eliminated.
 - Financial statements will show a one-time gain or loss as a result of the curtailment of future benefits for all employees.
 - Plan investment policy should be reviewed as all of the plan's liability becomes fixed.
 - Changes to investment policy may be desirable.
 - Better cost control.

Cash-Balance Plan In Last Two Options

- Replacement of the existing, traditional DB pension plan with a DB cash-balance plan.
- Contribute a set amount for each worker but put in nearly the same amount for all employees regardless of age or years on the job.
- Like a traditional pension, the
 - cash-balance plan promises a specific payout at retirement
 - Vested employees have more money in a cash-balance plan than in a regular plan should they decide to leave after just a few years
 - Leave prior to retirement, they can take a lump sum distribution
 - Roll it over into an individual retirement account (IRA) or another retirement plan.

Alternative No. 5

Pension Choice: Traditional DB Plan or New Benefits

- Give current employees a choice between “traditional” formula and new benefits—often a combination of a cash-balance plan formula and richer contribution within 401(k) plan.
- New participants go straight to new plan.
- **Issues:**
 - Complies with the Age Discrimination in Employment Act.
 - Intensive communications required.
 - Long-term fiduciary liability for participants’ choices.
 - What are reasonable assumptions?
 - Cost control is deferred to the long-term future.
 - ERISA 204(h) benefit cutback notice must be included within plan communication materials.
 - Financial statement impact is uncertain until elections are made.
 - One-time gains or losses are reflected within income statement in the fiscal years when participant choices are made.
 - Plan investment policy should be reviewed as the nature and term of the plan’s liability will change.
 - Changes to investment policy may be desirable.

Alternative No. 6

Change DB/DC Balance; Convert Traditional DB Plan to Cash-Balance Plan

- Accomplished by conversion to pure cash-balance plan with extended traditional benefit for grandfathered group and bigger matching contributions in 401(k) plan.
- Design strategy of the 1980s and '90s, resurgence with passage of the Pension Protection Act.
- Issues:
 - Better cost control, usually no reduction in overall cost.
 - Favors short-term, young employees.
 - How long should the wear-away be?
 - FAS 158 Financial Statement impact is likely improved; difference in ABO and PBO is reduced.
 - Income statement will show a one-time gain or loss as a result of the curtailment of future benefits for employees.
 - Plan investment policy should be reviewed as the nature and term of the plan's liability will change.
 - Changes to investment policy may be desirable.

Cost Containment Strategies

- Consumer Driven Plans
- DB VS 401(k)
- Dependant Eligibility Audits
- Wellness Incentive Programs
- Tiered Drug Programs
- Workforce Structure
- Tiered Contribution

Dependant Eligibility Audits

- Are you as vigilant as you should be in verifying eligibility for dependant coverage?
- Must now offer dependant coverage until age 26
 - Only if they are not covered elsewhere.
- Are they really married?

Cost Containment Strategies

- Consumer Driven Plans
- DB VS 401(k)
- Dependant Eligibility Audits
- Wellness Incentive Programs
- Tiered Drug Programs
- Workforce Structure
- Tiered Contribution

Wellness Incentive Programs

- Comprehensive wellness programs
 - More than a few books and videos
- Cash and Non-Monetary Incentives
 - Smoking Cessation
 - Weight Loss
 - Exercise Programs
 - Reduced absenteeism

Cost Containment Strategies

- Consumer Driven Plans
- DB VS 401(k)
- Dependant Eligibility Audits
- Wellness Incentive Programs
- Tiered Drug Programs
- Workforce Structure
- Tiered Contribution

Tiered Drug Programs

- Level 1 Medications
 - Used to preserve life or major body system
 - Cardiovascular, Psychiatric, Respiratory, Musculoskeletal, Endocrine, Neurological
 - Lower Co-Pay, Higher Reimbursement
- Level 2 Medications
 - Not required to preserve life
 - Acne treatment, Sleep aids, Anti-fungal,
 - Higher Co-Pay, Lower Reimbursement

Cost Containment Strategies

- Consumer Driven Plans
- DB VS 401(k)
- Dependant Eligibility Audits
- Wellness Incentive Programs
- Tiered Drug Programs
- Workforce Structure
- Tiered Contribution

Workforce Structure

- Do all of your Jobs really require full time employees?
- Leverage your older workings planning on retirement by offering flexible work arrangements
- Many adverse to part time employees
 - Less productive
 - Less Loyal
 - No “Skin in the Game”

Workforce Structure - Research

- Research has shown the opposite
- Study done by Dr. William H. Newbolt
- Studied the entire workforce of UPS
- Found Part-Time Employees
 - More Productive
 - More Loyal to Employer

Workforce Structure - Economics

- Job Sharing by Two Part-Time Employees
 - May result in more productivity
 - Greatly reduced benefit cost
 - Similar base salary cost
- Target
 - Your own retiree's with valuable skill sets
 - Individuals who don't need or desire your benefits package

Workforce Structure - Barriers

- Common Cooperative Practice
 - Pay Part Time Employees significantly lower rates
 - All PT make \$10 an hour very common
- Prevailing “Other” Industry Practice
 - Part Time Paid Higher Hourly Rates
 - Compensate for lack of benefits
 - Attract higher quality employees

Cost Containment Strategies

- Consumer Driven Plans
- DB VS 401(k)
- Dependant Eligibility Audits
- Wellness Incentive Programs
- Tiered Drug Programs
- Workforce Structure
- Tiered Contribution

Health care premiums as a percentage of base pay

- Employees paying for a than in the past,
 - concern about health care affordability
 - especially for lower-paid employees.
- Looking more seriously at cost sharing strategies based on pay
 - Health care premiums as a percentage of base pay,
 - Higher salaried employees paying more
 - Minority of employers are using or considering these approaches,
 - Expected to become popular over the next several years.
- Supported by the evolution of benefit administration and payroll systems that can more easily manage the complexities of this approach.

Topics

- History & Context
- Assessing your Package
- Benefit Trends
- Cost Containment
- Design Enhancement

Most Benefit Packages Like “Fixed Menu” Dinner

- All employees get all benefits
- May not be sufficient for some employees
- May be more than needed for some



Cafeteria Plan

- Employees choose only what they want /need.



Cafeteria Plan

- Company does not pay for unwanted benefits.



Structuring a Cafeteria Plan

- Determine Core Benefits
- Determine Funding
 - Employees given “Benefit Dollars”
 - Spend on
 - Premiums
 - Time Off
 - Cash

Implementing

- Develop Funding Limits
- Determine Structure
- Secure Vendors
- Communicate to Employees
- Implement
- Fine-Tune

Questions?

Michael D. Frizzell

5550 Overlook Circle

Winston-Salem, NC 27105

336.406.4075

Michael@MDFHRConsulting.com

www.MDFHRConsulting.com