Employee Benefits

Ninth Edition

Burton T. Beam, Jr., and John J. McFadden

with Karen Stefano, Contributing Editor

Employee Benefits

NINTH EDITION

BURTON T. BEAM, JR., AND JOHN J. MCFADDEN,
WITH KAREN STEFANO, CONTRIBUTING EDITOR

Dearborn™
A Kaplan Real Estate Education Company

President: Dr. Andrew Temte
Chief Learning Officer: Dr. Tim Smaby
Vice President, Real Estate Education: Asha Alsobrooks
Development Editor: Julia Marti

EMPLOYEE BENEFITS NINTH EDITION

Published by DF Institute, Inc., d/b/a Dearborn Real Estate Education
332 Front St. S., Suite 501
La Crosse, WI 54601
www.dearborn.com

Printed in the United States of America
11 12 13 10 9 8 7 6 5 4 3 2 1
ISBN: 978-1-4277-3564-5 / 1-4277-3564-6
PPN: 4106-4609

CONTENTS

PART TWO

Social Insurance

PART THREE

Group Benefits

PREFACE

Over the past three decades, few fields have changed as dramatically as that of employee benefits. Employers are spending an increasing portion of total compensation dollars on benefit plans. Some of this increased spending is a result of new or expanded benefits being offered. However, a significant portion of the increase is related to the costs of certain benefits, such as medical expense coverage, which are rising at a faster rate than wages. This spiraling cost has made employers more focused on containing benefit costs.

Legislation has also had a significant effect on employee benefit plans, causing employers to continually monitor and often to revise their plans. For example, the impact of the Employee Retirement Income Security Act of 1974 (ERISA) and subsequent legislation continually alters the area of pensions. The Age Discrimination in Employment Act resulted in benefits being provided to persons who previously had coverages terminated at a certain age, such as 65, and the Health Insurance Portability and Accountability Act of 1996 has greatly changed the area of medical expense insurance. The Affordable Care Act of 2010 also calls for sweeping changes to be implemented over the course of several years. In addition, the states continue to mandate the types of benefits that employees must be provided.

The federal tax treatment of employee benefit plans also has had a particularly significant impact on employee benefit plans. Certain types of plans, such as medical expense plans and qualified retirement plans, owe their popularity in large part to federal tax advantages. Cafeteria plans, consumer-directed health plans, and Section 401(k) cash or deferred plans have become more widespread largely because of legislative clarification of their tax treatment. Because the tax benefits for employee benefit plans result in a substantial annual loss of federal tax revenues, Congress has imposed an elaborate and ever-changing scheme of regulation on these plans. The information in this text reflects current law through late 2011.

This changing environment and the resultant need for up-to-date materials was one reason for the first edition of this book and remains a major consideration in this latest edition.

Nowhere have the changes occurred any faster than in the area of medical expense coverage. Managed care plans have, by far, become the dominant method of providing medical expense coverage to employees. However, this has led to a consumer backlash and concern over the quality of care. There has been considerable reaction to this backlash at the state level and through voluntary changes adopted by managed care plans. Debate on the issue continues at the federal level. Employers have also reacted by requiring accreditation of the managed care plans they offer their employees.

Within the managed care arena, there have also been significant changes as plans continue to evolve. Concerns about restrictions on the ability of patients to select their own providers have led to the continued growth of preferred-provider arrangements and point-of-service plans at the expense of health maintenance organizations (HMOs).

All types of medical expense plans are more likely to provide an array of benefits for alternatives to traditional medicine. In addition, the use of carve-outs for benefits, such as prescription drugs and disease management, continues to grow.

Finally, considerable interest is being shown in consumer-directed health plans by both employees and employers. Such plans, at least in theory, give employees an incentive to control medical care expenditures.

Other changes in this edition include the following:

- Added and modified examples
- Updated and added links to Web sites
- Current important statistics and indexed numbers
- Addition of public policy coverage
- An updated and revised chapter on Social Security and Medicare
- Added coverage on challenges facing global employers
- Revised pension material to reflect current law through late 2011

We have continued to use four other major guidelines in preparing this book. First, the book covers the broad spectrum of employee benefits, from social insurance programs to executive benefits. Second, the book is applicable to all sizes of employer groups, from the small employer using a multiple-employer trust to the large employer relying on alternative funding methods, including self-insurance. Third, the book explains the decisions involved in designing an employee benefit plan; it doesn't just describe the products available. Finally, we have tried to write a book that can be used not only in courses given by colleges and professional organizations but also as a reference resource for practitioners.

We have also tried to write a book that can be flexible for classroom use. If students have had other insurance courses, perhaps the material on social insurance can be eliminated. Depending on the length of the course and students' backgrounds, the detailed material on group insurance taxation and rate making might be skipped or covered superficially. In the retirement plan part, Chapters 26, 27, and possibly 28 might also be omitted. Furthermore, the material on retirement plans could also logically be taught before the material on group insurance and other welfare benefits.

It was difficult to decide where we should place the chapter on employee benefit planning and management. On the one hand, readers should be aware of the importance of planning and management issues before they pursue the material further. On the other hand, they will probably better understand the issues after they are familiar with the benefit environment and the products and services that exist in this environment. We recommend that the principles of the chapter not be ignored after an initial reading.

The chapter is an important one that should be reviewed again after the remainder of the book is read.

The changing nature of employee benefits makes it essential to remain up to date. For this reason, we have included a list of additional resources, including Web sites. We particularly urge readers to become familiar with the loose-leaf services, periodicals, and Web sites mentioned.

LEGAL REFERENCES IN THIS TEXT

This text occasionally cites legal authorities to help in finding further information about the subject, if the reader wishes. The term *the Code* refers to the Internal Revenue Code and *the regulations* refers to the Treasury Regulations, with other citations given more fully. *ERISA Section 000* refers to the indicated section of the Employee Retirement Income Security Act of 1974.

No attempt is made to provide a complete citation of authorities for all the propositions set forth. However, the general discussion in this text should be adequate to enable the interested reader to obtain citations of the necessary legal authorities from one of the loose-leaf qualified plan or tax services or one of the handbooks in the field of qualified plans. If accurate legal references are to be obtained, it is important to have thorough and up-to-date materials because the legal authorities are voluminous and subject to frequent change.

ACKNOWLEDGMENTS

As with any undertaking of this scope, we are grateful to the many persons who have helped make this book a reality, from those who were immensely helpful in preparing the first edition to those who have offered valuable suggestions for its revisions.

We would like to thank the following reviewers for their contributions to the ninth edition: Lawrence W. Kustra, Esq., and H. Kristl Davison.

Finally, we wish to acknowledge The American College, Bryn Mawr, Pennsylvania, for giving us permission to use the copyrighted material previously written by Burton T. Beam Jr. and contained in *Group Benefits: Basic Concepts and Alternatives*, 11th edition (Copyright © 2006, The American College Press).

We like to hear from our readers. You, along with the real estate professionals who have helped develop this edition, are partners in the real estate education process. Please e-mail us comments about this text at *contentinquiries@dearborn.com*.

Burton T. Beam Jr.
John J. McFadden

PART ONE

Introduction

CHAPTER 1

Introduction to Employee Benefits

OBJECTIVES

- Explain the meaning of the term *employee benefits*.
- Explain the significance of employee benefits in terms of both employer cost and benefits provided to employees.
- Identify the factors that have influenced the growth of employee benefits and explain the significance of each factor.
- Explain how public policy issues affect employee benefits.
- Identify the employee benefit trends that are likely to occur in the near future.
- Identify the job opportunities available in the field of employee benefits.

CHAPTER OUTLINE

Definition of Employee Benefits

Book Overview

Significance of Employee Benefits
- U.S. Chamber of Commerce
- LIMRA International
- Bureau of Labor Statistics

Factors Influencing the Growth of Employee Benefits
- Industrialization
- Organized Labor
- Wage Controls
- Cost Advantages
- Inflation
- Legislation

Public Policy Issues

The Future

Opportunities in Employee Benefits

Web Sites and Other Additional Resources

In the early part of the 20th century, very few employees received any compensation from their employers, other than direct wages for time actually worked. Employees or their families were responsible for meeting the needs of old age, poor health, and death. Vacations, if allowed at all, were usually without pay.

The 1940s and 1950s witnessed the increasing use and acceptance of employee benefits as a form of compensation in addition to direct wages. During the past three decades, this growth accelerated as new types of benefits were added and existing benefits expanded. Further, while employee benefits were once fairly standardized and free of government regulations, employers must now make more complex decisions regarding the benefits to be provided and the methods by which these benefits are funded.

DEFINITION OF EMPLOYEE BENEFITS

Before continuing, it is best to define exactly what is meant by **employee benefits**. The narrowest definition of employee benefits includes only employer-provided benefits for situations involving death, accident, sickness, retirement, or unemployment. Even this narrow interpretation produces disagreement over whether the definition should include benefits that are financed by employer contributions but provided under social insurance programs, such as workers' compensation insurance, unemployment insurance, Social Security, and Medicare.[1]

On the other hand, the broadest definition of employee benefits includes all benefits and services, other than wages for time worked, that employees receive in whole or in part from their employers. This book uses a broad definition and defines employee benefits as including the following five categories:[2]

1. Legally required payments for government programs—These include employer contributions to such programs as the following:
   - Social Security
   - Medicare
   - Unemployment compensation insurance
   - Workers' compensation insurance
   - Temporary disability insurance
2. Payments for private insurance and retirement plans—These include the cost of establishing such plans, as well as contributions in the form of insurance premiums or payments through alternative funding arrangements. Benefits are provided under these plans for personal loss exposures, for example:
   - Old age
   - Death
   - Disability
   - Long-term care expenses
   - Medical expenses
   - Dental expenses

   - Legal expenses
   - Property and liability losses
3. Payments or other benefits for time not worked—These include the following:
   - Vacations
   - Holidays
   - Jury duty
   - Maternity/paternity leave
   - Reserve/National Guard duty
   - Military leave
4. Extra cash payments, other than wages and bonuses based on performance, to employees—Benefits in this category may include the following:
   - Educational assistance
   - Moving expenses
   - Suggestion awards
   - Christmas bonuses
5. Cost of services to employees—These include the following examples:
   - Subsidized cafeterias
   - Employee discounts
   - Wellness programs
   - Employee-assistance programs
   - Day care
   - Adoption assistance
   - Financial planning programs
   - Retirement counseling
   - Free parking

BOOK OVERVIEW

The first category previously mentioned is usually called **social insurance** and is covered in Part Two of this book. The remaining categories are commonly called **group benefits** and consist of group insurance, other nonretirement benefits, and retirement benefits. The legal term often applied to group insurance and other nonretirement benefits is **welfare benefits**. Group insurance benefits are discussed in Part Three and other nonretirement benefits are covered in Part Four. Part Five is devoted to a discussion of retirement benefits.

SIGNIFICANCE OF EMPLOYEE BENEFITS

Some often-quoted data of the U.S. Chamber of Commerce, LIMRA International, and the Bureau of Labor Statistics can best show the significance of employee benefits. These data come from surveys conducted by the three organizations and are periodically updated. It often takes a year or more to collect and tabulate these statistics, and the data shown are for the latest survey years available at the time this book was revised.

U.S. Chamber of Commerce

In a 2008 study of 265 companies that employed the full-time equivalent of 426,383 employees, the U.S. Chamber of Commerce found that the average payment by employers for employee benefits was equal to 29.2 percent of payroll. However, benefits varied significantly among companies. For example, 10 percent of participating companies paid more than 51.7 percent of payroll in benefits, while an equal percentage paid less than 15.9 percent.[3] Of the 29.2 percent figure, 7.4 percent of payroll went for the employer's share of legally required social insurance payments, 6.5 percent for payments to private retirement and savings plans, and 8.6 percent for medical and medically related benefits. Within specific industries, benefit percentages tend to be higher for firms with 100 employees or more than for firms with fewer than 100 employees, and nonmanufacturing firms have slightly higher percentages than do manufacturing firms. The percentages also vary by geographic region. Metropolitan areas spent more than $3,300 per employee for medical payments and more than $3,500 for retirement payments than companies in nonmetropolitan areas. Stated in dollars, the Chamber of Commerce study showed that employees received an average of $14,919 in benefits in addition to wages.

The complete Chamber of Commerce study can often be found in libraries or at local chambers of commerce. It can also be ordered on the U.S. Chamber of Commerce's Web site: *www.uschamber.com*.

LIMRA International

LIMRA International is a membership organization of life insurance and financial services organizations that provides marketing and distribution information and advice to its more than 850 members. The data it gathers and the reports it issues can be found on its Web site: *www.limra.com*. However, much of its data is proprietary and can be accessed by members only.

Bureau of Labor Statistics

The Bureau of Labor Statistics is part of the U.S. Department of Labor and maintains many databases for the department. Periodically, the bureau publishes detailed information on the wages, earnings, and benefits of workers. The latest information from the bureau is on its Web site: *www.bls.gov*.

TABLE 1.1 Percentage of Workers Participating in Life and Disability Income Insurance, by Selected Characteristics, Private Industry[4]

Characteristics	Life	Disability Benefits	
		Short-Term Disability	Long-Term Disability
All employees	56	38	31
Worker Characteristics			
White-collar occupations	76	51	56
Service occupations	31	21	12
Full time	71	46	40
Part time	13	15	6
Union	81	64	35
Nonunion	54	35	31
Lowest 25% of average wage	24	17	7
Highest 25% of average wage	80	58	57
Establishment Characteristics			
Goods-producing	70	51	33
Service-producing	54	35	31
1–99 workers	40	26	20
100 workers or more	75	52	44
Geographic Areas			
New England	57	39	36
Middle Atlantic	55	72	31
East North Central	61	41	33
West North Central	59	31	30
South Atlantic	58	33	32
East South Central	61	34	35
West South Central	54	28	32
Mountain	55	27	27
Pacific	51	26	27

A survey, conducted in 2010, obtained data from approximately 9,000 private industry establishments, representing nearly 99 million workers. Table 1.1 shows the percentages of employees participating in life and disability income plans. Before viewing these statistics, note that they are for employees who participate in these plans. The number of employees who work for employers that provide such benefits plans to at least some employees is much higher. For example, a LIMRA International study indicated that almost all employers with 100 or more employees offer medical expense and life insurance benefits to employees. There are several reasons for this difference.

Many employees may not meet the eligibility requirements for plan benefits. For example, eligibility for long-term disability income benefits may require a minimum length of service, full-time status, and income above a certain amount. In addition, when employees are required to pay all or a portion of the cost of a benefit, they may decline the benefit because they cannot afford it or because they see little value in it. For example, young employees with no dependents may decline life insurance coverage.

Table 1.2 shows the percentage of employees participating in medical expense plans. What some observers view as disturbing about these statistics is that the number of employees participating in medical expense plans is only 51 percent. This percentage has dropped over the past ten years. A large number of persons who do not have

TABLE 1.2 Percentage of Workers Participating in Medical Expense Plans, by Selected Characteristics, Private Industry[5]

Characteristics	Medical Care	Dental Care	Vision Care
All employees	51	36	20
Worker Characteristics			
White-collar occupations	66	50	28
Service occupations	27	19	11
Full time	64	44	25
Part time	14	10	6
Union	77	63	47
Nonunion	48	33	17
Lowest 25% of average wage	22	13	8
Highest 25% of average wage	72	56	33
Establishment Characteristics			
Goods-producing	69	47	28
Service-producing	48	34	19
1–99 workers	42	23	13
100 workers or more	63	51	28
Geographic Areas			
New England	49	41	17
Middle Atlantic	53	37	24
East North Central	53	36	17
West North Central	52	37	15
South Atlantic	49	32	17
East South Central	55	37	26
West South Central	47	29	15
Mountain	49	33	21
Pacific	55	43	29

coverage from their own employer have coverage as a dependent under a spouse's or parent's plan. However, many persons are not eligible for benefits, usually because they work part time. In addition, many low-paid workers fail to elect coverage because they cannot afford the required employee contributions. For both these reasons, the number of Americans who are uninsured for medical expenses continues to grow.

Tables 1.3 and 1.4 show the percentages of workers who have access to other selected nonretirement benefits. With the exception of long-term care insurance, these benefits are typically provided to eligible employees without any employee cost sharing. In the case of long-term care insurance, employees usually pay all or most of the premium cost for benefits.

TABLE 1.3 Percentage of Workers with Access to Selected Benefits, by Selected Characteristics, Private Industry[6]

Characteristics	**Paid Holidays**	**Paid Vacations**	**Paid Jury Duty Leave**
All employees	78	77	68
Worker Characteristics			
White-collar occupations	89	87	85
Service occupations	54	59	49
Full time	90	91	77
Part time	40	37	42
Union	88	87	85
Nonunion	76	76	66
Lowest 25% of average wage	52	53	54
Highest 25% of average wage	89	89	85
Establishment Characteristics			
Goods-producing	88	88	70
Service-producing	75	75	68
1–99 workers	70	70	57
100 workers or more	87	85	82
Geographic Areas			
New England	76	75	80
Middle Atlantic	80	77	78
East North Central	79	78	69
West North Central	75	76	66
South Atlantic	78	79	69
East South Central	79	77	69
West South Central	80	78	65
Mountain	75	77	62
Pacific	75	76	59

TABLE 1.4 Percentage of Workers with Access to Selected Benefits, by Selected Characteristics, Private Industry[7]

Characteristics	Child Care Assistance	Long-Term Care Insurance	Subsidized Commuting
All employees	9	14	5
Worker Characteristics			
White-collar occupations	18	24	11
Service occupations	9	6	2
Full time	11	16	7
Part time	6	9	2
Union	14	20	6
Nonunion	9	14	5
Lowest 25% of average wage	5	6	1
Highest 25% of average wage	17	27	9
Establishment Characteristics			
Goods-producing	7	10	2
Service-producing	10	15	6
1–99 workers	4	6	3
100 workers or more	16	24	9
Geographic Areas			
New England	9	14	9
Middle Atlantic	9	14	6
East North Central	11	15	4
West North Central	8	12	5
South Atlantic	9	17	4
East South Central	0	14	2
West South Central	9	14	7
Mountain	8	14	7
Pacific	10	13	9

In the case of long-term care insurance, employees usually pay all or most of the premium cost for the benefit.

Table 1.5 shows the percentage of workers who participate in retirement plans. Note that the percentage for all plans is less than the sum of the percentages for defined-benefit plans and defined-contribution plans. The discrepancy occurs because some employers have both types of plans.

TABLE 1.5 Percentage of Workers Participating in Retirement Plans, by Selected Characteristics, Private Industry[8]

Characteristics	All Plans	Defined Benefit	Defined Contribution
All employees	50	19	41
Worker Characteristics			
White-collar occupations	68	25	60
Service occupations	23	7	18
Full time	59	22	50
Part time	21	8	15
Union	82	67	44
Nonunion	46	13	41
Lowest 25% of average wage	20	5	17
Highest 25% of average wage	75	36	62
Establishment Characteristics			
Goods-producing	60	28	49
Service-producing	47	17	40
1–99 workers	35	9	31
100 workers or more	66	30	54
Geographic Areas			
New England	50	20	43
Middle Atlantic	56	24	44
East North Central	52	22	42
West North Central	54	18	46
South Atlantic	47	15	38
East South Central	45	15	38
West South Central	44	14	39
Mountain	49	16	42
Pacific	47	20	38

FACTORS INFLUENCING THE GROWTH OF EMPLOYEE BENEFITS

No single factor can be identified as the reason for the substantial growth in employee benefits over time. Rather, this growth has resulted from a combination of elements, many of which are applicable to employee benefits in general. Frequently mentioned factors include the following:

- Industrialization
- The influence of organized labor

- Wage controls
- Cost advantages
- Inflation
- State and federal legislation

Industrialization

During the 19th century, the United States made the transition from an agrarian economy to one characterized by increasing industrialization and urbanization. The economic consequences of death, sickness, accidents, and old age became more significant as individuals began to depend more on monetary wages than on self-reliance and family ties to meet their basic needs. As a result, some employers began to provide retirement, death, and medical benefits to their employees. Although benevolence might have influenced the decision to provide such benefits, the principal reason was probably the employers' realization that it was in their own best interest to do so.

Not only did such benefits improve morale and productivity, they also reduced employee turnover and the expenses associated with it.

Although some earlier benefits were paid directly by employers, the development of group insurance enabled these benefits to be funded by systematic payments to an insurance company. As group insurance became more common, employers were faced with adopting new or better plans to remain competitive in attracting and keeping employees. This competition in employee benefits still exists.

Industrialization has also led to more government benefits, such as Social Security, Medicare, unemployment insurance, and workers' compensation insurance.

Organized Labor

Since a Supreme Court ruling in 1949, the right of labor unions to legally negotiate for employee benefits is unquestioned. Although union pressures before that time often resulted in the establishment or broadening of employee benefit plans, this ruling strengthened the influence of labor unions.

Labor unions have also affected benefits for nonunion employees because some employers provide generous benefit plans in an effort to discourage their employees from unionizing. In addition, employers with both union and nonunion employees often provide the same benefits for the nonunion employees as those stipulated in the union contracts.

Wage Controls

Employee benefit plans grew substantially during World War II and the Korean War. Although wages were frozen, no restrictions were imposed on employee benefits, thus making them an important factor in attracting and retaining employees in labor markets with little unemployment. When these conflicts ended, the new and enhanced benefits remained.

Cost Advantages

Because of the economies associated with group underwriting and administration, benefits can usually be obtained at a lower cost through group insurance rather than through separate policies purchased by individual employees. Similar savings can be realized by directly providing employees with certain services, such as financial planning, day care centers, and subsidized meals. The Internal Revenue Code also provides favorable tax treatment to employer contributions for certain types of group benefits. The employer may deduct most group benefit contributions as usual business expenses, and employees often have no taxable income as a result of employer contributions on their behalf. In addition, employees may receive tax-free benefits from certain types of group benefit plans and payments or services from many other types of group benefit programs, even if provided by employer contributions. However, there are often **nondiscrimination rules** that deny favorable tax treatment to some employees if the benefit plan does not provide equitable benefits to a large cross section of employees.

The extent of the favorable tax treatment applicable to group benefits is discussed in detail in later chapters. Nevertheless, it should be noted here that the types of group benefits with the most favorable tax treatment also tend to be the most prevalent.

Inflation

Inflation also affects group benefits. When benefit levels are related to employees' wages, the level and cost of these benefits increase as wages increase; when benefit levels are stated as fixed amounts, inflation results in employee pressure for increases. For most employers, the cost of group benefits has increased at a rate faster than wages, primarily because of the skyrocketing increase in the cost of providing medical expense benefits.

Legislation

Most states traditionally limited the types of groups that were eligible for group insurance coverage as well as the types, and in some cases the amounts, of coverage that could be written. Most of these states have liberalized their laws and allowed more group insurance products to be available to a greater variety of groups.

Furthermore, the federal government and many states have passed legislation mandating that certain benefits be included in group insurance contracts or that existing benefits be broadened. Examples include legislation requiring benefits for maternity, alcoholism, and drug abuse. These added benefits have also increased the cost of providing group insurance coverage.

Other benefits, such as family leave, must now be provided by many employers.

PUBLIC POLICY ISSUES

In the United States, employee benefits are significantly affected by a variety of state and federal regulatory arrangements, state and federal tax benefits and incentives, and even some direct governmental expenditures. These extensive governmental influences will be discussed throughout this book. The issue in this section is to assess the public policy or set of policies behind the legislation and regulations involved here, and speculate on the direction of future policies.

Current public policy regarding employee benefits in general, both here and in the other industrialized countries, has its origins primarily in the experiences of the Great Depression of the 1930s and the broadly shared determination at the end of World War II to prevent future recurrences of the hardships endured in the prewar period. The successful mobilization of national resources to fight the war provided a great deal of optimism about governmental and private-sector planning and intervention in other types of social activity, so the provision of a financial security safety net to the population as a whole did not then seem particularly challenging or problematic.

In the United States, benefit policy has taken a distinctively different direction than it has in most other industrialized countries. In Europe and elsewhere, the thrust of public policy has been to create a system of uniform governmental benefits for retirement, health, unemployment, and similar needs. Some European countries had already pioneered the use of government-provided social insurance as early as the 1880s, as in the case of Germany. The political consensus in the 1950s was different in the United States; here, the emphasis was on creating financial security through benefits from multiple sources: the government, federal and state; private employers; and individuals. Government provides such benefits as Social Security, Medicare, Medicaid, unemployment compensation, and aid for dependent children. Private employers often provide health insurance, disability insurance, and a variety of other benefits suited to their needs, with some incentives from federal and state tax law. Individuals maintain private insurance and pay out-of-pocket costs of benefits not provided otherwise. Private charity and implicit surcharges on insurance-premium payers (for example, the coverage of unreimbursed hospitalization costs) provide whatever is not covered under this tripartite arrangement.

Both the European and U.S. approaches to pension and welfare benefits have come under significant stress in recent years. The European welfare state is beset with rising costs due to demands for increasingly generous benefits, and a decline in the number of active workers in relation to the number of retirees. Because retirees use the largest share of benefits, while active workers pay the costs of benefits through payroll taxes, this demographic situation leads to financial stress in the system.

In the United States, governmental benefits are faced with the same demographic issues. Our situation is less critical in this regard because the governmental sector provides a smaller share of benefits than Europe, and the demographic problem posed by our aging population is eased somewhat by our higher birth and immigration rates. However, the overall situation is probably no less critical because, along with the stress on government programs, there is also a gradual withdrawal of employer support for benefit programs in the United States. The decline in private benefits will likely lead to pressures for increased governmental benefits.

Reduced employer support for employee benefits basically stems from a change in the perceived and actual nature of business organizations and their leadership. In the 1950s when employee benefits were expanding greatly, the emphasis in American business was to create huge business empires (e.g., General Motors, IBM) that would last for a long time and employ hundreds of thousands of workers, for the most part for their entire working careers. The time horizon of business planners was long range. This type of business structure seemed to be well established by the 1960s and was viewed by many commentators as a natural evolution that would last forever. This business climate was very favorable to the establishment of employer-provided benefits. Federal (and most state) tax laws encouraged employer-provided benefits to the maximum degree: Employer expenditures were generally deductible when paid, while taxation of employee benefits to the employee was forgiven or deferred to retirement.

The happy and favorable business environment of the 1950s and 1960s in the United States was based on many factors, including a lack of global competition for U.S. firms. Potential competitors with advanced technology (e.g., Japan, Europe) had been physically and financially devastated by World War II and took decades to recover; but by the 1970s, they were largely recovered. In addition, global trade and business activity were hampered by the wars of the 20th century, including the Cold War between the West and the Soviet Union and China. When the Iron Curtain fell in 1989, global trade began to recover to an extent not seen since before World War I.

The fact that U.S. firms must now scramble to reduce costs in order to meet global competition does not bode well for employees in general because compensation costs are a major expenditure. In the United States, the manufacturing sector has declined proportionately to total activity because manufacturing technology can be easily exported anywhere in the world to take advantage of low wages and workforce availability. This increases the relative importance of the service sector in the U.S. economy, and compensation is particularly dominant as a business cost in the service sector. As a result, U.S. businesses are under increased pressure to reduce compensation costs in order to maintain profitability in the short-run reckoning demanded by Wall Street.

The pressure to reduce compensation costs has already had some noticeable results. The defined-benefit plan, the most generous and appropriate type of retirement plan for most workers, is in significant decline. Companies are dropping these plans because they require long-range funding (see Chapter 24), which is at odds with the emphasis on short-term results demanded by investors. In addition, even many successful companies have declining U.S. workforces, which is a problem with regard to defined-benefit plan funding.

Health care has become increasingly costly because of new drugs and medical technologies, and an aging population. Although better medical care is a social good in itself, the benefits of better medical care do not directly create a cash flow to pay for it. Health insurance and the health care sector are also plagued by a near-insoluble system of perverse incentives that increase costs by rewarding providers for medical procedures and expenditures rather than for patient health outcomes. For example, in the treatment of chronic diseases, a growing sector of medical care as the population ages, day-to-day patient care is important in order to prevent costly complications. Most health insurance plans, however, discourage visits to the doctor through deductibles, copayments, and the like. Also, health insurers tend to control costs by limiting reimbursements to physicians for this type of practice, thus reducing the number of practitioners and the availability of patient care. However, reimbursements for high-cost care of complications of chronic disease are generally substantial, providing an incentive to the medical system to focus on this high-cost sector.

Currently, most employers are following strategies to reduce their costs for health insurance provided to employees. Cost reduction generally means that a greater part of the cost of insurance premiums or benefits is passed on to employees. In an era of generally stagnant wage growth, except at the very top of the income distribution, this puts considerable pressure on family budgets. The changes occurring in employer-provided health benefits are discussed extensively in subsequent chapters.

Governmental action to address current problems has so far not been encouraging. The federal government has been cutting taxes, increasing spending, and running severe deficits since the 1990s. The corresponding growth in government debt can only make it more difficult to finance expected growth in programs like Social Security and Medicare as the population ages, much less provide financial room for the government to pick up some of the costs of benefits being shed by employers.

At the federal government level, there is tension between small-government advocates who believe that the federal government should have little or no involvement with health care or other types of employee benefits and increasing public pressures for federal government action in view of cutbacks in employer-provided benefits. The hope that individuals can provide their own health care and other benefits in the "ownership society" favored by conservatives collides with the budgetary realities of most voters. As an illustration of the magnitude of the problem, recent estimates of the annual costs of health insurance for a family of four exceed the federal minimum wage for a full-time worker. Most observers believe that solutions, if any, will be forced by circumstances and will be less satisfactory than well-reasoned, phased-in remedies. There is, however, a hopeful interest in addressing the health care problem at the state level, and useful solutions may emerge there rather than through the federal government. The alternatives in this debate are discussed extensively in Chapter 9 and other chapters.

THE FUTURE

The consensus among employee benefit specialists is that in the absence of adverse economic conditions, group benefits will continue to evolve and grow. Although agreement about the specifics of these potential changes is not unanimous, there is reasonable agreement about general trends in the near future:

- Firms with fewer than 50 employees, and especially those with fewer than 10, will continue to be a market for new benefit plans—particularly with sustained economic improvement. Many insurance companies have developed products for this market so that small firms can now obtain products that were previously available only to large employers.
- Because of increasing benefit costs, employers are more likely to add new benefits by using voluntary plans under which employees who want coverage pay the full cost of the coverage through payroll deduction.
- The cost of providing medical expense benefits will continue rising faster than the general rate of inflation. These escalating costs will present a constant challenge to employers and governments seeking to contain them.

- Employers will continue to make employees pay a greater portion of their medical expenses through consumer-directed medical expense plans and/or increased deductibles, copayments, percentage participation, or premium contributions.
- Almost all employees will have medical expense coverage provided under managed care plans such as HMOs, preferred provider organizations (PPOs), and various hybrid arrangements.
- Employers will continue to drop or reduce retiree benefits, particularly medical expense coverage.
- Defined-benefit retirement plans will continue to be replaced by defined-contribution plans.
- Benefits for domestic partners will become more common.
- There will be continued government interest in providing more secure medical expense benefits as well as in making coverage available to a greater number of workers. As will be discussed in Chapter 9, The Affordable Care Act of 2010 brings about significant changes to health care policy. The legislation is scheduled to be implemented over several years. Because the legislation remains controversial, future political shifts may bring about further change.
- More employees will have benefits provided under cafeteria plans and will be able to substantially design their own benefit programs.
- Changing demographics will lead to growth in certain benefits, such as day care centers for children and retirement planning and long-term care insurance for the aging population.
- The efforts to contain medical costs and an increasing awareness of the importance of good health bode well for the proliferation and lasting success of wellness and employee-assistance programs.
- The use of technology will increase as employers apply software and technological advances to benefit administration. Online information will increasingly be made available to employees.

OPPORTUNITIES IN EMPLOYEE BENEFITS

The authors of this book are often asked, "What opportunities are there for me?" Employee benefits is a broad discipline that offers opportunities for persons from widely diverse backgrounds. Some of these are the following:

- Marketing majors—An important activity of any employee benefit provider is the marketing of its products and services to employers. These sales activities may be performed by commissioned agents of insurance companies, representatives of employee benefit consulting firms, and salaried employees of Blue Cross and Blue Shield plans or HMOs. Marketing departments of employee benefit providers also design and implement the sales activities of their firm.

- Human resources/management majors—Human resources departments frequently have the task of communicating benefits to employees, and in many firms, they may also administer the employee benefit program.
- Finance majors—The employee benefit departments of many large employers are under the direction of the finance department. The finance department is often involved in the self-funding of benefits. Finance majors are also needed to determine investment strategies for the billions of dollars invested by retirement plans.
- Insurance majors—Many employee benefits are sold by insurance companies.
- Accounting majors—Accountants with public and private employers are often involved with employee benefit activities. Accountants in private practice are frequently in a position to advise clients about employee benefit decisions.
- Communication majors—As employee benefits become more complex and expensive, employers are demanding better communication of benefits to employees. This communication might involve in-house personnel or materials prepared by employee benefit providers or consulting firms.
- Mathematics majors—The proper pricing of employee benefit products is an important function of the actuarial departments of employee benefit providers.
- Social science majors—Many job opportunities for social science majors involve interaction with people and advising them about programs to meet their needs. Better advice can be given with an understanding of social insurance programs, wellness programs, employee-assistance programs, dependent-care assistance programs, and the like.
- Majors in medical fields—Today, it is common for medical practitioners to be employed by benefit providers engaged in managed care activities. In fact, this is one of the growth areas for registered nurses.
- Paralegals and lawyers—In-house legal teams frequently have the task of developing and administering employee benefit programs. In addition, many law firms have attorneys who specialize in employee benefits issues.

This list is merely an example of the many opportunities available in the field of employee benefits. The providers of employee benefits products and services are diverse and, like any industry, need employees from a wide range of backgrounds.

WEB SITES AND OTHER ADDITIONAL RESOURCES

Employee benefits is an extensive and complex field of study. Although this book is far more than a broad overview of the field, it is impossible to cover every topic in detail. In addition, changes are always occurring. The appendix following Chapter 29 contains a list of Web sites and other resources to assist readers who want more detail or to keep abreast of these changes. Relevant Web sites are also mentioned in this text where appropriate.

KEY TERMS

employee benefits
group benefits
nondiscrimination rules
social insurance
welfare benefits

STUDY QUESTIONS

1. Explain the different ways in which the term *employee benefits* may be defined.
2. The U.S. Chamber of Commerce estimates that the cost of employee benefit programs averages about 29.2 percent of payroll. What factors might account for a particular firm's having a percentage-of-payroll figure that deviates from the average?
3. Why is the percentage of employees participating in benefit plans often lower than the percentage of employees who are eligible to participate?
4. How has organized labor influenced the growth of employee benefit plans?
5. How does inflation affect the cost of employee benefit plans?
6. Briefly explain how favorable tax laws have contributed to the growth of many types of employee benefits.
7. How do public policy issues affect employee benefits in the United States?

NOTES

1. The Social Security Administration uses a narrow definition in its studies of employee benefit plans. Its definition includes only benefits not underwritten or paid directly by federal, state, or local governments.
2. These categories are similar to those used by the U.S. Chamber of Commerce in its broad definition of employee benefits and the Department of Labor, Bureau of Labor Statistics.
3. U.S. Chamber of Commerce, *The 2008 Employee Benefits Study*.
4. U.S. Department of Labor, Bureau of Labor Statistics, *Employee Benefits in Private Industry, 2010*, Table 17.
5. U.S. Department of Labor, Bureau of Labor Statistics, *Employee Benefits in Private Industry, 2010*, Table 9.
6. U.S. Department of Labor, Bureau of Labor Statistics, *Employee Benefits in Private Industry, 2010*, Table 32.
7. U.S. Department of Labor, Bureau of Labor Statistics, *Employee Benefits in Private Industry, 2010*, Tables 38, 40.
8. U.S. Department of Labor, Bureau of Labor Statistics, *Employee Benefits in Private Industry, 2010*, Table 2.