

Providing Employee Benefits

What Do I Need to Know?

After reading this chapter, you should be able to:

- L01 Discuss the importance of benefits as a part of employee compensation.
- L02 Summarize the types of employee benefits required by law.
- L03 Describe the most common forms of paid leave.
- L04 Identify the kinds of insurance benefits offered by employers.
- L05 Define the types of retirement plans offered by employers.
- L06 Describe how organizations use other benefits to match employees' wants and needs.
- L07 Explain how to choose the contents of an employee benefits package.
- L08 Summarize the regulations affecting how employers design and administer benefits programs.
- L09 Discuss the importance of effectively communicating the nature and value of benefits to employees.

Introduction



Patagonia has a long and strong reputation for caring about the environment and helping customers enjoy nature while using its top-quality recreational gear and clothing. The Ventura, California-based company carries out its mission to build the best products while reducing its environmental impact through dedicated people who deliver results. Most are drawn to Patagonia by its mission. Pay rates are, at best, only slightly above the market rate, but generous benefits help to keep talented employees on board. All Patagonia employees, full- and part-time, receive a full health insurance package, and the headquarters boasts an on-site day care center. In addition, the company will pay employees for a sabbatical of up to two months that is spent working for environmental groups.¹

Like Patagonia's employees, employees at almost every organization receive more than dollars and cents in exchange for their efforts. They also receive a package of **employee benefits**—compensation in forms other than cash. Besides the use of corporate fitness centers, examples include paid vaca-

tion time, employer-paid health insurance, and pension plans, among a wide range of possibilities.

Employee Benefits

Compensation in forms other than cash.

This chapter describes the contents of an employee benefits package and the way organizations administer employee benefits. We begin by discussing the important role of benefits as a part of employee compensation. The following sections define major types of employee benefits: benefits required by law, paid leave, insurance policies, retirement plans, and other benefits. We then discuss how to choose which of these alternatives to include in an employee benefits package so that it contributes to meeting the organization's goals. The next section summarizes the regulations affecting how employers design and administer benefits programs. Finally, we explain why and how organizations should effectively communicate with employees about their benefits.

L01 Discuss the importance of benefits as a part of employee compensation.

The Role of Employee Benefits

As a part of the total compensation paid to employees, benefits serve functions similar to pay. Benefits contribute to attracting, retaining, and motivating employees. The variety of possible benefits also helps employers tailor their compensation to the kinds of employees they need. Different employees look for different types of benefits. Employers need to examine their benefits package regularly to see whether they meet the needs of today. At the same time, benefits packages are more complex than pay structures, so benefits are harder for employees to understand and appreciate. Even if employers spend large sums on benefits, if employees do not understand how to use them or why they are valuable, the cost of the benefits will be largely wasted.² Employers need to communicate effectively so that the benefits succeed in motivating employees. For an example of a company that gets its benefits program right, see the “Best Practices” box.

Employees have come to expect that benefits will help them maintain economic security. Social Security contributions, pensions, and retirement savings plans help employees prepare for their retirement. Insurance plans help to protect employees from unexpected costs such as hospital bills. This important role of benefits is one reason that benefits are subject to government regulation. Some benefits, such as Social Security, are required by law. Other regulations establish requirements that benefits must meet to obtain the most favorable tax treatment. Later in the chapter, we will describe some of the most significant regulations affecting benefits.

Even though many kinds of benefits are not required by law, they have become so common that today's employees expect them. Many employers find that attracting qualified workers requires them to provide medical and retirement benefits of some sort. A large employer without such benefits would be highly unusual and would have difficulty competing in the labor market. Still, the nature of the benefits package changes over time, as we will discuss at various points throughout the chapter.

Like other forms of compensation, benefits impose significant costs. On average, out of every dollar spent on compensation, 30 cents or more go to benefits. As Figure 13.1 shows, this share has grown over the past decades. These numbers indicate that an organization managing its labor costs must pay careful attention to the cost of its employee benefits.

Why do organizations pay a growing share of compensation in the form of benefits? It would be simpler to pay all compensation in cash and let employees buy their own insurance and contribute to their own savings plans. That arrangement would also give employees greater control over what their compensation buys. However, several forces have made benefits a significant part of compensation packages. One is that laws require employers to provide certain benefits, such as contributions to Social Security and unemployment insurance. Also, tax laws can make benefits favorable to employees. For example, employees do not pay income taxes on most benefits they

BENEFITS HELP MAKE SAS EMPLOYEES HAPPY

SAS, the largest privately owned software company, has made it onto *Fortune* magazine's list of Best Companies to Work For every year that list has been compiled. One of the notable reasons is a generous set of employee benefits. Employees can unwind with a swim, haircut, workout, or massage at the recreation and fitness center on the company's campus near Raleigh, North Carolina. A subsidized day care center and summer camp help employees ensure that their children are in good hands. Employees with errands to run can take care of them swiftly with on-site dry cleaning, car detailing, tax preparation, and a book exchange. The subsidized cafeteria offers takeout for any employee who wants to take dinner home for the family. The company has set up a lactation room where nursing mothers can settle into a recliner and listen to soft music while feeding their babies.

One of the most unusual benefits is one of the most generous: an on-site health care center for routine medical needs. Employees and their families can make appointments to see a doctor,

nurse practitioner, nurse, physical therapist, or psychologist. There's no charge to the employees (except for a missed appointment, which costs \$10), but the company says the center saves money because employees don't need to take as much time off as they would to visit doctors elsewhere, they get routine needs met before they become serious problems, and the company runs the center efficiently.

Generous benefits aren't a form of charity for employees, but rather part of a strategy to hire and keep the best people without paying top dollar in salaries. Taking care of people is all about the numbers for CEO Jim Goodnight, who has a doctorate degree in statistics and as co-founder owns two-thirds of the company's stock. Compared with 22 percent employee turnover in the industry, SAS reports turnover of just 2 percent. The average employee has been at SAS for 10 years. Of the company's 4,200 employees, 300 have worked there for at least 25 years. And for every year SAS has been in business, Goodnight says, it has turned a profit.

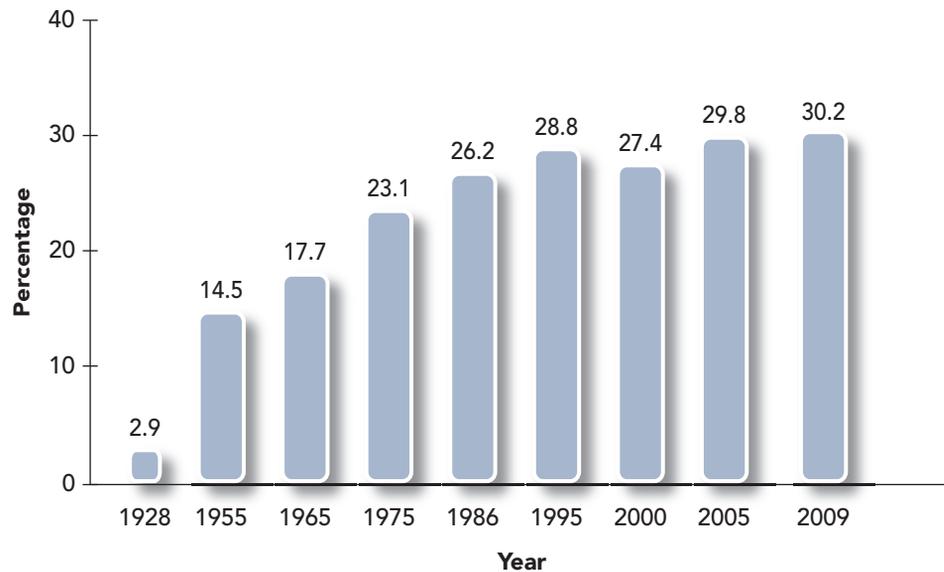
Offering perks is just one way SAS treats employees well. Employees have flexibility in setting their schedules, and they typically work just 35 hours a week. In fact, the worker-friendly policies don't make SAS into some kind of country club. SAS keeps its workers comfortable so they can work creatively, without distractions. In Goodnight's experience, exhausted, stressed-out workers don't produce great work. Happy employees would agree. Bev Brown, who works in external communications, told a reporter, "People do work hard here, because they're motivated to take care of a company that takes care of them."

Sources: David A. Kaplan, "SAS: A New No. 1 Best Employer," *Fortune*, January 22, 2010, <http://money.cnn.com>; Leah Friedman, "Nursing Mothers Get a Break, Starting Now," *News & Observer (Raleigh, N.C.)*, April 28, 2010, Business & Company Resource Center, <http://galenet.galegroup.com>; and Stefan Stern, "The Real Value of Managing Information and People," *Financial Times*, February 1, 2010, Business & Company Resource Center, <http://galenet.galegroup.com>.

receive, but they pay income taxes on cash compensation. Therefore, an employee who receives a \$1,000 raise "takes home" less than the full \$1,000, but an employee who receives an additional \$1,000 worth of benefits receives the full benefits. Another cost advantage of paying benefits is that employers, especially large ones, often can get a better deal on insurance or other programs than employees can obtain on their own. Finally, some employers assemble creative benefits packages that set them apart in the competition for talent. For example, International Business Machines and Texas Instruments offer an online course that helps employees cope with the demands of being a caregiver for an ill family member, while Pitney Bowes and Marriott International offer insurance that pays the full cost of drugs for chronic conditions like asthma and high blood pressure.³

Figure 13.1

Benefits as a Percentage of Total Compensation



SOURCE: Bureau of Labor Statistics, "Employer Costs for Employee Compensation," <http://data.bls.gov>, accessed April 28, 2010.

L02 Summarize the types of employee benefits required by law.

Benefits Required by Law

The federal and state governments require various forms of social insurance to protect workers from the financial hardships of being out of work. In general, Social Security provides support for retired workers, unemployment insurance assists laid-off workers, and workers' compensation insurance provides benefits and services to workers injured on the job. Employers must also provide unpaid leave for certain family and medical needs. Because these benefits are required by law, employers cannot gain an advantage in the labor market by offering them, nor can they design the nature of these benefits. Rather, the emphasis must be on complying with the details of the law. Table 13.1 summarizes legally required benefits.

Social Security

In 1935 the federal Social Security Act established old-age insurance and unemployment insurance. Congress later amended the act to add survivor's insurance (1939), disability insurance (1956), hospital insurance (Medicare Part A, 1965), and

Table 13.1

Benefits Required by Law

BENEFIT	EMPLOYER REQUIREMENT
Social Security	Flat payroll tax on employees and employers
Unemployment insurance	Payroll tax on employers that depends on state requirements and experience rating
Workers' compensation insurance	Provide coverage according to state requirements. Premiums depend on experience rating
Family and medical leave	Up to 12 weeks of unpaid leave for childbirth, adoption, or serious illness
Health care	Provisions of 2010 law phased in through 2014

supplementary medical insurance (Medicare Part B, 1965) for the elderly. Together, the law and its amendments created what is now the Old Age, Survivors, Disability, and Health Insurance (OASDHI) program, informally known as **Social Security**. This program covers over 90 percent of U.S. employees. The main exceptions are railroad and federal, state, and local government employees, who often have their own plans.

Workers who meet eligibility requirements receive the retirement benefits according to their age and earnings history. If they elect to begin receiving benefits at full retirement age, they can receive full benefits, or if they elect to begin receiving benefits at age 62, they receive benefits at a permanently reduced level. The full retirement age rises with birth year: a person born in 1940 reaches full retirement age at 65 years and 6 months, and a person born in 1960 or later reaches full retirement age at 67. The benefit amount rises with the person's past earnings, but the level goes up very little after a certain level. In 2008, the maximum monthly benefit was \$2,185. The government increases the payments each year according to the growth in the consumer price index. Also, spouses of covered earners receive benefits, even if they have no covered earnings. They receive either the benefit associated with their own earnings or one-half of the amount received by the covered earner, whichever is greater.

Benefits may be reduced if the worker is still earning wages above a maximum, called the *exempt amount*. In 2009, the exempt amount was \$14,160 for beneficiaries under the full retirement age. A beneficiary in that age range who earns more than the exempt amount sees a reduction in his or her benefit. The amount of the reduction is \$1 for every \$2 the person earns above the exempt amount. For example a 63-year-old who earned \$16,160 in 2009 would have earned \$2,000 above the exempt amount, so the person's Social Security benefits would be reduced by \$1,000. During the year a worker reaches full retirement age, the maximum untaxed earnings are \$37,680 (in 2009), and benefits are reduced \$1 for every \$3 in earnings. Beginning in the month they reach full retirement age, workers face no reduction in benefits for earning above the exempt amount. For workers below that age, the penalty increases the incentive to retire or at least reduce the number of hours worked. Adding to this incentive, Social Security benefits are free from federal income taxes and free from state taxes in about half the states.

Employers and employees share the cost of Social Security through a payroll tax. The percentage is set by law and has changed from time to time. In 2009, employers and employees each paid a tax of 7.65 percent on the first \$106,800 of the employee's earnings, with 6.2 percent of earnings going to OASDI and 1.45 percent going to Medicare (Part A). For earnings above \$106,800, only the 1.45 percent for Medicare is assessed.

Unemployment Insurance

Along with OASDHI, the Social Security Act of 1935 established a program of **unemployment insurance**. This program has four objectives related to minimizing the hardships of unemployment. It provides payments to offset lost income during involuntary unemployment, and it helps unemployed workers find new jobs. The payment of unemployment insurance taxes gives employers an incentive to stabilize



Kathleen Casey-Kirschling was the first of the baby boomers to begin receiving Social Security benefits. The widening gap between those contributing to the system and those receiving benefits is a major concern.

Social Security

The federal Old Age, Survivors, Disability, and Health Insurance (OASDHI) program, which combines old age (retirement) insurance, survivor's insurance, disability insurance, hospital insurance (Medicare Part A), and supplementary medical insurance (Medicare Part B) for the elderly.

Unemployment Insurance

A federally mandated program to minimize the hardships of unemployment through payments to unemployed workers, help in finding new jobs, and incentives to stabilize employment.

employment. And providing workers with income during short-term layoffs preserves investments in worker skills because workers can afford to wait to return to their employer, rather than start over with another organization. Technically, the federal government left it to each state's discretion to establish an unemployment insurance program. At the same time, the Social Security Act created a tax incentive structure that quickly led every state to establish the program.

Most of the funding for unemployment insurance comes from federal and state taxes on employers. The federal tax rate is currently 0.8 percent of the first \$7,000 of each employee's wages. The state tax rate varies. For a new employer, rates range from 1 percent to 6 percent, and the taxable wage base ranges from \$7,000 to \$32,200, so the amount paid depends a great deal on where the company is located.⁴ Also, some states charge new employers whatever rate is the average for their industry, so the amount of tax paid in those states also depends on the type of business. In the severe recession of 2008–2009, layoffs were so widespread that unemployment insurance funds were drained and many states dramatically hiked premiums for unemployment insurance. In Hawaii, for example, the rate jumped from \$90 per employee to an average around \$1,000 per employee, with some employers paying as much as \$2,040.⁵

No state imposes the same tax rate on every employer in the state. The size of the unemployment insurance tax imposed on each employer depends on the employer's **experience rating**—the number of employees the company laid off in the past and the cost of providing them with unemployment benefits. Employers with a history of laying off a large share of their workforces pay higher taxes than those with few layoffs. In some states, an employer with very few layoffs may pay no state tax. In contrast, an employer with a poor experience rating could pay a tax as high as 5.4 to 12.27 percent, depending on the state. The use of experience ratings gives employers some control over the cost of unemployment insurance. Careful human resource planning can minimize layoffs and keep their experience rating favorable.

To receive benefits, workers must meet four conditions:

1. They meet requirements demonstrating they had been employed (often 52 weeks or four quarters of work at a minimum level of pay).
2. They are available for work.
3. They are actively seeking work. This requirement includes registering at the local unemployment office.
4. They were not discharged for cause (such as willful misconduct), did not quit voluntarily, and are not out of work because of a labor dispute (such as a union member on strike).

Workers who meet these conditions receive benefits at the level set by the state—typically about half the person's previous earnings—for a period of 26 weeks. States with a sustained unemployment rate above a particular threshold or significantly above recent levels also offer extended benefits for up to 13 weeks. Sometimes Congress funds emergency extended benefits. All states have minimum and maximum weekly benefit levels.

Experience Rating

The number of employees a company has laid off in the past and the cost of providing them with unemployment benefits.

Workers' Compensation

State programs that provide benefits to workers who suffer work-related injuries or illnesses, or to their survivors.

Workers' Compensation

Decades ago, workers who suffered work-related injury or illness had to bear the cost unless they won a lawsuit against their employer. Those who sued often lost the case because of the defenses available to employers. Today, the states have passed **workers' compensation** laws, which help workers with the expenses resulting from

job-related accidents and illnesses.⁶ These laws operate under a principle of *no-fault liability*, meaning that an employee does not need to show that the employer was grossly negligent in order to receive compensation, and the employer is protected from lawsuits. The employer loses this protection if it intentionally contributes to a dangerous workplace. Employees are not eligible if their injuries are self-inflicted or if they result from intoxication or “willful disregard of safety rules.”⁷

About 9 out of 10 U.S. workers are covered by state workers’ compensation laws, with the level of coverage varying from state to state. The benefits fall into four major categories: (1) disability income, (2) medical care, (3) death benefits, and (4) rehabilitative services. The amount of income varies from state to state but is typically two-thirds of the worker’s earnings before the disability. The benefits are tax free.

The states differ in terms of how they fund workers’ compensation insurance. Some states have a single state fund. Most states allow employers to purchase coverage from private insurance companies. Most also permit self-funding by employers. The cost of the workers’ compensation insurance depends on the kinds of occupations involved, the state where the company is located, and the employer’s experience rating. Premiums for low-risk occupations may be less than 1 percent of payroll. For some of the most hazardous occupations, the cost may be as high as 100 percent of payroll. Costs also vary from state to state, so that one state’s program requires higher premiums than another state’s program. As with unemployment insurance, unfavorable experience ratings lead to higher premiums. Organizations can minimize the cost of this benefit by keeping workplaces safe and making employees and their managers conscious of safety issues, as discussed in Chapter 3.

Unpaid Family and Medical Leave

In the United States, unpaid leave is required by law for certain family needs. Specifically, the **Family and Medical Leave Act (FMLA)** of 1993 requires organizations with 50 or more employees within a 75-mile radius to provide as much as 12 weeks of unpaid leave after childbirth or adoption; to care for a seriously ill child, spouse, or parent, for an employee’s own serious illness; or to take care of urgent needs that arise when a spouse, child, or parent in the National Guard or Reserve is called to active duty. In addition, if a family member (child, spouse, parent, or next of kin) is injured while serving on active military duty, the employee may take up to 26 weeks of unpaid leave under FMLA. Employers must also guarantee these employees the same or a comparable job when they return to work. The law does not cover employees who have less than one year of service, work fewer than 25 hours per week, or are among the organization’s 10 percent highest paid. The 12 weeks of unpaid leave amount to a smaller benefit than is typical of Japan and most countries in Western Europe. Japan and West European nations typically require paid family leave.

Experience with the Family and Medical Leave Act suggests that a majority of those opting for this benefit fail to take the full 12 weeks. In about one out of four situations, employees take their leave intermittently, over periods of days or even hours, creating a significant record-keeping task.⁸ Other employees, especially female executives, are simply keeping parental leaves under FMLA to a minimum, less than the available 12 weeks. Many are eager to return to their careers, and others fear that staying away for three months would damage their career opportunities.⁹ Of course, another reason for not taking the full 12 weeks is that not everyone can afford three months without pay, especially when responsible for the expenses that accompany childbirth, adoption, or serious illness.

Family and Medical Leave Act (FMLA)

Federal law requiring organizations with 50 or more employees to provide up to 12 weeks of unpaid leave after childbirth or adoption; to care for a seriously ill family member, or for an employee’s own serious illness; or to take care of urgent needs that arise when a spouse, child, or parent in the National Guard or Reserve is called to active duty.

When employees experience pregnancy and childbirth, employers must also comply with the Pregnancy Discrimination Act, described in Chapter 3. If an employee is temporarily unable to perform her job due to pregnancy, the employer must treat her in the same way as any other temporarily disabled employee. For example, the employer may provide modified tasks, alternative assignments, disability leave, or leave without pay.

Health Care Benefits

Patient Protection and Affordable Care Act
Health care reform law passed in 2010 that includes incentives and penalties for employers providing health insurance as a benefit.

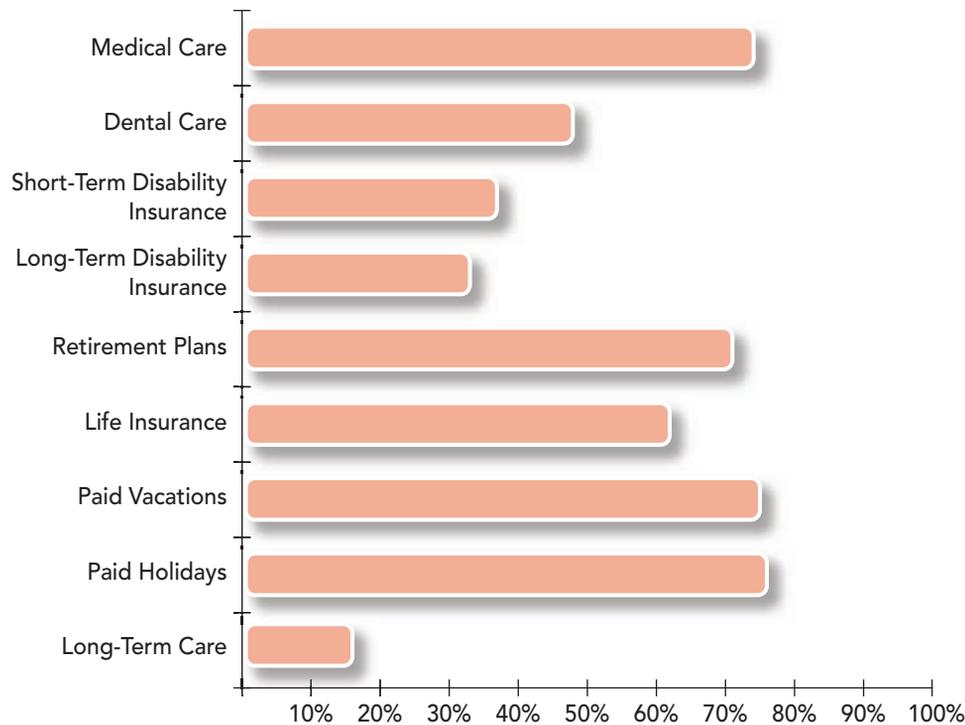
In 2010, Congress passed the **Patient Protection and Affordable Care Act**, a complex package of changes in how health care is to be paid for, including requirements for insurance companies, incentives and penalties for employers providing health insurance as a benefit, expansion of public funding including Medicaid and community health centers, and creation of health insurance exchanges as an option for the sale of health insurance. Provisions of the law are being phased in between 2010 and 2014.

The first provisions of the law that take effect mainly involve requirements for insurance companies—for example, that they must cover children with pre-existing conditions and dependent children through age 26 and may not impose lifetime limits on coverage or end coverage for people when they get sick. Small-business employers (up to 25 employees) are affected by one change that takes effect in 2010: a tax credit equal to half the cost of providing health insurance benefits. In 2014, automatic enrollment in health insurance is required at companies with over 200 employees. Companies with more than 50 employees that do not provide health insurance will have to pay a penalty. Because the law is complex and details of implementation are still being worked out, HR departments must educate themselves about the requirements and communicate with employees, many of whom may be worried about how the law will affect them. A useful starting point is the government's health reform Web site, www.healthreform.gov.

Optional Benefits Programs

Other types of benefits are optional. These include various kinds of insurance, retirement plans, and paid leave. Figure 13.2 shows the percentage of full-time workers having access to the most common employee benefits. (Part-time workers often have access to and receive fewer benefits.) The most widely offered benefits are paid leave for vacations and holidays, life and medical insurance, and retirement plans. In general, benefits packages at smaller companies tend to be more limited than at larger companies.

Benefits such as health insurance often extend to employees' dependents. Traditionally, these benefits have covered employees, their spouses, and dependent children. Today, many employers also cover *domestic partners*, defined either by local law or by the companies themselves. Typically, a domestic partner is an adult nonrelative who lives with the employee in a relationship defined as permanent and financially interdependent. Some local governments provide for registration of domestic partners. Organizations offering coverage to domestic partners generally require that the partners sign a document stating they meet the requirements for a domestic partnership. Benefits provided to domestic partners do not have the same tax advantages as benefits provided to spouses. The partner's benefits are taxed as wages of the employee receiving the benefits.

**Figure 13.2**

Percentage of Full-Time Workers with Access to Selected Benefit Programs

SOURCE: Bureau of Labor Statistics, "Employee Benefits in the United States, March 2009," news release, July 28, 2009, www.bls.gov; and Bureau of Labor Statistics, "Employee Benefits Survey," <http://www.bls.gov/ncs/ebs/benefits/2009/>, accessed April 30, 2010.

Paid Leave

The major categories of paid leave are vacations, holidays, and sick leave. Employers also should establish policies for other situations that may require time off. Organizations often provide for paid leave for jury duty, funerals of family members, and military duty. Some organizations provide for other paid leave, such as time off to vote or to donate blood. Establishing policies communicates the organization's values, clarifies what employees can expect, and prevents situations in which unequal treatment leads to claims of unfairness.

At first blush, paid vacation, holidays, sick leave, and other paid leave may not seem to make economic sense. The employer pays the employee for time spent not working, so the employer receives nothing in return for the pay. Some employers may see little direct advantage. This may be the reason that Western European countries require a minimum number of paid vacation days, with new employees receiving 30 days off in many countries. The United States, in contrast, has no such legal requirement. It is up to U.S. employers to decide whether paid leave has a payoff in recruiting and retaining employees. At U.S. companies, paid vacation is typically two weeks or less a year for the first few years (see the "Did You Know?" box). To receive as much vacation as European employees, U.S. workers must typically stay with an employer for more than 20 years.¹⁰

Paid holidays are time off on specified days in addition to vacation time. In Western Europe and the United States, employees typically have about 10 paid holidays each year, regardless of length of service. The most common paid holidays in the United States are New Year's Day, Memorial Day, Independence Day, Labor Day, Thanksgiving Day, and Christmas Day.

L03 Describe the most common forms of paid leave.

Did You Know?

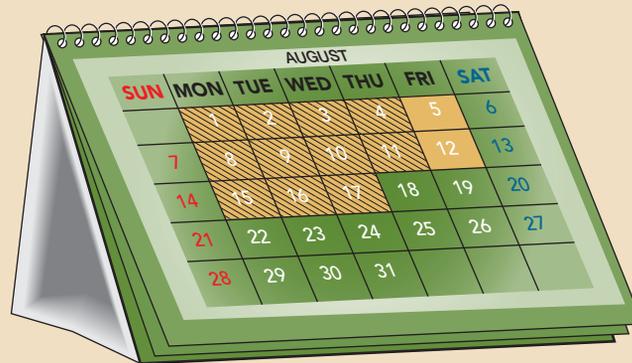
U.S. and Japanese Workers Take Short Vacations

On average, workers in the United States reported receiving 13 vacation days but using only 11 of them. Japanese workers were

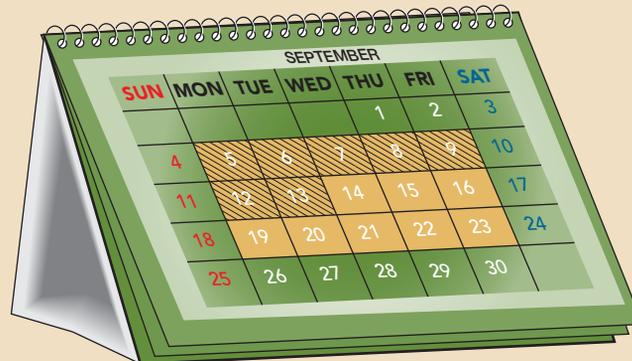
even less willing to take time off: they reported receiving 15 days of vacation but taking only 7 of those days.

Source: Kenji Hall, "Can Vacation Reform Help Japan's Economy?" *BusinessWeek*, April 22, 2009, www.businessweek.com.

U.S. Vacations



Japanese Vacations



Sick leave programs pay employees for days not worked because of illness. The amount of sick leave is often based on length of service, so that it accumulates over time—for example, one day added to sick leave for each month of service. Employers must decide how many sick days to grant and whether to let them continue accumulating year after year. If sick days accumulate without limit, employees can “save” them in case of disability. If an employee becomes disabled, the employee can use up the accumulated sick days, receiving full pay rather than smaller payments from disability insurance, discussed later. Some employers let sick days accumulate for only a year, and unused sick days “disappear” at year-end. This may provide an unintended incentive to use up sick days. Some healthy employees may call in sick near the end of the year so that they can obtain the benefit of the paid leave before it disappears.

Employers may counter this tendency by paying employees for some or all of their unused sick days at year-end or when the employees retire or resign.

An organization's policies for time off may include other forms of paid and unpaid leave. For a workforce that values flexibility, the organization may offer paid *personal days*, days off that employees may schedule according to their personal needs, with the supervisor's approval. Typically, organizations offer a few personal days in addition to sick leave. *Floating holidays* are paid holidays that vary from year to year. The organization may schedule floating holidays so that they extend a Tuesday or Thursday holiday into a long weekend. Organizations may also give employees discretion over the scheduling of floating holidays.

The most flexible approach to time off is to grant each employee a bank of *paid time off*, in which the employer pools personal days, sick days, and vacation days for employees to use as the need or desire arises. This flexibility is especially attractive to younger workers, who tend to rate work/life balance as one of the most important sources of job satisfaction. The flexibility also fits with the U.S. trend toward more frequent but shorter vacations. With these advantages, paid time off has become more widespread than traditional policies separating types of leave, according to a recent survey.¹¹

Employers should also establish policies for leaves without pay—for example, leaves of absence to pursue nonwork goals or to meet family needs. Unpaid leave is an employee benefit because the employee usually retains seniority and benefits during the leave.

Group Insurance

As we noted earlier, rates for group insurance are typically lower than for individual policies. Also, insurance benefits are not subject to income tax, as wages and salaries are. When employees receive insurance as a benefit, rather than higher pay so they can buy their own insurance, employees can get more for their money. Because of this, most employees value group insurance. The most common types of insurance offered as employee benefits are medical, life, and disability insurance. As noted in the earlier discussion of benefits required under law, the U.S. government will require medium-sized and large businesses to offer health insurance or pay a penalty beginning in 2014; but until then, medical insurance is an optional benefit, and businesses continue to have many choices in the types of coverage they offer.

Medical Insurance

For the average person, the most important benefit by far is medical insurance.¹² As Figure 13.2 shows, almost three-quarters of full-time employees receive medical benefits. The policies typically cover three basic types of medical expenses: hospital expenses, surgical expenses, and visits to physicians. Some employers offer additional coverage, such as dental care, vision care, birthing centers, and prescription drug programs. Under the Mental Health Parity Act of 1996, health insurance plans offered to employees must have the same maximum dollar benefits for covered mental illness as for other medical and surgical benefits. Some states have stricter requirements than the federal law. However, insurance plans can and do impose other restrictions on mental health care, such as limits on the number of days of hospitalization, and some employers avoid the restrictions by offering insurance without any mental health coverage.¹³



Paid time off is a way for employees to enjoy time with their families and to refresh their bodies and spirits. Is paid time off an important criteria for you when accepting a position?

LO4 Identify the kinds of insurance benefits offered by employers.

Consolidated Omnibus Budget Reconciliation Act (COBRA)

Federal law that requires employers to permit employees or their dependents to extend their health insurance coverage at group rates for up to 36 months following a qualifying event, such as a layoff, reduction in hours, or the employee's death.

Employers that offer medical insurance must meet the requirements of the **Consolidated Omnibus Budget Reconciliation Act (COBRA)** of 1985. This federal law requires employers to permit employees to extend their health insurance coverage at group rates for up to 36 months following a “qualifying event.” Qualifying events include termination (except for gross misconduct), a reduction in hours that leads to loss of health insurance, and the employee's death (in which case the surviving spouse or dependent child would extend the coverage). To extend the coverage, the employee or the surviving spouse or dependent must pay for the insurance, but the payments are at the group rate. These employees and their families must have access to the same services as those who did not lose their health insurance.

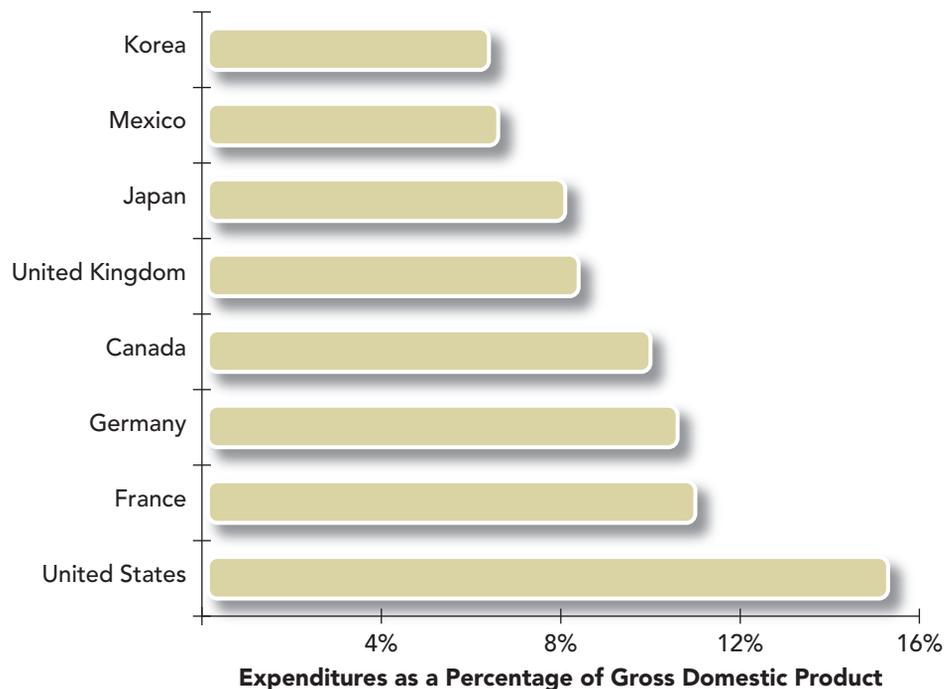
As we will discuss later in the chapter, health insurance is a significant and fast-growing share of benefits costs at U.S. organizations, far outpacing the inflation rate and even the rise in the overall cost of health care in the United States.¹⁴ Figure 13.3 shows that the United States spends much more of its total wealth on health care than other countries do. Most Western European countries have nationalized health systems, but the majority of Americans with coverage for health care expenses get it through their own or a family member's employer. As a result, a growing number of employees whose employers cannot afford this benefit are left without insurance to cover health care expenses.

Employers have looked for ways to control the cost of health care coverage while keeping this valuable benefit. They have used variations of managed care, employee-driven savings, and promotion of employee wellness:

- With *managed care*, the insurer plays a role in decisions about health care, aimed at avoiding unnecessary procedures. The insurer may conduct claims review, studying

Figure 13.3

Health Care Costs in Various Countries



SOURCE: Organization for Economic Cooperation and Development, “Public Finance: Public Expenditure,” *OECD Factbook 2009*, pp. 220–21, accessed at www.oecd.org.

claims to determine whether procedures are effective for the type of illness or injury. Patients may be required to obtain approval before hospital admissions, and the insurer may require alternatives to hospital stays—for example, outpatient surgery or home health care.

- A **health maintenance organization (HMO)** is a health care plan that requires patients to receive their medical care from the HMO's health care professionals, who are often paid a flat salary, and provides all services on a prepaid basis. In other words, the premiums paid for the HMO cover all the patient's visits and procedures, without an additional payment from the patient. By paying physicians a salary, rather than a fee for each service, the HMO hopes to remove any incentive to provide more services than the patients really need. HMO coverage tends to cost less than traditional health insurance. The downside is that employees sometimes complain cost-control incentives work so well that they are denied access to services they actually need.
- A **preferred provider organization (PPO)** is a health care plan that contracts with health care professionals to provide services at a reduced fee. Often, the PPO does not require employees to use providers in the network, but it pays a larger share of the cost of services from PPO providers. For example, the employee might pay 10 percent of the cost of a test by an in-network provider and 20 percent if the employee goes out of the PPO network. PPOs have quickly grown to become the most widely used health plan among U.S. employers. Recent data found that among workers with health insurance, about two-thirds were enrolled in a PPO; most of the remainder—almost one-fourth—were in an HMO.¹⁵
- With a **flexible spending account**, employees set aside a portion of pretax earnings to pay for eligible expenses. In particular, a *medical savings account* lets employees use their pretax savings to pay for qualified health care expenses (for example, payment of premiums). To avoid taxation, the money in the account must meet IRS requirements. Contributions to this account may not exceed \$5,000 per year and must be designated in advance. The money in the account may be spent on health care expenses of the employee and employee's dependents during the plan year. At the end of the year, any remaining funds in the account revert to the employer. The major advantage of flexible spending accounts is that the money in the account is not taxed, so employees will have more take-home pay. But if they do not use all the money in the flexible spending account, they lose the amount they do not spend. Therefore, employees are most likely to benefit from a flexible spending account if they have predictable health care expenses, such as insurance premiums.
- *Consumer-driven health plans* (CDHPs) are intended to provide health coverage in a way that gets employees involved as consumers making decisions to lower costs. A CDHP typically brings together three elements: insurance with a high deductible, a medical savings account in which the employer contributes to employee-controlled accounts for paying expenses below the deductible, and health education aimed at helping employees improve their health and thus lower their need for health care. According to surveys, employees are at least initially less satisfied with CDHPs than with traditional health care plans. Employers should allow at least six months between introducing the plan and completing the enrollment process, so they can educate employees about how a CDHP can empower them in making decisions about their health and health care. Despite this challenge, the potential savings has led companies such as Humana and Black & Decker to offer

Health Maintenance Organization (HMO)

A health care plan that requires patients to receive their medical care from the HMO's health care professionals, who are often paid a flat salary, and provides all services on a prepaid basis.

Preferred Provider Organization (PPO)

A health care plan that contracts with health care professionals to provide services at a reduced fee and gives patients financial incentives to use network providers.

Flexible Spending Account

Employee-controlled pretax earnings set aside to pay for certain eligible expenses such as health care expenses during the same year.



Tom Johnson runs on a treadmill at the Western & Southern Financial Group headquarters building in Cincinnati. The company is encouraging employees to reduce their health risks as insurance costs climb. Can you think of firms that offer other unique benefits to reduce health risks?

Employee Wellness Program (EWP)

A set of communications, activities, and facilities designed to change health-related behaviors in ways that reduce health risks.

Short-Term Disability Insurance

Insurance that pays a percentage of a disabled employee's salary as benefits to the employee for six months or less.

Long-Term Disability Insurance

Insurance that pays a percentage of a disabled employee's salary after an initial period and potentially for the rest of the employee's life.

CDHPs. At Black & Decker, a key to success was to offer a large enough medical savings account to make the plan attractive to employees.¹⁶

- An **employee wellness program (EWP)** is a set of communications, activities, and facilities designed to change health-related behaviors in ways that reduce health risks. Typically, an EWP aims at specific health risks, such as high blood pressure, high cholesterol levels, smoking, and obesity, by encouraging preventive measures such as exercise and good nutrition. *Passive* programs provide information and services, but no formal support or motivation to use the program. Examples include health education (such as lunchtime courses) and fitness facilities. *Active* wellness programs assume that behavior change requires support and reinforcement along with awareness and opportunity. Such a program may include counselors who tailor programs to individual employees' needs, take baseline measurements (for example, blood pressure and weight), and take follow-up measures for comparison to the baseline. In general, passive health education programs cost less than fitness facilities and active wellness programs.¹⁷ All these variations have had success in reducing risk factors associated with cardiovascular disease (obesity, high blood pressure, smoking, lack of exercise), but the follow-up method is most successful. The "eHRM" box describes how one company uses an online benefits portal as part of an effective wellness program.

Life Insurance

Employers may provide life insurance to employees or offer the opportunity to buy coverage at low group rates. With a *term life insurance* policy, if the employee dies during the term of the policy, the employee's beneficiaries receive a payment called the death benefit. In policies purchased as an employee benefit, the usual death benefit is twice the employee's yearly pay. The policies may provide additional benefits for accidental death and dismemberment (loss of a body part such as a hand or foot). Along with a basic policy, the employer may give employees the option of purchasing additional coverage, usually at a nominal cost.

Disability Insurance

Employees risk losing their incomes if a disability makes them unable to work. Disability insurance provides protection against this loss of income. Typically, **short-term disability insurance** provides benefits for six months or less. **Long-term disability insurance** provides benefits after that initial period, potentially for the rest of the disabled employee's life. Disability payments are a percentage of the employee's salary—typically 50 to 70 percent. Payments under short-term plans may be higher. Often the policy sets a maximum amount that may be paid each month. Because its limits make it more affordable, short-term disability coverage is offered by more employers. Fewer than half of employers offer long-term plans.

In planning an employee benefits package, the organization should keep in mind that Social Security includes some long-term disability benefits. To manage benefits costs, the employer should ensure that the disability insurance is coordinated with Social Security and any other programs that help workers who become disabled.

ONLINE BENEFITS PORTAL PUSHES WELLNESS EFFORT AT LEVITON



Leviton Manufacturing Company helps its customers save energy by using its lighting management systems. So when the company built a new headquarters, it logically applied that commitment to the environment and constructed an eco-friendly building. Motion sensors turn off lights in areas that aren't being used, and blinds automatically raise and lower themselves to adjust for the sun's impact on heating and cooling needs. That commitment to the environment might not seem to apply to human resource management, but Fran Ruderman, Leviton's senior director of benefits and compensation, saw an opportunity.

Under Ruderman, the company committed to eliminating paper from its benefits system by putting all the information online. Employees access the information at a benefits portal called HR InTouch. Employees use HR InTouch to enroll in health care

and retirement savings plans, update their personal and dependent information, and check the balance in their health savings account. Because not all employees have access to a computer on the job or at home, Ruderman had computer kiosks installed at each company location, so everyone can use the system conveniently.

An important application of HR InTouch has been getting employees more engaged with Leviton's wellness programs. Employees can log on to see interactive videos on a variety of health topics, including how to manage stress and how to eat wisely while traveling. During the company's open-enrollment period, when traffic to the site would be heavy, the company posted a video of Leviton's chief executive, Don Hendler, encouraging employees to take part in the wellness program.

A related effort is aimed at lowering health care expenses

by encouraging employees with chronic conditions (for example, diabetes and high cholesterol) to be actively engaged in managing those conditions to prevent complications. Through that program, called Medication Dedication, the company encourages employees to use low-cost generic medicines or, if no generic is available, lowers the cost of the brand-name drugs these employees need. Medication Dedication and the wellness programs together have reduced costs by almost 8 percent among the employees responsible for most of the company's claims.

Sources: Joanne Wojcik, "Leviton Goes Green to Save Green," *Business Insurance*, November 30, 2009, Business & Company Resource Center, <http://galenet.galegroup.com>; and Joanne Wojcik, "Rising to the Benefits Challenge," *Business Insurance*, November 30, 2009, Business & Company Resource Center, <http://galenet.galegroup.com>.

Long-Term Care Insurance

The cost of long-term care, such as care in a nursing home, can be devastating. Today, with more people living to an advanced age, many people are concerned about affording long-term care. Some employers address this concern by offering long-term care insurance. These policies provide benefits toward the cost of long-term care and related medical expenses.

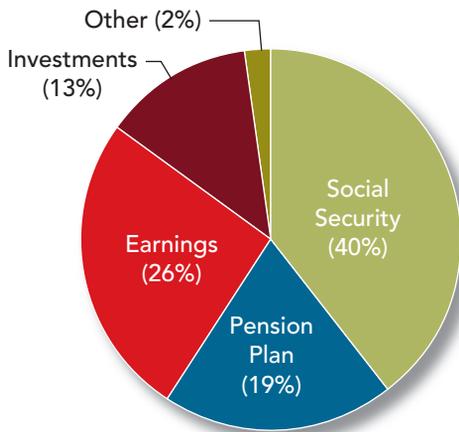
Retirement Plans

Despite the image of retired people living on their Social Security checks, Figure 13.4 shows that those checks amount to less than half of a retired person's income. Among persons over age 65, pensions provided a significant share of income in 2006. Employers have no obligation to offer retirement plans beyond the protection of Social Security, but most offer some form of pension or retirement savings plan. About half of employees working for private businesses (that is, nongovernment jobs) have employer-sponsored retirement plans. These plans are most common for

LO5 Define the types of retirement plans offered by employers.

Figure 13.4

Sources of Income for Persons 65 and Older



SOURCE: Based on Employee Benefit Research Institute, "Sources of Income for Persons Aged 55 and Over," Chapter 7, *EBRI Databook on Employee Benefits*, Chart 7.1b, updated March 2010, www.ebri.org.

Contributory Plan

Retirement plan funded by contributions from the employer and employee.

Noncontributory Plan

Retirement plan funded entirely by contributions from the employer.

Defined-Benefit Plan

Pension plan that guarantees a specified level of retirement income.

Employee Retirement Income Security Act (ERISA)

Federal law that increased the responsibility of pension plan trustees to protect retirees, established certain rights related to vesting and portability, and created the Pension Benefit Guarantee Corporation.

higher-earning employees. Among employees earning the top one-fourth of incomes, more than 80 percent participate in a retirement plan, and about one out of four employees in the bottom one-fourth have such plans.¹⁸ Retirement plans may be **contributory plans**, meaning they are funded by contributions from the employer and employee, or **noncontributory plans**, meaning all the contributions come from the employer.

Defined-Benefit Plans

Employers have a choice of using retirement plans that define the amount to be paid out after retirement or plans that define the amount the employer will invest each year. A **defined-benefit plan** guarantees a specified level of retirement income. Usually the amount of this defined benefit is calculated for each employee based on the employee's years of service, age, and earnings level (for example, the average of the employee's five highest-earnings years). These calculations typically result in pension payments that range from 20 percent of final salary for an employee who is relatively young and has few years of service to 35 percent of the final salary of an older employee who has

spent many years with the organization. Using years of service as part of the basis for calculating benefits gives employees an incentive to stay with the organization as long as they can, so it can help to reduce voluntary turnover.

Defined-benefit plans must meet the funding requirements of the **Employee Retirement Income Security Act (ERISA)** of 1974. This law increased the responsibility of pension plan trustees to protect retirees, established certain rights related to vesting (earning a right to receive the pension) and *portability* (being able to move retirement savings when changing employers), and created the **Pension Benefit Guarantee Corporation (PBGC)**. The PBGC is the federal agency that insures retirement benefits and guarantees retirees a basic benefit if the employer experiences financial difficulties. To fund the PBGC, employers must make annual contributions of \$33 per fund participant. Plans that are *underfunded*—meaning the employer does not contribute enough to the plan each year to meet future obligations—must pay an additional premium tied to the amount by which the plan is underfunded.¹⁹ The PBGC's protection applies to the pensions of 44 million workers.

With a defined-benefit plan, the employer sets up a pension fund to invest the contributions. As required by ERISA, the employer must contribute enough for the plan to cover all the benefits to be paid out to retirees. Defined-benefit plans protect employees from the risk that the pension fund will not earn as much as expected. If the pension fund earns less than expected, the employer makes up the difference from other sources. If the employer experiences financial difficulties so that it must end or reduce employee pension benefits, the PBGC provides a basic benefit, which does not necessarily cover the full amount promised by the employer's pension plan. The PBGC establishes a maximum; in 2007, it was the lesser of $\frac{1}{12}$ of an employee's annual gross income or \$3,712 per month.

Defined-Contribution Plans

An alternative to defined benefits is a **defined-contribution plan**, which sets up an individual account for each employee and specifies the size of the investment into that account, rather than the amount to be paid out upon retirement. The

amount the retiree receives will depend on the account's performance. Many kinds of defined-contribution plans are available, including the following:

- *Money purchase plan*—The employer specifies a level of annual contributions (for example, 10 percent of salary). The contributions are invested, and when the employee retires, he or she is entitled to receive the amount of the contributions plus the investment earnings. (“Money purchase” refers to the fact that when employees retire, they often buy an annuity with the money, rather than taking it as a lump sum.)
- *Profit-sharing and employee stock ownership plans*—As we saw in Chapter 12, incentive pay may take the form of profit sharing and employee stock ownership plans (ESOPs). These payments may be set up so that the money goes into retirement plans. By defining its contributions in terms of stock or a share of profits, the organization has more flexibility to contribute less dollar value in lean years and more in good years.
- *Section 401(k) plans*—Employees contribute a percentage of their earnings, and employers may make matching contributions. The amount employees contribute is not taxed as part of their income until they receive it from the plan. The federal government limits the amount that may be contributed each year. The limit for 2007 and 2008 was \$15,500; it may increase by up to \$500 a year through 2010, depending on the inflation rate. The contribution limits are higher for persons 50 and older.²⁰

These plans free employers from the risks that investments will not perform as well as expected. They put the responsibility for wise investing squarely on the shoulders of each employee. A defined-contribution plan is also easier to administer. The employer need not calculate payments based on age and service, and payments to the PBGC are not required. Considering the advantages to employers, it is not surprising that a growing share of retirement plans are defined-contribution plans. Three decades ago, the majority of workers with pension plans had defined-benefit plans, and less than one-fourth had defined-contribution plans. Today, following a steady decline in the number of defined-benefit plans and a steady rise in the number of defined-contribution plans, that pattern is reversed.²¹ Still, many organizations offer both kinds of retirement plans.

When retirement plans make individual employees responsible for investment decisions, the employees need information about retirement planning. Retirement savings plans often give employees much control over decisions about when and how much to invest. Many employees do not appreciate the importance of beginning to save early in their careers. As Figure 13.5 shows, an employee who invests \$3,000 a year (\$250 a month) between the ages of 21 and 29 will have far more at age 65 than an employee who invests the same amount between ages 31 and 39. Another important lesson is to diversify investments. Based on investment performance between 1946 and 1990, stocks earned an average of 11.4 percent per year, bonds earned 5.1 percent, and bank savings accounts earned 5.3 percent. But in any given year, one of these types of investments might outperform the other. And within the categories of stocks and bonds, it is important to invest in a wide variety of companies. If one company performs poorly, the investments in other companies might perform better. However, studies of investment decisions by employees have found that many employees hold a sizable share of their retirement savings in stock of the company they work for, and few have followed basic guidelines for diversifying investments among stocks, bonds, and savings accounts according to their age and investment

Pension Benefit Guarantee Corporation (PBGC)

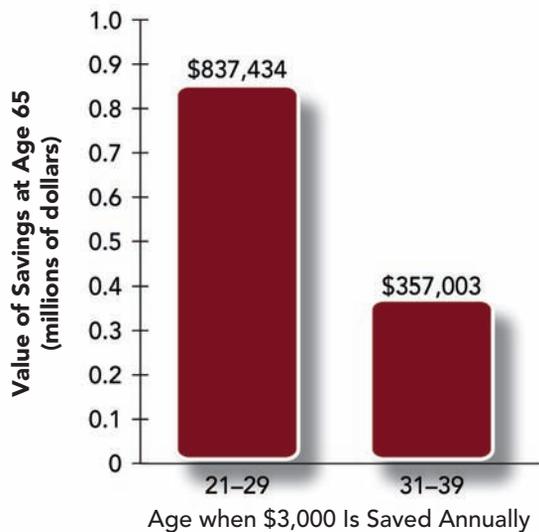
Federal agency that insures retirement benefits and guarantees retirees a basic benefit if the employer experiences financial difficulties.

Defined-Contribution Plan

Retirement plan in which the employer sets up an individual account for each employee and specifies the size of the investment into that account.

Figure 13.5

Value of Retirement Savings Invested at Different Ages



Note: Investment portfolio consists of 60 percent stocks, 30 percent bonds, and 10 percent cash (e.g., money-market funds, bank savings accounts), assuming average rates of return based on historical rates from 1946 to 1990.

Cash Balance Plan

Retirement plan in which the employer sets up an individual account for each employee and contributes a percentage of the employee's salary; the account earns interest at a predefined rate.

This type of retirement plan consists of individual accounts, as in a 401(k) plan. But in contrast to a 401(k), all the contributions come from the employer. Usually, the employer contributes a percentage of the employee's salary, say, 4 or 5 percent. The money in the cash balance plan earns interest according to a predetermined rate, such as the rate paid on U.S. Treasury bills. Employers guarantee this rate as in a defined-benefit plan. This arrangement helps employers plan their contributions and helps employees predict their retirement benefits. If employees change jobs, they generally can roll over the balance into an individual retirement account.

A switch from traditional defined-benefit plans to cash balance plans, like any major change, requires employers to consider the effects on employees as well as on the organization's bottom line. Defined-benefit plans are most generous to older employees with many years of service, and cash balance plans are most generous to young employees who will have many years ahead in which to earn interest. For an organization with many experienced employees, switching from a defined-benefit plan can produce great savings in pension benefits. In that case, the older workers are the greatest losers, unless the organization adjusts the program to retain their benefits. After IBM switched to a cash-benefit plan, a group of employees filed an age discrimination lawsuit. IBM won the lawsuit on appeal, and the Pension Protection Act of 2006 seeks to clarify the legal requirements of such plans. As a result, some companies may renew their interest in cash balance plans, but IBM has decided to focus on its 401(k) plan.

Government Requirements for Vesting and Communication

Along with requirements for funding defined-benefit plans, ERISA specifies a number of requirements related to eligibility for benefits and communication with employees. ERISA guarantees employees that when they become participants in a pension plan

needs.²² To help employees handle such risks, some organizations provide financial planning as a separate benefit, offer an option to have a professional invest the funds in a 401(k) plan, or direct funds into default investments geared toward the needs of employees at different life stages. For example, when a Portland, Oregon, developer called Classic American Homes found that its employees made poor investments, such as moving into risky real estate funds *after* real estate prices had been rising, the company began offering just one fund that combines 60 percent stocks and 40 percent bonds.

In spite of these challenges, defined-contribution plans also offer an advantage to employees in today's highly mobile workforce. They do not penalize employees for changing jobs. With these plans, retirement earnings are less related to the number of years an employee stays with a company.

Cash Balance Plans

An increasingly popular way to combine the advantages of defined-benefit plans and defined-contribution plans is to use a **cash balance plan**.

and work a specified number of years, they earn a right to a pension upon retirement. These rights are called **vesting rights**. Employees whose contributions are *vested* have met the requirements (enrolling and length of service) to receive a pension at retirement age, regardless of whether they remained with the employer until that time. Employees' own contributions to their pension plans are always completely vested. In most cases, the vesting of employer-funded pension benefits must take place under one of two schedules selected by the employer:

1. The employer may vest employees after five years and may provide zero vesting until that time.
2. The employer may vest employees over a three- to seven-year period, with at least 20 percent vesting in the third year and at least an additional 20 percent in each year after the third year.

These two schedules represent minimum requirements. Employers may vest employees more quickly if they wish. Two less-common situations have different vesting requirements. One is a “top-heavy” pension plan, meaning pension benefits for *key employees* (such as highly paid top managers) exceed a government-specified share of total pension benefits. A top-heavy plan requires faster vesting for nonkey employees. Another exception from the usual schedule involves multiemployer pension plans. These plans need not provide vesting until after 10 years of employment.

The intent of vesting requirements is to protect employees by preventing employers from terminating them before they meet retirement age in order to avoid paying pension benefits. In addition, it is illegal for employers to transfer or lay off employees as a way to avoid pension obligations, even if these changes are motivated partly by business need.²³ One way employers may legally try to minimize pension costs is in choosing a vesting schedule. For example, if many employees leave after three or four years of employment, the five-year vesting schedule would minimize pension costs.

ERISA's reporting and disclosure requirements involve the Internal Revenue Service, the Department of Labor, and employees.²⁴ Within 90 days after employees enter a plan, they must receive a **summary plan description (SPD)**, a report that describes the plan's funding, eligibility requirements, risks, and other details. If the employee requests one, the employer must also make available an individual benefit statement, which describes the employee's vested and unvested benefits. Many employers provide such information regularly, without waiting for employee requests. This type of communication helps employees understand and value their retirement benefits.

“Family-Friendly” Benefits

As employers have recognized the significance of employees' need to manage conflicts between their work and family roles, many have added “family-friendly” benefits to their employee benefits. These benefits include family leave policies and child care. The programs discussed here apply directly to the subset of employees with family responsibilities. However, family-friendly benefits often have spillover effects in the form of loyalty because employees see the benefits as evidence that the organization cares about its people.²⁵ The following types of benefits are typical:

- *Family leave*—Family or parental leave grants employees time off to care for children and other dependents. As discussed earlier in the chapter, federal law requires 12 weeks of unpaid leave. Companies may choose to offer more generous leave policies. Paid family leave remains rare in the United States, however, despite

Vesting Rights

Guarantee that when employees become participants in a pension plan and work a specified number of years, they will receive a pension at retirement age, regardless of whether they remained with the employer.

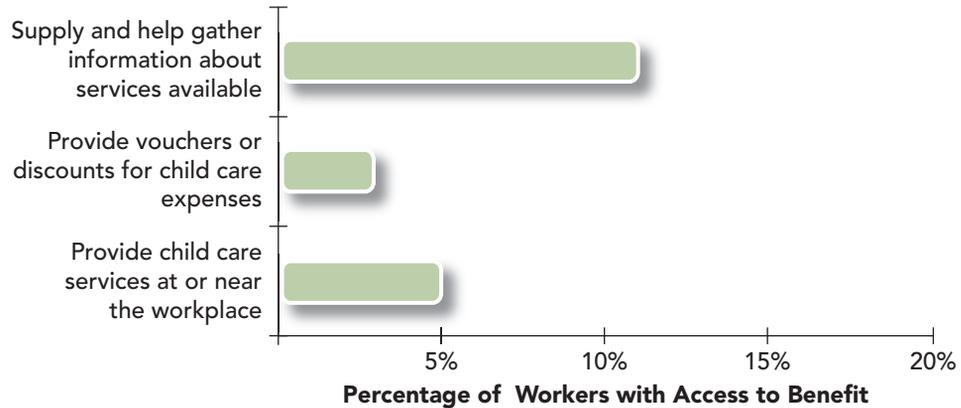
Summary Plan Description (SPD)

Report that describes a pension plan's funding, eligibility requirements, risks, and other details.

L06 Describe how organizations use other benefits to match employees' wants and needs.

Figure 13.6

Percentage of Employees
with Various Levels of
Child Care Benefits



SOURCE: John E. Buckley, "Beyond Basic Benefits: Employee Access to Other Types of Benefits, 1979–2008," *Compensation and Working Conditions Online*, May 29, 2009, www.bls.gov.

some state laws. By contrast, more than 120 countries provide paid family leave by law. The norm in Western Europe is at least three to four months' maternity leave at 80 to 100 percent of pay, plus additional (often unpaid) parental leave for both parents.²⁶

- **Child care**—Child care benefits may take several forms, requiring different levels of organizational involvement. As shown in Figure 13.6, the lowest level of involvement, offered by 19 percent of companies with at least 100 workers, is for the organization to supply and help employees collect information about the cost and quality of available child care. At the next level, organizations provide vouchers or discounts for employees to use at existing child care facilities. At the highest level of involvement, the employer provides child care at or near the work site. Staffing a child care facility is costly and involves important liability concerns. At the same time, the results of this type of benefit, in terms of reducing absenteeism and enhancing productivity, have been mixed.²⁷ When Providian Financial Corporation, a credit card company with headquarters in San Francisco, determined that for many of its employees, the big hurdle with child care and elder care was affordability, it set up flexible spending accounts for dependent care.²⁸
- **College savings**—As workers' children grow up, their needs shift from maternity leave and child care to college tuition. Some organizations have supported this concern by sponsoring tax-favored 529 *savings plans*. These plans, named after the section of the Internal Revenue Code that regulates them, let parents and other family members defer taxes on the earnings of their deposits into the 529 account. Some states also provide a (limited) tax deduction for these contributions. As an employee benefit, organizations can arrange with a broker to offer direct deposit of a portion of employees' paychecks into their accounts. Besides offering the convenience of direct deposit, employers can negotiate lower management fees. To support employee retention, United Supermarkets offers its employees a college-savings plan and matches contributions with a percentage that increases annually for four years.²⁹
- **Elder care**—As the population of the nation's elderly grows, so do the demands on adult children to care for elderly parents, aunts, and uncles. When these people become ill or disabled, they rely on family or professional caregivers.

Responsibilities such as providing assistance, paying for professional caregivers, and locating services can be expensive, time consuming, and exhausting, often distracting employees from their work roles. In response, many employers have added elder care benefits. These benefits typically emphasize information and support, rather than direct financial assistance. For example, organizations may provide access to counseling, flexible schedules, and printed resources. An increasing popular benefit is referrals to health advocacy services, which can help employees pick Medicare Part D drug coverage, find long-term care facilities, or prepare a checklist of questions for a doctor visit.³⁰ Even companies that cannot afford to offer counseling or referral services can use intranets to provide links to helpful websites such as the National Alliance for Caregiving (www.caregiving.org), the National Council on Aging (www.benefitscheckup.org), and the federal government's benefits information site (govbenefits.gov).

Other Benefits

The scope of possible employee benefits is limited only by the imagination of the organization's decision makers. Organizations have developed a wide variety of benefits to meet the needs of employees and to attract and keep the kinds of workers who will be of value to the organization. Traditional extras include subsidized cafeterias, on-site health care for minor injuries or illnesses, and moving expenses for newly hired or relocating employees. Stores and manufacturers may offer employee discounts on their products.

To encourage learning and attract the kinds of employees who wish to develop their knowledge and skills, many organizations offer *tuition reimbursement* programs. A typical program covers tuition and related expenses for courses that are relevant to



In order to provide a relaxed environment for their employees, one of the perks at Neversoft Entertainment is allowing employees to bring their pets to work. What other unique benefits do companies offer their employees?

the employee's current job or future career at the organization. Employees are reimbursed for these expenses after they demonstrate they have completed an approved course.

Especially for demanding, high-stress jobs, organizations may look for benefits that help employees put in the necessary long hours and alleviate stress. Recreational activities such as on-site basketball courts or company-sponsored softball teams provide for social interaction as well as physical activity. Employers may reward hard-working groups or individuals with a trip for a weekend, a meal, or any activity employees are likely to enjoy. Some companies, including Minneapolis design agency Sevnthsin and Vancouver Web site designer Mezine, allow employees to bring their pets to work. Mezine cofounder Dean Gagnon explains the benefit: "It's almost impossible to have a bad day with a dog walking around the office."³¹

L07 Explain how to choose the contents of an employee benefits package.

Selecting Employee Benefits

Although the government requires certain benefits, employers have wide latitude in creating the total benefits package they offer employees.³² Decisions about which benefits to include should take into account the organization's goals, its budget, and the expectations of the organization's current employees and those it wishes to recruit in the future. Employees have come to expect certain things from employers. An organization that does not offer the expected benefits will have more difficulty attracting and keeping talented workers. Also, if employees believe their employer feels no commitment to their welfare, they are less likely to feel committed to their employer.

The Organization's Objectives

A logical place to begin selecting employee benefits is to establish objectives for the benefits package. This helps an organization select the most effective benefits and monitor whether the benefits are doing what they should. Table 13.2 is an example of one organization's benefits objectives. Unfortunately, research suggests that most organizations do not have written benefits objectives.

Among companies that do set goals, the most common objectives include controlling the cost of health care benefits and retaining employees.³³ The first goal explains the growing use of wellness programs and consumer-directed health plans. For the second goal, employers need to learn what employees care about. In some cases, the approach may be indirect, helping the company distinguish itself as an employer that certain kinds of employees will be attracted to and committed to. For example, a company that establishes itself as committed to the environment could offer benefits in line with that goal—say, bicycle storage for commuters and vouchers for taking the bus to work.³⁴ Employees with a passion for the environment would be especially engaged by such offerings.

Employees' Expectations and Values

Employees expect to receive benefits that are legally required and widely available, and they value benefits they are likely to use. For example, the "HR Oops!" box illustrates the value employees place on product discounts. To meet employee expectations about benefits, it can be helpful to see what other organizations offer. Employers can purchase survey information about benefits packages from private consultants. In addition, the Bureau of Labor Statistics gathers benefits data. The BLS Web site (www.bls.gov) is therefore a good place to check for free information about employee



Table 13.2**An Organization's
Benefits Objectives**

- To establish and maintain an employee benefit program that is based primarily on the employees' needs for leisure time and on protection against the risks of old age, loss of health, and loss of life.
- To establish and maintain an employee benefit program that complements the efforts of employees on their own behalf.
- To evaluate the employee benefit plan annually for its effect on employee morale and productivity, giving consideration to turnover, unfilled positions, attendance, employees' complaints, and employees' opinions.
- To compare the employee benefit plan annually with that of other leading companies in the same field and to maintain a benefit plan with an overall level of benefits based on cost per employee that falls within the second quintile of these companies.
- To maintain a level of benefits for nonunion employees that represents the same level of expenditures per employee as for union employees.
- To determine annually the costs of new, changed, and existing programs as percentages of salaries and wages and to maintain these percentages as much as possible.
- To self-fund benefits to the extent that a long-run cost savings can be expected for the firm and catastrophic losses can be avoided.
- To coordinate all benefits with social insurance programs to which the company makes payments.
- To provide benefits on a noncontributory basis except for dependent coverage, for which employees should pay a portion of the cost.
- To maintain continual communications with all employees concerning benefit programs.

SOURCE: Adapted from B. T. Beam Jr. and J. J. McFadden, *Employee Benefits*, 3rd ed. © 1992 by Dearborn Financial Publishing, Inc. Published by Dearborn Financial Publishing, Inc., Chicago. All rights reserved.

benefits in the United States. With regard to value, medical insurance is a high-value benefit because employees usually realize that surgery or a major illness can be financially devastating. Vision and dental care tend to be much less expensive, but many employees appreciate this type of coverage because so many people receive dental or vision care in the course of a year. As a result, many employers are finding that employees are even happy to pay the modest premiums for dental and vision coverage themselves because of the value they place on this benefit.³⁵

Employers should also consider that the value employees place on various benefits is likely to differ from one employee to another. At a broad level, basic demographic factors such as age and sex can influence the kinds of benefits employees want. An older workforce is more likely to be concerned about (and use) medical coverage, life insurance, and pensions. A workforce with a high percentage of women of childbearing age may care more about disability or family leave. Young, unmarried men and women often place more value on pay than on benefits. However, these are only general observations; organizations should check which considerations apply to their own employees and identify more specific needs and differences. One approach is to use surveys to ask employees about the kinds of benefits they value. The survey should be carefully worded so as not to raise employees' expectations by seeming to promise all the benefits asked about at no cost to the employee.

The choice of benefits may influence current employees' satisfaction and may also affect the organization's recruiting, in terms of both the ease of recruiting and the kinds of employees attracted to the organization. For example, a benefits package that has strong medical benefits and pensions may be particularly attractive to older people or to those with many dependents. Such benefits may attract people with extensive

Underestimating the Importance of Employee Discounts

Part of knowing what employees value is knowing what they don't want to lose. Brian Dunn learned that the hard way as an executive of Best Buy.

Dunn hoped to improve profitability by cutting costs, and he thought employees would accept a smaller employee discount. To be certain, the company monitored comments on its employee social-networking site, the Water-cooler. The results were soon in:

employees flooded the site with 54 pages of comments, most of them furious.

Just five days later, Dunn reviewed the reaction with senior management. The decision was easy: Best Buy backed down and restored the employee discount to its original level.

Questions

1. Are you surprised that employee discounts are a

highly valued benefit at Best Buy? Why or why not? What kinds of employees would this benefit attract?

2. Suggest a way that Best Buy could have reduced the costs of benefits without sparking employee anger.

Source: Based on Matthew Boyle, "Look before You Chop Employee Perks," *BusinessWeek*, February 20, 2009, www.businessweek.com.

Cafeteria-Style Plan

A benefits plan that offers employees a set of alternatives from which they can choose the types and amounts of benefits they want.

experience and those who wish to make a long-term commitment to the organization. This strategy may be especially beneficial when turnover costs are very high. On the other hand, offering generous health care benefits may attract and retain people with high health care costs. Thus, organizations need to consider the signals sent by their benefits package as they set goals for benefits and select benefits to offer.

Organizations can address differences in employees' needs and empower their employees by offering flexible benefits plans in place of a single benefits package for all employees. These plans, often called **cafeteria-style plans**, offer employees a set of alternatives from which they can choose the types and amounts of benefits they want. The plans vary. Some impose minimum levels for certain benefits, such as health care coverage; some allow better employees to receive money in exchange for choosing a "light" package; and some let employees pay extra for the privilege of receiving more benefits. For example, some plans let employees give up vacation days for more pay or to purchase extra vacation days in exchange for a reduction in pay.

Cafeteria-style plans have a number of advantages.³⁶ The selection process can make employees more aware of the value of the benefits, particularly when the plan assigns each employee a sum of money to allocate to benefits. Also, the individual choice in a cafeteria plan enables each employee to match his or her needs to the company's benefits, increasing the plan's actual value to the employee. And because employees would not select benefits they don't want, the company avoids the cost of providing employees with benefits they don't value. Another way to control costs is to give employees incentives to choose lower-cost options. For example, the employee's deductible on a higher-cost health plan could be larger than on a relatively low-cost HMO.

A drawback of cafeteria-style plans is that they have a higher administrative cost, especially in the design and start-up stages. Organizations can avoid some of the higher cost, however, by using software packages and standardized plans that have been developed for employers wishing to offer cafeteria-style benefits. Another possible drawback is that employee selection of benefits will increase rather than decrease costs because employees will select the kinds of benefits they expect to need the most.

For example, an employee expecting to need a lot of dental work is more likely to sign up for a dental plan. The heavy use of the dental coverage would then drive up the employer's premiums for that coverage. Costs can also be difficult to estimate when employees select their benefits.

Benefits' Costs

Employers also need to consider benefits costs. One place to start is with general information about the average costs of various benefits types. Widely used sources of cost data include the Bureau of Labor Statistics (BLS), Employee Benefit Research Institute, and U.S. Chamber of Commerce. Annual surveys by the Chamber of Commerce state the cost of benefits as a percentage of total payroll costs and in dollar terms.

Employers can use data about costs to help them select the kinds of benefits to offer. But in balancing these decisions against organizational goals and employee benefits, the organization may decide to offer certain high-cost benefits while also looking for ways to control the cost of those benefits. The highest-cost items tend to offer the most room for savings, but only if the items permit choice or negotiation. Also, as we noted earlier, organizations can control certain costs such as workers' compensation by improving their experience ratings. Cost control is especially important—and difficult—when economic growth slows or declines.

In recent years, benefits related to health care have attracted particular attention because these costs have risen very rapidly and because employers have a number of options. Concern over costs has prompted many employers to shift from traditional health insurance to PPOs and CDHPs. Some employers shift more of the cost to employees. They may lower the employer's payments by increasing the amounts employees pay for deductibles and coinsurance (the employee's share of the payment for services). Or they may require employees to pay some or all of the difference in cost between traditional insurance and a lower-cost plan. Excluding or limiting coverage for certain types of claims also can slow the increase in health insurance costs. Employee wellness programs, especially when they are targeted to employees with risk factors and include follow-up and encouragement, can reduce risk factors for disease.³⁷

Legal Requirements for Employee Benefits

As we discussed earlier in this chapter, some benefits are required by law. This requirement adds to the cost of compensating employees. Organizations looking for ways to control staffing costs may look for ways to structure the workforce so as to minimize the expense of benefits. They may require overtime rather than adding new employees, hire part-time rather than full-time workers (because part-time employees generally receive much smaller benefits packages), and use independent contractors rather than hire employees. Some of these choices are limited by legal requirements, however. For example, the Fair Labor Standards Act requires overtime pay for nonexempt workers, as discussed in Chapter 11. Also, the Internal Revenue Service strictly limits the definition of "independent contractors," so that employees cannot avoid legal obligations by classifying workers as self-employed when the organization receives the benefits of a permanent employee. Other legal requirements involve tax treatment of benefits, antidiscrimination laws, and accounting for benefits.

L08 Summarize the regulations affecting how employers design and administer benefits programs.

Tax Treatment of Benefits

The IRS provides more favorable tax treatment of benefits classified as *qualified plans*. The details vary from one type of benefit to another. In the case of retirement plans, the advantages include the ability for employees to immediately take a tax deduction for the funds they contribute to the plans, no immediate tax on employees for the amount the employer contributes, and tax-free earnings on the money in the retirement fund.³⁸

To obtain status as a qualified plan, a benefit plan must meet certain requirements.³⁹ In the case of pensions, these involve vesting and nondiscrimination rules. The nondiscrimination rules provide tax benefits to plans that do not discriminate in favor of the organization's "highly compensated employees." To receive the benefits, the organization cannot set up a retirement plan that provides benefits exclusively to the organization's owners and top managers. The requirements encourage employers to provide important benefits such as pensions to a broad spectrum of employees. Before offering pension plans and other benefits, organizations should have them reviewed by an expert who can advise on whether the benefits are qualified plans.

Antidiscrimination Laws

As we discussed in Chapter 3, a number of laws are intended to provide equal employment opportunity without regard to race, sex, age, disability, and several other protected categories. Some of these laws apply to the organization's benefits policies.

Legal treatment of men and women includes equal access to benefits, so the organization may not use the employee's gender as the basis for providing more limited benefits. That is the rationale for the Pregnancy Discrimination Act, which requires that employers treat pregnancy as it treats any disability. If an employee needs time off for conditions related to pregnancy or childbirth, the employee would receive whatever disability benefits the organization offers to employees who take disability leave for other reasons. Another area of concern in the treatment of male and female employees is pension benefits. On average, women live longer than men, so on average, pension benefits for female employees are more expensive (because the organization pays the pension longer), other things being equal. Some organizations have used this difference as a basis for requiring that female employees contribute more than male employees to defined benefit plans. The Supreme Court in 1978 determined that such a requirement is illegal.⁴⁰ According to the Supreme Court, the law is intended to protect individuals, and when women are considered on an individual basis (not as averages), not every woman outlives every man.

Age discrimination is also relevant to benefits policies. Two major issues have received attention under the Age Discrimination in Employment Act (ADEA) and amendments. First, employers must take care not to discriminate against workers over age 40 in providing pay or benefits. For example, employers may not set an age at which retirement benefits stop growing as a way to pressure older workers to retire.⁴¹ Also, early-retirement incentive programs need to meet certain standards. The programs may not coerce employees to retire, they must provide accurate information about the options available, and they must give employees enough time to make a decision. In effect, employees must really have a choice about whether they retire.

When employers offer early retirement, they often ask employees to sign waivers saying they will not pursue claims under the ADEA. The Older Workers Benefit Protection Act of 1990 set guidelines for using these waivers. The waivers must be voluntary and understandable to the employee and employer, and they must spell out

the employee's rights under the ADEA. Also, in exchange for signing the waiver, the employee must receive "compensation," that is, greater benefits than he or she would otherwise receive upon retirement. The employer must inform employees that they may consult a lawyer before signing, and employees must have time to make a decision about signing—21 days before signing plus 7 days afterward in which they can revoke the agreement.

The Americans with Disabilities Act imposes requirements related to health insurance. Under the ADA, employees with disabilities must have "equal access to whatever health insurance coverage the employer provides other employees." Even so, the terms and conditions of health insurance may be based on risk factors—as long as the employer does not use this basis as a way to escape offering health insurance to someone with a disability. From the standpoint of avoiding legal challenges, an employer who has risk-based insurance and then hires an employee with a disability is in a stronger position than an employer who switches to a risk-based policy after hiring a disabled employee.⁴²

Accounting Requirements

Companies' financial statements must meet the many requirements of the Financial Accounting Standards Board (FASB). These accounting requirements are intended to ensure that financial statements are a true picture of the company's financial status and that outsiders, including potential lenders and investors, can understand and compare financial statements. Under FASB standards, employers must set aside the funds they expect to need for benefits to be paid after retirement, rather than funding those benefits on a pay-as-you-go basis. On financial statements, those funds must appear as future cost obligations. For companies with substantial retirement benefits, reporting those benefits as future cost obligations greatly lowers income each year. Along with rising benefits costs, this reporting requirement has encouraged many companies to scale back benefits to retirees.

Communicating Benefits to Employees

Organizations must communicate benefits information to employees so that they will appreciate the value of their benefits. This is essential so that benefits can achieve their objective of attracting, motivating, and retaining employees. Employees are interested in their benefits, and they need a great deal of detailed information to take advantage of benefits such as health insurance and 401(k) plans. It follows that electronic technology such as the Internet and supporting databases can play a significant role in modern benefit systems. Many companies are putting benefits information on their intranets. The "HR How To" box provides further suggestions for communicating effectively the value of the organization's benefits.

In actuality, employees and job applicants often have a poor idea of what benefits they have and what the market value of their benefits is. Research asking employees about their benefits has shown that employees significantly underestimate the cost and value of their benefits.⁴³ Probably a major reason for their lack of knowledge is a lack of communications from employers. Employees don't know what employers are spending for benefits, so many of them doubt employers' complaints about soaring costs and their impact on the company's future.⁴⁴ In one study, employees said their company neglected to tell them how to be better consumers of health care, and they would be willing to make changes in their lifestyle if they had a financial incentive to

L09 Discuss the importance of effectively communicating the nature and value of benefits to employees.

COMMUNICATING ABOUT BENEFITS

If benefits are aimed at increasing employees' satisfaction, making them feel more valued by and engaged with the organization, then employers defeat the purpose if they don't communicate. Research has shown that effective communication reinforces the value of the benefits and is associated with a positive attitude toward them. Here are some tips for getting out the word about the company's benefits:

- Communicate frequently, not just when it's time for employees to enroll in insurance and savings plans. Besides regular communications with all employees, the organization might consider personalized messages to employees at the time of major life events, such as marriage or the birth of a child, that may trigger different benefits needs or a fresh focus on finances.
- Use at least three different forms of communication: visual (for example, online

videos or brochures with graphs and photos), auditory (for example, presentations at meetings or on podcasts), and hands-on (interactive tools such as calculators for comparing benefits options).

- Besides telling employees what the benefits *are*, provide information about how to get the most out of company benefits. For example, when employees saw their defined-contribution retirement funds shrink during the recent recession, they might have become discouraged about investing. That was an opportunity for employers to help younger workers take a long-term view and consider that continuing to invest when the market is down can deliver big returns later. Older employees might be interested in education about how to protect their investments and stretch their dollars in retirement.
- Make sure employees understand the message. Provide

opportunities to ask questions online or in person. When a decision needs to be made, give employees plenty of time to review the options. One recent study found that employees need at least three weeks to review benefits options before making decisions.

- If employees do not all speak English as their primary language, provide materials in the languages employees are familiar with and consider providing access to bilingual customer service representatives to answer questions about the benefits.

Sources: Mike Simonds, "Better ROI from Benefits," *BusinessWeek*, January 8, 2010, www.businessweek.com; Anthony J. Nugent, "Measuring Up: The Strategic Use of Benchmarking and Voluntary Benefits," *Benefits Selling*, February 2010, Business & Company Resource Center, <http://galenet.galegroup.com>; and Joanne Sammer, "Rescuing Pension Plans," *HR Magazine*, May 2009, www.shrm.org.

do so. Such research suggests to employers that better communication, coupled with well-designed benefits plans, will pay off in practical terms.

Employers have many options for communicating information about benefits. To increase the likelihood that employees will receive and understand the messages, employers can combine several media, such as brochures, question-and-answer meetings, intranet pages, memos, and e-mail. Some other possible media include paycheck inserts, retirement or health coaching, training programs, and benefits fairs. An investment of creativity in communications to employees can reap great returns in the form of committed, satisfied employees.

thinking ethically

IS IT FAIR FOR EXECUTIVES' RETIREMENTS TO BE MORE SECURE?

Blame it on the economy? In 2009, according to Boston College's Center on Retirement Research, the 401(k) retirement plans of 50 million employees lost a total of \$1 trillion or more when the value of their investments took a dive. But while most employees were hit hard, executives at some companies were protected. Because the Internal Revenue Service limits the amount of contributions to 401(k) plans, employers set up supplemental plans for their higher-paid employees. At some companies, these plans include less-risky fixed-income funds that deliver returns even when stock funds are declining.

In some cases, the differences were dramatic. Walmart's 401(k) retirement plan lost 18 percent of its value in 2009. Some employees did worse; manager Jacqueline D'Andrea says she lost 60 percent of the value in her plan. In contrast, Walmart's CEO enjoyed a \$2.3 million gain in his supplemental retirement savings. Other companies with dramatic differences include Comcast, where executives' deferred-compensation accounts rose 12 percent while employees' 401(k)s

fell 29 percent, and McKesson, where executives enjoyed an 8 percent gain versus a 31 percent loss for employees.

SOURCE: Based on Ellen E. Schultz and Tom McGinty, "Executives Enjoy 'Sure Thing' Retirement Plans," *Wall Street Journal*, December 15, 2009, <http://online.wsj.com>.

Questions

1. Discuss whether it is fair for executives to receive larger retirement plans than employees in lower-ranking jobs. With more money to invest, should they have more investment options, such as fixed-income funds? Why or why not?
2. How, if at all, should employers help employees manage the risks of investing in defined-contribution retirement plans?
3. Assume you work in the HR division of Walmart. How would you communicate with employees about the performance of their retirement funds in a year when their value falls? How would you address the difference between employees' returns and executives' returns?

SUMMARY

LO1 Discuss the importance of benefits as a part of employee compensation.

Like pay, benefits help employers attract, retain, and motivate employees. The variety of possible benefits also helps employers tailor their compensation packages to attract the right kinds of employees. Employees expect at least a minimum level of benefits, and providing more than the minimum helps an organization compete in the labor market. Benefits are also a significant expense, but employers provide benefits because employees value them and many benefits are required by law.

LO2 Summarize the types of employee benefits required by law.

Employers must contribute to the Old Age, Survivors, Disability, and Health Insurance program known as Social Security through a payroll tax shared by employers and employees. Employers must also pay federal and state taxes for unemployment insurance, based on each employer's experience rating, or percentage of employees a company has laid off in the past. State laws require that

employers purchase workers' compensation insurance. Under the Family and Medical Leave Act, employees who need to care for a baby following birth or adoption or for an ill family member must be granted unpaid leave of up to 12 weeks. Under the Patient Protection and Affordable Care Act, employers need to prepare for future requirements to provide all employees with health insurance, as well as to educate themselves about other provisions such as insurance exchanges, tax rebates for small businesses, and broadened coverage from health insurers.

LO3 Describe the most common forms of paid leave.

The major categories of paid leave are vacations, holidays, and sick leave. Paid time off may seem uneconomical, which may be the reason U.S. employers tend to offer much less vacation time than is common in Western Europe. At large U.S. companies, paid vacation is typically 10 days. The typical number of paid holidays is 10 in both Western Europe and the United States. Sick leave programs often provide full salary replacement for

a limited period of time, with the amount of sick leave usually based on length of service. Policies are needed to determine how the organization will handle unused sick days at the end of each year. Some organizations let employees roll over some or all of the unused sick days into the next year, and others let unused days expire at the end of the year. Other forms of paid leave include personal days and floating holidays.

LO4 Identify the kinds of insurance benefits offered by employers.

Medical insurance is one of the most valued employee benefits. Such policies typically cover hospital expenses, surgical expenses, and visits to physicians. Some employers offer additional coverage, such as dental care, vision care, birthing centers, and prescription drug programs. Under the Consolidated Omnibus Budget Reconciliation Act of 1985, employees must be permitted to extend their health insurance coverage at group rates for up to 36 months after they leave the organization. To manage the costs of health insurance, many organizations offer coverage through a health maintenance organization or preferred provider organization, or they may offer flexible spending accounts. Some encourage healthy behaviors through an employee wellness program. Life insurance usually takes the form of group term life insurance, with the usual benefit being two times the employee's yearly pay. Employers may also offer short-term and/or long-term disability insurance, with disability payments being a percentage of the employee's salary. Some employers provide long-term care insurance to pay the costs associated with long-term care such as nursing home care.

LO5 Define the types of retirement plans offered by employers.

Retirement plans may be contributory, meaning funded by contributions from employer and employee, or noncontributory, meaning funded only by the employer. These plans may be defined-benefit plans, which guarantee a specified level of retirement income, usually based on the employee's years of service, age, and earnings level. Benefits under these plans are protected by the Pension Benefit Guarantee Corporation. An alternative is to set up a defined-contribution plan, such as a 401(k) plan. The employer sets up an individual account for each employee and guarantees the size of the investment into that account, rather than the amount to be paid out on retirement. Because employees have control over investment decisions, the organization may also offer financial planning

services as an employee benefit. A cash balance plan combines some advantages of defined-benefit plans and defined-contribution plans. The employer sets up individual accounts and contributes a percentage of each employee's salary. The account earns interest at a predetermined rate, so the contributions and benefits are easier to predict.

LO6 Describe how organizations use other benefits to match employees' wants and needs.

Employers have responded to work-family role conflicts by offering family-friendly benefits, including paid family leave, child care services or referrals, college savings plans, and elder care information and support. Other employee benefits have traditionally included subsidized cafeterias, on-site health clinics, and reimbursement of moving expenses. Stores and manufacturers may offer discounts on their products. Tuition reimbursement encourages employees to continue learning. Recreational services and employee outings provide social interaction as well as stress relief.

LO7 Explain how to choose the contents of an employee benefits package.

A logical place to begin is to establish organizational objectives and select benefits that support those objectives. Organizations should also consider employees' expectations and values. At a minimum, organizations offer the benefits employees have come to view as basic; some organizations go so far as to match extra benefits to individual employees' needs and interests. Cafeteria-style plans are an intermediate step that gives employees control over the benefits they receive. Employers must also weigh the costs of benefits, which are significant.

LO8 Summarize the regulations affecting how employers design and administer benefits programs.

Employers must provide the benefits that are required by law, and they may not improperly classify employees as "independent contractors" to avoid paying benefits. Tax treatment of qualified plans is favorable, so organizations need to learn the requirements for setting up benefits as qualified plans—for example, ensuring that pension plans do not discriminate in favor of the organization's highly compensated employees. Employers may not use employees' gender as the basis for discriminating against anyone, as in pension benefits on the basis that women as a group may live longer. Nor may employers discriminate against workers over age 40 in providing pay or benefits, such as pressuring older workers to retire by limiting retirement benefits.

When employers offer early retirement, they must meet the requirements of the Older Workers Benefit Protection Act of 1990. Under the Americans with Disabilities Act, employers must give disabled employees equal access to health insurance. To meet the requirements of the Financial Accounting Standards Board, employers must set aside the funds they expect to need for retirement benefits ahead of time, rather than funding the benefits on a pay-as-you-go basis.

LO9 Discuss the importance of effectively communicating the nature and value of benefits to employees.

Communicating information about benefits is important so that employees will appreciate the value of their benefits. Communicating their value is the main way benefits attract, motivate, and retain employees. Employers have many options for communicating information about benefits, such as brochures, meetings, intranets, memos, and e-mail. Using a combination of such methods increases employees' understanding.

KEY TERMS

cafeteria-style plan, p. 406
 cash balance plan, p. 400
 Consolidated Omnibus Budget Reconciliation Act (COBRA), p. 394
 contributory plan, p. 398
 defined-benefit plan, p. 398
 defined-contribution plan, p. 398
 employee benefits, p. 383
 Employee Retirement Income Security Act (ERISA), p. 398

employee wellness program (EWP), p. 396
 experience rating, p. 388
 Family and Medical Leave Act (FMLA), p. 389
 flexible spending account, p. 395
 health maintenance organization (HMO), p. 395
 long-term disability insurance, p. 396
 noncontributory plan, p. 398
 Patient Protection and Affordable Care Act, p. 390

Pension Benefit Guarantee Corporation (PBGC), p. 398
 preferred provider organization (PPO), p. 395
 short-term disability insurance, p. 396
 Social Security, p. 387
 summary plan description (SPD), p. 401
 unemployment insurance, p. 387
 vesting rights, p. 401
 workers' compensation, p. 388

REVIEW AND DISCUSSION QUESTIONS

- Why do employers provide employee benefits, rather than providing all compensation in the form of pay and letting employees buy the services they want?
- Of the benefits discussed in this chapter, list the ones you consider essential—that is, the benefits you would require in any job offer. Why are these benefits important to you?
- Define the types of benefits required by law. How can organizations minimize the cost of these benefits while complying with the relevant laws?
- What are some advantages of offering a generous package of insurance benefits? What are some drawbacks of generous insurance benefits?
- Imagine that you are the human resource manager of a small architectural firm. You learn that the monthly premiums for the company's existing health insurance policy will rise by 15 percent next year. What can you suggest to help your company manage this rising cost?
- In principle, health insurance would be most attractive to employees with large medical expenses, and retirement benefits would be most attractive to older employees. What else might a company include in its benefits package to appeal to young, healthy employees? How might the company structure its benefits so these employees can take advantage of the benefits they care about most?
- What issues should an organization consider in selecting a package of employee benefits? How should an employer manage the trade-offs among these considerations?
- How do tax laws and accounting regulations affect benefits packages?
- What legal requirements might apply to a family leave policy? Suggest how this type of policy should be set up to meet those requirements.
- Why is it important to communicate information about employee benefits? Suppose you work in the HR department of a company that has decided to add new benefits—dental and vision insurance plus an additional two days of paid time off for “personal days.” How would you recommend communicating this change? What information should your messages include?

BUSINESSWEEK CASE

BusinessWeek GE Gets Radical with Health Benefits

It's been a hard year to work at General Electric. Salary freezes have hit its famously performance-driven employees, with some managers taking pay cuts. The price of GE stock, which once made millionaires out of even hourly workers, has gone nowhere as the rest of the market has risen. A 68 percent dividend cut—the first in 71 years—has stung execs who rely on a heavy dose of restricted shares.

And now GE is making changes that could deal another blow to morale. The company is forcing 75,000 salaried U.S. employees and 8,000 retirees under the age of 65 to choose what's known as a consumer-directed health plan, which includes deductibles that run as high as \$4,000 a year. Traditional plans, where employees pay higher premiums in exchange for predictable co-pays up front, are no longer available for salaried workers. One employee says his colleagues "are looking at this as a cut in pay."

GE says the plan is being rolled out to make employees better health-care consumers and to coincide with its new "Healthymagination" strategy, a companywide initiative for health-care innovation. While GE says its future cost savings are unclear, people with knowledge of the situation estimate it could save \$1 billion over the next decade or so. With three tiers of premiums and deductibles, GE spokesperson Sue Bishop notes, employees still have options. "It's not that different from their car insurance," she says. "You get to choose the amount of your premium, and that determines the amount of your deductible."

The total cost of care will depend, of course, on the individual. Consumer-driven plans can save money for healthy workers who rarely visit a doctor or shop around. Typically, employees have lower premiums and save pre-tax dollars in health-savings accounts to pay much higher

deductibles, with companies providing contributions to offset expenses. (GE will fund up to \$1,000 for two of the three tiers.) While GE's plans offer free preventive care, for the first time, it's making smokers pay an extra \$625 a year.

Workplace experts say that while many companies are adopting consumer-directed plans—about half now offer one, according to consultancy Watson Wyatt Worldwide—most offer them as part of a broader menu. Wharton School professor Peter Cappelli argues that this isn't the year to be piling big changes on an already battered employee base. "There's the death-by-a-thousand-cuts issue," he says. Veteran recruiter Peter Crist adds that the health-care change could add to the grousing he hears from GE executives. "At the high end, it's not just the money," says Crist. "It's the aggravation."

Indeed, there are indications that many are anxious about their new benefits, even if they can take comfort in knowing GE's salary freeze will lift in 2010. Some are overwhelmed by the complexity of the new plans. GE is offering Web tools, town halls, and coaches to help. But James N. Cawse, a former staff scientist at GE Global Research, says: "I'm a statistical analysis guy and I finally had to draw up a spreadsheet to make any sense of it."

SOURCE: Reprinted from Jena McGregor, "Health Care: GE Gets Radical," *BusinessWeek*, November 19, 2009, www.businessweek.com.

Questions

1. Based on the discussion of health plans in the text and the description in this case, why do you think GE wanted to move all employees into consumer-driven health plans?
2. What are the risks of this change? How can GE decide whether those risks are worth taking?
3. What aspects of the plans would you expect employees to be worried or upset about? How could human resource management address those concerns?

Case: Employees Gobble Up the Benefits at General Mills

Number one on *Fortune's* 2009 list of Best Companies to Work For. Voted by its employees as among the top five on Glassdoor.com's Best Places to Work. Placing on *Working Mother's* list of 100 Best Companies and among the top five of its Best Companies for Multicultural Women. And finally, number one on *Computerworld's* 2009 list of the 100 Best Places to Work in IT.

With all that praise, General Mills must be doing something right by its employees. And much of what people are talking about involves employee benefits at the

company, whose products include Yoplait yogurt and Progresso soup.

Some of the benefits are flashy: the company's headquarters near Minneapolis boasts an on-site health clinic, fitness center, auto service center, and grocery, plus a concierge service to run errands for employees at the low cost of \$6. Other benefits are practical for busy employees: flex-time, on-site infant care, and backup child care. Use of the infant day care is subsidized by the company. Still others are ideal for those with career ambitions: employees

can take an educational leave for up to two years with tuition reimbursement or (in the case of R&D employees) an “innovation sabbatical” of up to six months of paid time to do research in their field.

General Mills sees the benefits as more than frills. According to the company’s senior vice president of global human resources, Mike Davis, a flexible but challenging workplace “is critically tied to attracting and retaining top talent, driving innovation and, ultimately, connecting with customers around the world.” Chief executive Ken Powell agrees, explaining that the company seeks to build a culture that is “performance-driven, where people work hard to achieve goals and are excited by the challenges of their jobs” but do not “lose sight of family and community”—a balance that, Powell says, helps the company keep “the best talent.”

The benefits also are not simply a way to buy loyalty. The company’s leaders see benefits as one expression of a company that cares about its people. Speaking of the intangible ways the company lives these values, Ken Charles, vice president of diversity and inclusion, says, “Inclusion is free, respect is free, having a manager who listens is free.” One benefits objective, Charles explains, is to keep employees on board “for 35 years.” Turnover among employees in the Twin Cities facilities is just 3 percent.

One of those dedicated employees is Karla Juarez, who joined General Mills as an intern earning a degree in computer science and stayed with the company, tackling one challenging assignment after another. Juarez told

Computerworld, “General Mills has done a good job of wanting to keep me here and given me enough support and benefits that I want to do just that.” For information technology workers like Juarez, though (and perhaps for many of its other great people), what they appreciate most is not the fitness center, but rather the chance to do interesting work in a challenging environment with other talented people.

SOURCES: Suzanne Ziegler, “General Mills Is a Place Employees Come to Stay,” *Minneapolis Star Tribune*, May 10, 2009, Business & Company Resource Center, <http://galenet.galegroup.com>; “Mayo Clinic, General Mills Make *Fortune’s* ‘Best’ List,” *HR Specialist: Minnesota Employment Law*, April 2010, Business & Company Resource Center, <http://galenet.galegroup.com>; “Glassdoor.com Unveils Employees’ Choice Award for Top 50 Best Places to Work for 2010,” *Internet Wire*, December 16, 2009, Business & Company Resource Center, <http://galenet.galegroup.com>; “Working Mother 100 Best Companies 2009” and “Best Companies for Multicultural Women,” *Working Mother*, www.workingmother.com, accessed April 29, 2010; and Julia King, “No. 1: General Mills, ‘Company of Champions,’” *Computerworld*, June 8–15, 2009, pp. 24–25.

Questions

1. What employee benefits that are *not* described in this case would you expect to be important to employees at General Mills? Why do you think they aren’t mentioned?
2. What evidence can you find in this case that benefits at General Mills are tied to benefits objectives and corporate objectives?
3. How can General Mills ensure that its benefits are not just luxurious expenses but also contribute to business success?



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Review

- Chapter learning objectives

Application

- Video case and quiz: “Child Care Help”
- Self-Assessment: Will you find a job that offers the benefits you want?
- Web Exercise: Evaluate a company that helps businesses to set up intranets
- Small-business case: Babies Welcome at T3

Practice

- Chapter quiz

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