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Plan Design Issues: The Employee Perspective

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Moderator: WILLIAM TORRIE
Panelists: JULIE JARECKE GEBAUER
GLORIA S. LESMEISTER
Recorder: WILLIAM TORRIE

Summary: Panelists discuss the retirement income needs of employees and how those needs are being met by existing and evolving retirement programs. The discussion also addresses the risks being assumed by individual employees under various plan design scenarios and the need to educate employees about those risks.

This panel of experts provides attendees with in-depth information on plan design issues and allows ample time to ask questions on related topics.

Mr. William Torrie: This session will provide the employee perspective. We have two very good speakers. Gloria Lesmeister is from Mercer in Houston. She has been in the field for about 15 years. We also have Julie Gebauer. Julie is the practice leader of employee benefit services for TPF&C in their New York office, and she has a similar period of experience. I understand their presentation is going to come out as kind of a joint presentation; one of them will make some comments and the other will respond to the comments.

Ms. Gloria Lesmeister: You may wonder why you should care what the employee thinks, but I can tell you that it will make a difference in the success of your program, and you will be making sure that your employer gets the most bang for his or her buck. We're going to go through a national survey that was done, and go through the demographic results of that opinion survey. The analysis of data throughout the survey shows the value of the benefit that the employee perceived and how satisfied the employee was with that benefit. This gives rise to priorities that the employer should set with regard to employee benefits. Then what we're probably going to do throughout our comments is give ideas of what you can do, given those priorities.

Who has opinions? Everybody has opinions. The demographics of your workforce should be considered. One workforce might be very mature, meaning everyone is eligible for early retirement. I have a client that has more than 50% of its population eligible for early retirement. There are other populations that are very young. There are populations that are predominantly female. Your populations, as they change, are going to have different opinions about the value of benefits. In fact, two employers with the exact same program can have a different appreciation for those programs based on demographics or even just the communications, given the same demographics. One employer's program may be perceived as very valuable just because that employer communicated it effectively.

Ms. Julie Jarecke Gebauer: In my experience, I have seen employers who offer less generous benefits than another employer and get greater bang for the buck. In addition to communication, the driver behind that is the service quality. Is the service quality around benefits administration the same level that the company provides to its customers? If not, shouldn't it be? If there is a higher level service quality, the general perception of benefits is higher, based on research that has been done at Towers Perrin.

Two other factors are visibility and portability, which we'll talk about as we go through this, especially around the retirement program. Portability often means more to employees than the actual dollars that are in their hands. We actually did some research at a major financial institution here in New York, and employees voted that they wanted to have a lump sum in their pension plan, and they'd take lower benefits so they could have access to their money, rather than have a higher benefit. In addition to looking at employee satisfaction, which is an important driver, another real important driver is employees' commitment to help a company succeed. We sort of say, here in New York, that employees always have something to be dissatisfied about. If you're really looking for high satisfaction, you might not get the levels you want. Another measure would be, does this program that you're developing support the human resources (HR) strategy well enough to help sustain and increase employees' commitment to help the organization succeed?

Ms. Lesmeister: The basis for the opinions we will discuss were taken from Godwins, Booke & Dickenson's "Can Meeting Employee Needs Improve the Bottom Line?," which appeared in the 1995–96 National Survey of Life Stage Needs. The employers are going to wonder why you want to survey the employees and what they're going to get out of it. This was done by telephone interviews with 1,000 randomly selected employees across the U.S. They had a very good selection of age, gender was 50/50, and service ranged from very low service to high service individuals. There were part-time and full-time workers. They did have a requirement that everyone work at least 20 hours a week and be over 18 years of age. They were trying to at least make sure that these were full-time workers. There are many other surveys out there that give similar results.

Ms. Gebauer: I'll contrast these results with Towers Perrin's benefits effectiveness index and total awards alignment index, which have been conducted on a similar polling basis, with randomly selected employees from around the country. The difference in the Towers Perrin surveys is that employees were screened to make sure that they were with large employers. The Towers Perrin surveys were of companies with at least 500 employees.

Ms. Lesmeister: On the basis of this study, they polled about 38 employee benefits. It's hard to come up with 38 employee benefits, but some of them were quite original. The main ones, of course, were medical programs, retirement, savings plans, and retiree medical. One of the breakdowns in the study was union affiliation. In this study, they found that union members ranked their short-term disability (STD) and their long-term disability (LTD) as very important in their total benefits program. If I were the actuary on this, and I had a large union population that was looking for change, I'd want to know what the retirement plan did for disability. How did it integrate with the other disability programs? How are the leave programs integrated, and what's done during a disability break for the savings plan? I'd want to integrate across all the benefits how things work, and how the union members appreciate it.

Ms. Gebauer: Those of you who work with companies that have large union populations know that retirement benefits, and benefits in general, seem to be a very emotional thing, and any changes around union benefits are very ticklish. Make sure you get a buy-in from the union early on, and perhaps even include union members in a task force to tackle the design issues around benefits and especially around pensions.

Ms. Lesmeister: The next breakdown was employer size. Another one of the restrictions in this study was that employees had to work for an employer of at least 50 employees. So, very small plans were totally disregarded. Small was defined as from 50 to 500 employees, mid-range was 500 to 1,000, large mid-size was 1,000 to 4,999, and large was more than 5,000 employees. The survey found that employees of large populations are satisfied with their retirement savings program. That's kind of a loaded question. It didn't say that they valued it the most. They probably valued the medical benefits the most. They were probably more concerned with the different benefit than the retiree savings program.

Ms. Gebauer: The Towers Perrin research showed similar results, not surprisingly, that savings plan satisfaction was high. Another thing that was tested in the Towers

Perrin research was understanding. They wanted to make sure that there was high satisfaction and high understanding. With regard to the savings plan, of course, as you would expect, the understanding was rated high as well. As an interesting contrast, when you look at the retirement pension plan (meaning traditional pension plans, not the hybrid plans like cash balance or pension equity), you generally find that employees will say they're satisfied with the pension plan. More than 60% of the people, in our research, said they were satisfied. That satisfaction rating was lower than the savings plan and the medical plan. What is interesting, though, is when you ask employees about how well they understood their traditional pension plan, the responses had very low scores. The scores were about 30–35% in typical employee surveys. Our general polling research showed that about 35% said they understood their pension plan. That understanding rating did not vary that much by age. It was slightly higher for the older employees, but not as significant as you might expect. It is interesting that employers may not be getting as much bang for their buck with the traditional pension plans because employees really don't understand how those plans operate or what their value is.

Ms. Lesmeister: Another aspect studied was work schedule. By that, they meant part-time or full-time employees. The comment made in the survey was that part-time employees ranked retirement savings plans higher than medical benefits. You would think a lot of those part-time employees might not get offered a retirement savings plan. Is that part-time employee the main breadwinner for the family, or is that person a spouse? If it's a spouse, then the person is not as concerned about medical benefits because the main breadwinner would probably provide the medical benefits. The savings plan would be more of a way for the family to save money, and possibly get a match.

Ms. Gebauer: I think this finding is interesting because it's different from what I've seen in actual experience. Many employers are thinking about part-time employees as a much more important part of their workforce in the future. They are thinking about the really tight labor market here in the U.S. Some employers have actually said that they would have to move outside the U.S., but others are trying to find other interesting work arrangements, and part-time employment is one of those. Part-time work for people who might otherwise have retired is one subset of that. We found that part-time workers, for some of the large employers we dealt with, were really focused on their net take-home pay. The medical benefits and the contributions for those medical benefits were really driving the net take-home pay. That became more important than a savings plan, which sounded interesting to them. As Gloria said, the people we're dealing with are probably not secondary wage earners; they felt they couldn't afford to get the benefit because they were using their net take-home pay to cover their expenses and couldn't afford to save and get the match in the plan.

Ms. Lesmeister: The next aspect studied was called life stages. Several life stages were studied. They were single, single with children, married, married with children, and those taking care of an elder dependent. For the single people, pay was the most important thing, and you can kind of imagine that for most people pay is the most important thing. Benefits come in second, however, single parents with children started to be very concerned about benefits, especially medical benefits. Married people were, by and large, very satisfied with their benefits, but once they got over age 40, it seemed that they started worrying about their benefits more. Employees who are responsible for an elderly dependent were more concerned with a flexible work arrangement than other benefits.

Ms. Gebauer: I think these results shouldn't be surprising, especially the groups that value benefits most. Single parents with children tend to use the medical plan quite a bit. They get a lot of value from that. Employees over age 40 value benefits at least twice as much as someone over age 25. Depending upon the exact benefits that are provided, it is maybe even more than twice as much for a 40-year-old as compared to a 25-year-old. These are not surprising results, and they are similar to the results that we saw in the Towers Perrin research.

Ms. Lesmeister: Another group that was studied was broken down by age—younger than 40, 40–50, and over 50. Those under 40 were worried about their job advancement. Those 40–50 were less satisfied with all the retirement benefits, and those over 50 were more satisfied, except for the elusive area of retiree medical benefits. However, the study did show that under age 40, retirement benefits are ranked second, right after medical benefits.

Ms. Gebauer: The Towers Perrin research was not dissimilar. The understanding of pension plans and the appreciation of pension plans increased with age. It talks about retirement benefits. Under age 40, retirement benefits are second. That would likely include the savings plan. So that is one factor to consider when you look at these results. When we break the results apart, the 25-year-olds and the 35-year-olds are not putting the traditional pension plan near the top as they rank benefits. Medical benefits, work-life benefits, and flex time all tend to rank higher than the traditional pension plan.

Ms. Lesmeister: The next aspect that was studied was gender. The survey polled about 50% females and 50% males. The survey showed that women traditionally do value benefits more than men, and this could be partially due to women using more health care for maternity, at least I know I did. A single parent is generally a mother who would use more medical benefits to help their children. Also, women tend to live longer. I want my husband to live long, so we'll be using those benefits for a very long time. We appreciate annuities that keep paying us until we're 95 years old.

Another aspect was educational background. They split the survey into high school graduates and college graduates. I don't think that there are many who had not attained their high school diploma. For those with high school diplomas only, healthcare needs were not being met. They probably had more of a need. They had more time to actually go to the doctor, and I'm not exactly sure what that survey result means. For the college graduates, medical and retirement were more important than the STD, LTD, or life insurance. They did value the benefits more than the high school graduates.

Ms. Gebauer: Employers need to look at cross-sections of their employees, at the skills required to do different types of jobs, and then take the value that employees place on benefits and the importance of various benefits and work the benefits program potentially differently for different cohorts of employees. That has been done in a number of organizations, and it works best when done in the context of the total rewards program, especially when you think about pay for different levels of people. You should also think about benefits for different levels of people and make sure that the benefits programs are aligned best with the interests of the individuals.

Ms. Lesmeister: Let's discuss length of service as an aspect. The breakdowns for the length-of-service group were under 1 year, 1–5 years, 6–11 years, 11–15 years, and 16 years and over. Those with 11–15 years of service and those with 16 or more years of service valued the retirement benefits more than their medical benefits. Those with less than one year of service seemed to be basically upset about all of their benefits (For the most part, those with less than one year of service aren't really eligible for many benefits). The 1–5 group looked at their sick leave and their STD more than retirement. If they had cliff-vesting, they didn't have anything yet. Those with 6–11 years wanted to work less hours and have paid time off and dental benefits. Those with more than 11 years valued their benefits, especially their retirement benefits. This is probably correlated with getting older.

Ms. Gebauer: When you think about the design of a traditional pension plan, you realize that there is in many pension plans a cliff, as I came to call it. I think a number of people refer to that magic point when you hit early retirement eligibility. The value of your benefit could triple in a day, depending upon how generous the early retirement subsidies are in your plan. So as employees continue along with a company and get closer to that early retirement eligibility (those with more than 11 years), they start to think that the value of that special benefit of early retirement looks like it's within reach, and I think it becomes much more valuable.

Ms. Lesmeister: If they're getting close to that early retirement eligibility, it is not likely that they will leave. If the employer wanted to allow those people to have turnover, he may have handcuffed them to the employer. If they're close, they're not going to leave until they get that triple benefit. So if the employer expected turnover, he or she's not going to get it.

The next breakdown was overtime eligibility. I always hate things with the word *not* in it. Those not eligible for overtime are less satisfied with the retirement savings program. When I read this opinion, I was wondering what the pay definition was in the retirement savings program. Is it possible that the overtime is included in the defined-benefit (DB) plan? Is it possible to defer it as well? Life insurance is usually based on base pay, so I wouldn't think that overtime eligibility would be affected by base pay. However, I guess the corollary of this is, what about bonuses? Are bonuses included in the pay definition for DB plans or for deferring to a savings plan? No comment.

There are breakdowns by $20,000 increments of household income. The low-income group was basically those earning less than $20,000. I was thinking about this when we were going over the part-time employees aspect. We have an employer who has a very large population of people earning under $20,000. This employer thought about putting in a savings plan. These were people who were the main breadwinners, and they're not earning even $20,000. We tried to convince the employer that these people are living paycheck to paycheck. They don't have a lot of disposable income to put into a savings plan. And I think that's why the comment came back about the lowest income bracket employees being dissatisfied with the savings plan. It didn't do anything for them.

Ms. Gebauer: You'll get a different result if an employer has put a negative election in the savings plan approach. If someone is hired, the employer says, "Your pay is $19,800. We're going to put $200 into a savings plan for you. If you really want to you can take that in cash, but you have to sign something and get it to us if you want it in cash instead of it going into the savings plan." So this negative election approach really gets a lot of lower paid people into the savings plan. They get used to living with $200 less, and the participation in the plan is high. The value that employees put on it is very high as well; it becomes a very valuable benefit for the lower paid population.

Ms. Lesmeister: Medical and retirement benefits are ranked first and second for all income groups. There were other breakdowns as well. There was marital status, but that was basically covered under life stages. There was the working status of the spouses: Were they working part-time or full-time? Much of this just had to do with general employee satisfaction. There was also a breakdown for type of job and position, whether they were profit or not-for-profit, and the type of industry, manufacturing, and service. If you'd like those results, I can always refer you to the survey.

There were some employee groups that weren't included in the study. I guess these were the forgotten employees of a employer population. Employees on leave may not be appearing at work every day, but you have to be concerned with them. When you're designing an overall program, I'd like you to consider what you're going to do for those people on STD and LTD. How are their benefits integrating across their 401(k) plan, their service, their DB plan, and their STD and LTD plan so that everything is integrated? There isn't any overlap, but it gives them protection and you've realized the cost of those people on leave.

Let's discuss rehired employees. I'm one of those people. I have been with Mercer in Houston twice. How will design affect those with a break in service? There is one nice thing about the Mercer plan. If you ever come to work for Mercer, they don't have the five-year rule. If you ever come back or if you worked 2 years 20 years ago, you can bridge it. How is the plan design in your retirement program going to help or hurt retired employees? Retired employees are unique in that they have grandfathered benefits following them that they were entitled to, and they're going to come back and haunt you for the rest of your life. Deferred vested employees, for the most part, don't get much opinion because they quit the employer on their own. If they were vested, they got their DB plan and their savings plan. But they're not really interviewed for the employer's measurement of how they want their employees to be satisfied. However, another inactive group is retired executives. Think about being a first-time actuary on a case and you don't know the ex-CEO's name. You might say, "What does it matter about this Mr. X?" A retired CEO can always come back to the current CEO and say, "If you take away that retiree medical benefit, I'll come down there." He or she may own a lot of stock or have a lot of push on the current decision makers, so don't discount those benefits. However, retired executives probably have a lot of nonqualified plans, which, again, are backed by the promise of the current decision makers that they're going to make good on those promises.

Ms. Gebauer: When considering the groups of people that you're trying to serve by redesigning a benefits program, particularly a pension plan, you really need to balance the demands of three constituencies. There are shareholders, who tend to be the most important group of people that an organization is concerned about satisfying. There are also employees; within that group of employees, you have the executives and the lowest paid employees of the organization, who have different weight. The third group comprises retirees and other terminated employees. The way I've seen it play out in my experience is that shareholders are the first group a company becomes concerned about; second is employees, and third is retirees.

Ms. Lesmeister: Retirees have time to read all those communications that the active employees may not be reading, and they'll have time to call up and complain to the benefits department if they read something they don't like, which drives them into the benefits department. If you're considering a plan design change, how is this going to affect the benefits department? They may be part of the decision makers who you're trying to convince to change a benefit plan. Have they just spent a lot of money putting in a calculator system to calculate benefits under the current plans? Do they have other HR information systems that do not collect the data they're going to need for a plan design change? If you change the definition of pay, are they actually going to be able to collect it? If you have something based on hours, are they collecting the actual hours or can they even do the things that we've decided in the plan design change? They probably want to integrate their pay systems with their benefit systems to make sure that they're collecting all the information they need for this new plan design.

Ms. Gebauer: Think about benefits as part of the HR organization, and how they view the value of benefits relative to what line managers perceive benefits to be. There was a distinct difference in the research that we did at Towers Perrin because we did separate HR managers, line managers, and other employees. We found that the HR people tended to think that benefits would drive different behavior and would be valued more highly and be a more important factor in deciding to join or stay with a company. Line managers, of course, thought that direct pay, stock, and work environment were the key drivers. And I think when we dug a little bit, we found that employees' views lined up more with the line managers than with the benefits managers and HR managers. So there could be, within the organizations you're working with, some conflicting opinions about what benefits can accomplish and what they can support in terms of the HR strategy and the business strategy.

Ms. Lesmeister: I have one closing note on the employees in the benefits department. Never underestimate them because they may grow up to be the director of benefits, and they'll remember things. There are people who will be suspicious when they encounter change. People nearing early retirement don't want anything taken away, especially the retiree medical program. There are people out there who know that they have better-than-average benefits. They might know that they have a very heavily subsidized lump-sum option, and they're very aware of changes to assumptions or take-aways in the future. There are people out there who realize something's going to be happening to their business. There might be a merger, a spin-off, or a layoff. They want job security first, but, given that their jobs are secure, they're going to wonder what you're going to cut back. What's in it for the employer, and what are you going to take away from them?

Ms. Gebauer: I was involved with one specific situation where an organization decided they needed to rethink their retirement program and actually tried to allay the suspicions of most of those cohorts of employees. Those people communicated early on and communicated a great deal with their employees. They let the employees know that a task force was formed to study the effectiveness of the retirement program. They let them know they were doing focus groups and interviews with executives, and after they did the focus groups and interviews with the executives they relayed the results. When they set objectives for the retirement program based on the input from executives and employees and from the business strategy that the company was trying to accomplish they communicated those objectives with the employees. Then they communicated the design imperatives. They might say, "We know we can't take away the lump sum. You don't know what the design is going to be, but the lump sum is going to stay there." This was the most successful redesign project I've ever been involved with. You have to have the right corporate culture to be able to accomplish that.

Ms. Lesmeister: Here's our pause to talk about some surveys that we've done internally both at Mercer and Towers Perrin. We had a very similar situation, or results that are similar to what Julie was just explaining. There was a merger situation in which there was a large employer and a smaller employer. The smaller employer was very afraid that it was going to lose everything.

The acquiring employer did not want to give that impression and sent out employee surveys to find out what the smaller group's (with1,000 employees) priorities were. This helped implement the plan design so that the acquired company had good employee satisfaction and the acquiring employer/employee continued its employee satisfaction. It did take several steps of communication to convey that the plan would undergo a merger activity or that it would undergo changes in the benefits. The acquiring employer talked to the executives and to the decision makers. They had a cross-section of employees from every job position within each of the acquiring and acquired companies. They told them that they were working on it. They told them that the results were done. They communicated the results. They made the employees feel like they were part of the change, and, when we visited later, the employees did feel satisfied and appreciated being involved in the change process.

Ms. Gebauer: Another interesting story is about a company that decided to implement a trendy new design, a pension equity plan, without getting input from employees. Management thought this was a neat way to make its benefit a little bit easier to understand, get more bang for the buck, and address some of the workforce issues. It was all based on input from the HR department and its benefits consultant. The company put in an actuary's dream plan. It was not a straightforward pension equity plan, but it was a really nifty design. It accomplished a lot. It delivered benefits to the fast-trackers, who were the people that it wanted to deliver it to. In order to deliver benefits that they were trying to target, the design got really complicated. Two years later, they found out that the program was even less appreciated than their old final-average-pay pension plan—not a result they were expecting, and not a result they were pleased with. They looked at the design again, and they talked to employees about what was driving them. They talked to managers about what would be helpful in recruiting and retaining employees. They are in the process of implementing a much easier to understand design—a cash-balance plan that actually meets their needs better than the pension equity plan did, given their workforce issues. It's not to say that a pension equity plan is not appropriate for some employers, but this organization didn't really find out what was going to drive employees and what was going to be easy for them to understand. They found themselves in a really untenable situation.

Ms. Lesmeister: What Julie found out was that instead of improving the employee satisfaction with this program, it actually went down. That's one thing that we're going to be getting into next; you must establish a benchmark. You need an initial set of employee opinions. It's kind of hard to say whether it's good or bad unless you can measure it against something else. You can measure a first survey against industry standards. There are many surveys out there, but it's always best to come back to the same employer and revisit those identical questions a year or two year later because the employer is going to prioritize those issues on that study. If he or she finds out that they said, "Very unsatisfied with the retirement program," he or she will start noticing these things and set his or her agenda to prioritize these kinds of programs. If he or she comes up with a strategy and revisits it a year later and the employees are still very dissatisfied, he or she will have a problem and need help. If it swings from very dissatisfied to very satisfied, he or she will be happy, reprioritize, and worry about something else the next time. Do you have any more stories, Bill?

Mr. Torrie: One is a personal story. My daughter had just completed her first year on a permanent job, and she knew she was going to be able to participate in a 401(k) plan. She, my former wife, and I got together and talked about asset allocation. I said, the first thing you should know is whether you have a DB plan because then you can treat the DB plan as a fixed-income investment. That would affect how you would allocate your assets in the 401(k) plan.

Ms. Lesmeister: Did your daughter's eyes glaze over at that point?

Mr. Torrie: What's even more important is my former wife's eyes glazed over. I said, "You know, you have a lump-sum plan. This is a well-known employer and a well-known lump-sum plan." She had been in this plan for ten years. She said, "I do?" I told her that was why the company had to really communicate benefits in an ongoing way. I don't think that this should be a pitch for a cash-balance plan, but that is a way, when you give your periodic statements on the savings plan, you include the cash-balance plan. It's a way for people to be constantly reminded that this is an ongoing benefit, and it lets them know what they have. My former wife had a significant lump sum, and had no idea that she had it. If it had not been for that little incident, she probably would not have known it until it was paid to her.

We were called in the late 1970s by a nonprofit organization that had a 403(b) plan. Employees would contribute 5% of pay, and the sponsoring organization would match it. It would go into well-known 403(b) accounts. The problem was that most of the people put their money into the equity fund. At the time, the equities had not performed very well. The organization saw employees retiring with very poor pension benefits and decided it had to correct this.

So we designed a floor offset plan for the organization. When we designed it, we said we would take the total accounts in this 403(b) plan and convert them to an annuity on a level life-annuity basis using very generous PBGC-type conversion rates. The problem was, within the next couple of years the equity started performing very well, and nobody was getting any benefits out of this plan. In fact, nobody understood the plan. Employees periodically got these statements. They would see the annuity conversion for the equity fund. They were very small annuities, so when they did a little calculation the offset was a small indexed annuity. Of course, they didn't know it was indexed. But they thought they were going to get these big annuities out of the pension plan we designed. We worked with two HR people to design the plan. They had reviewed the calculations for years, and we corrected every one that they sent to us. When they retired, they were disappointed because they received no benefits out of this plan, even though everything was done according to the way they had solved the problem. When the mark was up, people got the pensions they expected, and when the mark was done, they would have gotten what they expected. Those are my two recent war stories.

Ms. Gebauer: I know this is a story at least one person in the audience will recognize. We're working with one employer to help them redesign their pension plan. We did focus groups, along with executive interviews. One really memorable event happened in one focus group. As we were talking about the pension plan, an individual very close to retirement said, "Do you mean the savings plan for which I always get a quarterly statement?" We said, "No, the pension plan that's 1.7% of final average pay, blah, blah, blah, blah, blah." And I think she retired the next day.

Ms. Lesmeister: That can probably go with the communications effectiveness. Many times, the most frequently used method of communicating from employers to employees are these wonderful summary plan descriptions. They're about 8,000 pages long, and I wouldn't read them unless I was forced to. A summary of material modifications is another really fun piece of material. It seems like employees respond best to more personalized information, like employee benefit statements. There are companies that allow employees to access their retirement plan; they do modeling and that tends to increase their interest in the DB plan. Those with lump-sum options are shown those options based on a monthly Pension Benefit Guaranty Corporation (PBGC) rate. I am totally aghast that it went to 3.75% here.

When there are mergers, acquisitions, and divestitures, people would like to know what's going on to make sure that their job is secure and to find out what they're going to have after the merger, acquisition, or divestiture.

Ms. Gebauer: Of course, it's very important to appropriately pose the questions that you're asking employees. You don't want to ask, "Would you like more pension benefits?" The automatic answer is, "Yes, and I'd like more medical benefits, more savings plan benefits, and everything else." You set expectations if you don't ask the questions appropriately. One approach that works quite effectively is to ask employees to do a trade-off analysis. If you have a dollar to spend, and this is a zero-sum game, how do you want me to spend it? Here's how it's being spent today, including how much goes to pay, how much goes to the pension plan, and so on, so tell me how you'd like me to spend it. That has been a very effective research tool on a lot of design projects. It often shows that people would like more money to go into direct pay, but it verifies that they don't want benefits to go away. They are absolutely needed to play. Companies, especially large employers, must have them in the game, but they aren't as important to people as the direct pay component.

Ms. Lesmeister: This kind of reminds me about Bill's story about his wife not knowing she had a lump-sum option. Some employees may not even know they have a DB plan. So it's nice to measure how much they appreciate these benefits, or even if they know they have them. It would require input from everybody: employees, HR, finance, the legal department, and executives. They're all going to have a different opinion. Someone who's the actual payer, like someone in the finance department, can focus on costs. The legal department will make sure everything's OK. HR has its own opinions about what benefits people want. The actual employee does have an opinion. Executives are going to add things about how they can get more, the possibility of a nonqualified plan, and how they can reflect their bonus in their pay definition for the DB plan. They want to know how they can defer more and get more people participating in the savings plan so they can defer more money. You need to reflect all the input because everybody's going to have an opinion. And if you can blend it all, you'll have a more successful program.

Ms. Gebauer: I think the blending has to be appropriate. Remember, what we're ultimately trying to do is develop a benefits program, and within that benefits program there is a pension plan or a retiree medical plan that supports the HR strategy of the organization. HR strategy has to support the business strategy. What we're really thinking about is the employee perspective and the employer perspective coming together in the deal. You have to make sure that you're actually delivering on the things that are of most value to employees and driving that commitment to company success higher than what it might otherwise be. So, the blending has to be appropriate; just because every employee wants a higher pension benefit and an increase in his or her savings plan benefit doesn't mean that's the answer. Remember all of the constituencies you're trying to satisfy and the business objectives of the organization as well.

Ms. Lesmeister: In measuring opinions, I put down here that a benchmark is a must. How do you know if something's bad unless you can measure it against something else? A benchmark is a must to determine whether this is an issue or not. There are many ways to gather information. You can mail opinion surveys, you can have telephone surveys, or you can conduct focus groups. The employer's strategy needs to be in the background. Employers might try to make sure not to lose a certain segment of their employee group. Let's say they are losing all of their programmers because everybody is offering a million bucks if programmers come over and solve Y2K problems. Employers are going to want to make sure to include that group in the survey because they want the programmers to stay. They need to know the crucial employee groups that they have to satisfy. They need to revisit that periodically to make sure they have made some improvements or determine whether they have made it worse. They need to reprioritize the issues that are important now.

Ms. Gebauer: And, generally, when you're gathering employee input, it's a good idea to get both quantitative and qualitative input; the quantitative input comes from a survey. Surveys, with the improvements in technology, as most of you know, have gotten very easy to do. We used to have to make sure we had an appropriate sample. Once we had that, we could go out to employees with paper survey instruments, have them fill it in with a number two pencil, and send it back. Now you just do it over the Internet, every employee has an opportunity to respond, and you can get a lot of really good feedback that way. To supplement that with the qualitative feedback from employees is an important step as well.

Ms. Lesmeister: I think the Internet is a fantastic idea because the problem with a lot of your employees is that they don't have time to fill out a survey. They think they have better things to do with their spare time than filling out a survey. But if they realized that we're actually trying to get their input for the design of their programs, they probably would participate. Employees are usually very flattered to be asked.

Let's go from opinions to how that influences the plan design. I think there should be an overall benefit strategy that combines the DB plan, the savings plan, stock plans, and the retiree medical plan. I was talking with a *Financial Accounting Standard* (*FAS*) *No. 106* actuary about that old three-legged stool: the employer, the employee, and the government. He advised that you better worry about medical because it can be a very shaky fourth leg on that stool. If someone is eligible for early retirement but has no access to a medical program, he or she may stay until he or she's Medicare-eligible. If he or she's eligible for retiree medical, that may help him or her go out the door. There are many integration issues in all of these plans to create a good overall benefit strategy.

Ms. Gebauer: It's not a surprise to anyone that, based on the accrual patterns in these plans, the ultimate accrual pattern is very interesting because you try to accomplish different things. The savings plan accrual is a smooth curve. The pension plan accrual tends to be one that jumps up at 55 and then increases gradually after 55, if that's the early retirement age. The retiree medical plan design stays flat until you hit the retirement eligibility. It then jumps up, and then goes down. And so, when you mesh all that together, you have to make sure that you're sending consistent messages. Or, if you're sending conflicting messages, you have to make sure that there's a good rationale for doing so among the different plans that comprise the retirement program.

Ms. Lesmeister: From the employee perspective on overall retirement, if they were asked, "Are you ready for retirement?" or, "How are you going to make it to your retirement?" they're going to respond, "What do I have to do? Aren't you taking care of me? You're my employer; you're supposed to be taking care of me." If they have a DB plan, to some extent they'll be taken care of. Social Security will be out there when they retire; they'll have some income. To the extent Medicare is out there in some shape or form, they'll have some help on their medical benefits. There is that stool again. They are responsible. Employers are trying to get their employees to feel more responsible about taking care of themselves both at work, by guiding their own career development, and at retirement, by saving not only in their retirement plan but in their personal savings. The employee is going to wonder, "What am I entitled to? I didn't even know I had a DB plan." But there's a problem of keeping it simple. They will ask, "Can I afford to retire? I don't know how much I need to retire." They might need financial planning. There might be too little turnover. If they don't feel they can afford to retire, they'll stay on. I don't know how productive they are. You should try to figure out a way to measure productivity, but you can handcuff them to your population. These are people who will not leave. They're marginally productive, but they're not going to leave because there's no place to go. And what if Social Security and Medicare change drastically? We already know Medicare is going under some changes, and we know Social Security somehow, someway, is going to change. How are they integrated into this entire perspective? Did you do replacement ratios 20 years ago when you put in the plan? Did you count on Social Security providing so much? Will these populations be able to count on Social Security? There's a lot coming down the pike that they want to know about, and we're going to have to help them find out about it.

Ms. Gebauer: My view is that this all points to planning and education and understanding. We start by making sure that employees understand the deal that they have with the employer organization. Is the concept of paternalism and entitlement still alive at this organization? Chances are it's not. Chances are that has moved to a commitment to help me succeed. As long as you're a contributing member of the workforce, we'd love to have you here. We want to help you retool and continue to be relevant for the organization, but if not, you cannot expect lifetime employment. So if you cannot expect lifetime employment, what do you have to do early on in your career so that you can leave the workforce for another organization?

Make sure that you have begun your retirement planning. Or, if you're later in your career, what do you need to do to make sure that you can retire gracefully so that you'll have enough money to meet your expenses? It's a matter of understanding the importance of savings and investing properly, knowing what risks you are willing to take, and knowing what your time horizon is for making the investments. To answer this, I have seen a number of organizations, at the time of retirement plan redesigns or overall benefit program redesigns, introduce group financial planning for their employees. Oftentimes it's initially done on a company-pay-all basis, which helps to get employees used to the concept of using this. After a 12-to-24-month period, this is truly a benefit for employees; it changes to only partially company paid or fully employee paid. We can support employees in giving them more responsibility for saving for retirement and for investing for retirement by providing education to them as well.

Ms. Lesmeister: Under the DB plan, employees generally have several questions: "When am I entitled to receive a benefit?" "Do I have to wait until I am 55 and have 10 years of service to get this cliff?" "This doesn't sound very portable." As Julie was saying earlier, portability can be a very important benefit; it is not just a matter of the amount of the benefits—it is the possibility that it's portable. You can handcuff employees to an employer without that portability. Does the employer want that? What pay is used in the benefit formula? Perhaps it is base pay. Your compensation director might be undergoing a pay change. He might decide that we've had this high base pay for years and years and wants to go into a high incentive pay environment with lower base pay. Everybody has a stake. There are 50% target goals.

On the retirement side, we need to know what's going on the pay side. If our DB plan is base-pay-only, we know what's going on. Make sure not to lose sight of what the other people in the organization are doing and what disability benefits are available. Are these coordinated with the STD and LTD programs? What death benefits are available? I feel like I've seen it all on the death benefits; I've seen the orphan's benefits and I swear that they must have ex-spouse orphan's dog's benefits in some of the benefit plans I've done. Is there a lump sum available? Usually that's a very popular option; it is very popular with people with PBGC interest rates. They don't really want you to go to the General Agreement on Tariffs and Trade. But with the interest-rate environment the way it is, those are very expensive benefits because market values and that PBGC rate are going down while those lump sums are going up.

Ms. Gebauer: And in terms of the employee perspective, the group of employees that is most important to the organization will influence the type of design you should have. Are you really trying to make sure that you're using benefits as a differential? We want to deliver most benefits to our fast-trackers. Maybe that points to a pension equity or a final-average-pay design. If you add on top of that a benefit that's easy to understand, that's portable, that employees can get their arms around, that might lead you to a pension equity plan. But if you want benefits simply to be that threshold level needed to play, you might stick with a less-generous final-pay plan, a career-pay plan, or a cash-balance plan, where there is not as much differentiation for the fast-track, higher paid employees.

These are employees whom one would think would be crucial to the organization, as pay generally relates to the importance of the individual within the organization. On top of that, you might need this to be easy for your employees to understand. One critical goal for me is ease of understanding for employees so that they support the deal that we have with them. It is perhaps a tool to help in recruiting so that I can somehow position this as another component of compensation. That often leads you to a cash-balance design to make sure that you're meeting what the employees are expecting from the plan as well.

Ms. Lesmeister: In your savings plan design, an employee is often concerned with the match or when he or she is vested in it. The employee might ask, "Can I take a lump sum? Can I take a loan? How much pay can I save?" This might be more from an executive who has been cut back every year in December and wants to put more money in the savings plan. "Which investment options should I pick?" Boy, stay away from this one. If they want investment advice, don't be the one saying, "I think you should put it all in Fund A," because they'll come back at you on that one. What happens if the market falls? In a savings plan, what if they did have it all in equities and they just lost 10% of their investment over the last month? How old are they? They are in it for the long term. The exception is if you're 65 years old, and you just happen to have a lot in equity—what are you going to do? When the October market fell back in 1987, there were people saying, "Well, I was going to retire this month, and now I can't." How is this keeping those people handcuffed to the organization?

Ms. Gebauer: I think another point on the savings plan design, from an employer's perspective, is making sure that it's married to the DB redesign. As we talked about before, make sure that there is education rather than advice on investments. If you pull it all together, there are some interesting designs available. People do want that choice in investments. As for DB plans, there are some very innovative cash-balance designs that you've probably been talking about over the last couple of days that really allow for investment choice for employees. There are some interesting ways to get around the rules of 417(e) by defining a retirement age after 5 years of service. What you've done is convert your DB plan to something that looks very much like a defined-contribution plan. You have a cash-balance plan that gives employees investment choice and in-service distributions. You don't have to issue suspension-of-benefits notices. It's a really interesting picture.

The issue you have to deal with then is that the risk associated with this investment for employees might be greater than it would have otherwise been if you had your traditional DB plan or a cash-balance plan with some kind of a fixed-income index. So, again, the employee's perspective that we found was, "I want control of my money." Think of that in the savings plan and make sure they have enough investment options in the DB plan. If you've gone to one of the more innovative approaches, cash balance or pension equity, is there some way that you can give them more choice on those investments?

Ms. Lesmeister: I really agree with Julie on the investment choice. Some employers only have it in employer stock. I know of an employer who terminated their DB plan, rolled over all the amounts into the savings plan, which was actually more of an employee stock ownership plan, and went bankrupt. That was a really sad day for a lot of the employees.

Let's discuss retiree medical design. One of the frequently asked questions is, "Why don't we have it? Am I eligible for it?" Usually plan design changes are going to impact the deductibles and the copayments, and limit the use of doctors. Employees will ask questions like, "How does this program integrate with Medicare? Does it stop at Medicare eligibility? Does it wrap around Medicare after Medicare eligibility? Can they take this away from me?" I'm sure we've seen the lawsuits that have orbited around retiree medical benefits, and a lot of it depends on what has been communicated to participants. Those older retirees, people who retired 20 years ago, had no communications that said those benefits would ever be changed; therefore, employers are very reluctant to take it away from them. They fear a lawsuit. But those people, nowadays, are getting communications that do say that they can amend the plan and that they have the right to terminate. So, as changes come, the employer always wants it in his or her back pocket because medical cost-of-living expenses have been increasing over the years, and the employer can only fund so much.

Other questions an employee might have are, "How much is it going to cost me? Is the employer going to pay all of it? Are they going to pay part of it?" We've actually seen some programs where they didn't actually offer retiree medical for early retirements, but they offered entrance into a medical plan. The employee had to pay all of the cost, but it at least gave the employee access to a medical program so that it didn't really handcuff the employee to the employer.

Ms. Gebauer: It is no surprise that 25-year-olds don't think much about retiree medical benefits. However, 55-year-olds do, so in thinking about retiree medical design the first question you should ask yourself is, "Should I have it or not?" This gets back to what we've been saying—what workforce do I need? What's the best way to bring them into the organization and retain them? And if you're looking at a young workforce with multiple careers that continues to turn over, retiree medical is probably not necessary for your organization. As more organizations have looked at this cost, more organizations are taking it away. The issue that organizations face is, "Can I get people to retire before Medicare eligibility if there is no retiree medical design?" It comes back to education and access.

The biggest issue that we found in the research that we've done is that people are reluctant to retire before Medicare eligibility for fear that they will not have access to medical coverage. It is not necessarily the amount that they will have to contribute. Many organizations see what *FAS No. 106* cost does to the per capita cost of labor. I can make sure that they have access pre-65 and post-65. There are all sorts of options now, especially with Medicare Plus Choice implementation. We're seeing that trend is access-only along with changes to medical account plans.

A recent change that we've seen is organizations saying, "Here's a benefit that people really don't understand the value of. Maybe this is an organization that has moved to a cash-balance or a pension-equity plan, or an indexed cash-balance plan. How do I get this retiree medical promise looking like this cash-balance plan or other plan so that my employees (even the younger ones) will put more value on it." This is an organization that feels they need to have retiree medical to manage the workforce out at retirement, putting in a medical account, and perhaps even a matched medical account, where someone sets up a voluntary employees' beneficiary association (VEBA) and says, "You know, you have responsibility for saving for medical as well. We'll match the VEBA contribution dollar for dollar or 50 cents on the dollar." Some organizations have matched their employees' VEBA contribution two dollars for every dollar so that employees are encouraged to provide a benefit too. Again, it's to make it visible to employees to get them to understand what they're going to need to save, and what the company is providing in this regard.

Ms. Lesmeister: Every employee population is different. See what's most important to your employer's employee population, especially the ones who they want to keep, such as the fast-trackers. Get the most appreciation from design changes. Get the most bang for your buck. The employer wants return on his or her investment. The message you're going to see here is communicate and listen. Communicate that you're considering a new plan design. Listen to the employee input. Communicate that you want input and listen. Communicate that you're working on it. Communicate what you've done and how it affects employees.

Communicate new educational issues. As Julie was pointing out, let's say the match of a savings plan was in employer stock and now they're saying, "OK, you have the choice. You can invest it any way you want." They're going to need some financial planning. It's an educational opportunity. Communicate how to complete the enrollment form. I just got one from Mercer. It just intimidates me to even open up the envelope, but I know I have to fill it out within the next 30 days. Who knows what kind of medical benefits I'll get. Communicate how changes can be made. You're going to have life changes, and you're going to have reasons to change your deferral to a savings plan, etc.

Ms. Gebauer: While you communicate, employers, be honest. If there's a cutback, don't try to wrap it up in something and say it's an improvement. Employees are smart; they'll figure it out. There may be some features that are improvements.

Highlight those, but explain if there's a change in benefits delivery or a reallocation of benefits from longer service to shorter service; make sure you let people know about it. Let people know about any special transition benefits and highlight those early on and often. If the suspicious people are the 55-year-olds who are eligible for early retirement and you're protecting them and not changing their benefits at all, don't let them start making calls to the benefits department. Tell them that they're grandfathered and protected. The old plan keeps running for them.

Ms. Lesmeister: One of the bad things in a plan design is to find out later that one of the executives you've been interviewing actually falls into one of these categories and you didn't protect him or her. He or she will bring out that there needs to be a transition benefit.

Communicate that you will be asking for input to measure the success of the new program. You've done a benchmark. Now you want to revisit it and see if it was an improvement. If it wasn't, you need to address that. Be sure to communicate.

Why are we doing this? Why are we listening to employees? We've never done it in the past. Benefits carry a significant cost. After-pay benefits can be 20–40% of their pay. Why should we spend money on an ineffective program if the employees don't appreciate these things and they cost a lot? Employers want efficient, quality employees. They don't want employees calling up the benefits department every hour of the day trying to figure out what the summary plan description really means. They want employees at work who don't have worries about their benefits. They're going to be productive and, in turn, make profits for the employer.

Ms. Gebauer: While benefits are not the key driver in recruiting and retaining employees, we have found in our research that they are needed to play. If you don't have them at a sufficiently high level, there can be a problem. Make sure that your program meets this definition for your employees as well.

Ms. Lesmeister: Why is revisiting employee opinions important? You need to have a benchmark, and you need to revisit to measure improvement. Everything changes. Opinions change and people change. A company's entire workforce might have had 100% turnover since the last opinion survey. The economy changes, interest rates drop, and the market drops. The company changes over time. You're going to have mergers and acquisitions. I saw an oil and gas firm in Houston turn into a food-service organization through an acquisition and divestiture. I've always remembered this firm as being an oil and gas firm. Now it has nothing to do with oil and gas anymore. Companies change. The only way to measure change or improvement is to establish a benchmark. How can you know if you're doing better if you don't know what things were like in the past? The idea here is to identify issues for the employer so that he or she can prioritize and spend his or her money in the most efficient way.

Mr. Torrie: The one benefit, if you will, that wasn't mentioned was working conditions. I had one client who had an 80% final-average-pay plan. After about 30 years, you could put that together with Social Security and retire with more than 100% of what you were currently receiving. They said there were a lot of old people who weren't leaving.

Mr. Thomas Naffe Rice: I'd just like to make a comment about DB plans being understandable to employees. We are not part of Social Security. Employees over age 40 can understand what DB plans are. It's not too complex if you have a final-average-pay plan and you get a certain percentage for each year of service. I had been in the corporate world. I think the employee in Social Security probably doesn't really know what he or she's going to get. I think it's easier to understand that if you work 30 years and use a 2.5% formula, you get 75% of your pay when you leave. That's pretty easy to understand; you have a deferred compensation plan that you can save to add to that. It's not so much DB plans that aren't understandable. It may be that young people don't appreciate them, but they're certainly necessary for people over age 40. I think that part of the problem is we make it more complex than we have to. Also, Social Security is not well-defined. If we work on those problems, I think that we could have an understandable DB plan. Then focus on the younger age group and what they're interested in. Portability and savings can be handled through deferred compensation, profit sharing, a 401(k), or whatever. In Louisiana, our people have a pretty good idea of what they're going to get.

Ms. Gebauer: I think those are good points. When you talk with employees, distinguish between understanding the operation of the program versus understanding the value of the program. The thing that we've identified as very difficult for most employees to understand is the time value of money. What is today's value, for a 35-year-old, of something that starts at 65 and continues for the rest of his or her lifetime? I don't know how employers have effectively tackled that problem. I think most employers have had difficulty in tackling that problem of understanding value.

Mr. Rice: I'm not exactly sure what the problem really is with the final-average-pay plan. What about inflation after retirement? Of course, you have cost-of-living adjustments, and I believe you said that a retiree has a lot of time. In the state of Louisiana, retirees can influence legislation more than actives.

I think career average plans in the corporate world were probably put in to save money for the employer before he or she found out 401(k) plans can reduce his or her costs considerably more. Career average plans, to me, are very hard to understand. Unless it's a final-average-pay plan, I don't think the employee is going to know what he or she's going to have. I think that's something to consider. I understand that an employer is trying to cut costs, but a lot of it is the move to career average. Somebody who has an account through a savings plan and is getting close to retirement doesn't have any idea what that account is worth. I think most of them think they can just divide by 10 to get so much this month. They have no idea. I think if we, as actuaries, look at it, the best bet we've ever had, and still have, is the DB plan for the final average pay, in terms of communication. If we can help the economy and motivate employers to put them back in, then we can probably resolve that issue. At least we won't have to spend a fortune in communication for those over age 40. I understand the reality of it, but I think that if you can explain Social Security better to employees, that would help as well. Maybe we could help draw that somehow. I don't know.