Benefit Plan Risk: A Global Perspective

Taking five key steps will help organizations manage risks facing their global benefit plans and ensure that benefit plans support strategic goals.

Organizations around the world offer their employees benefits such as medical and pension plans in an effort to attract and retain the best talent. But these plans carry risk of unexpected costs, noncompliance with regulations and disappointing return on investment.

Smart organizations have always worked to mitigate that risk. But a confluence of factors, from stock market volatility to increasing regulatory scrutiny, has made managing benefit plan risk a key focus of every human resources (HR) function.

The challenges are more varied and threatening than ever before. But five essential steps can go a long way in helping an organization manage its benefit plan risk:

1. Understand the overall business context.
2. Define a global benefits strategy.
3. Accommodate local market practices.
4. Apply governance for continuous monitoring and improvement.
5. Communicate to all stakeholders.

Mounting Risk

First, the challenges. Benefit costs have been increasing rapidly and significantly, especially for medical plans. What was affordable even a few years ago today is cost prohibitive. Looking out five years or more, the potential price tag can be staggering.

Because of stock market volatility, some pension accounts have suffered significant losses, and the prospects for recouping those losses in the short term are dim. Markets around the world are expected to remain soft and, worse, unpredictable for the foreseeable future.

Another risk to pension funds is that retirees are living longer. In much of the industrialized world, life expectancy is in the mid- to high 80s, whereas two decades ago it was ten years shorter. That can set long-term pension costs much higher than they were predicted to be.

It’s the unpredictability of these issues that keeps a chief financial officer awake at night. It’s one thing to have rising costs that can be planned for and thus managed. It’s far more challenging to have to react on the fly to unexpected cost increases.
These financial factors are hitting organizations in an era of increasing regulatory scrutiny. Violating such regulations—which can vary significantly from one jurisdiction to another—carries threats of fines, legal fees and contractual, civil and even criminal liability. They also come at a time of widespread outsourcing. The complexity of outsourced HR only increases benefit plan risk.

Faced with these challenges, there are several ways that organizations can manage volatility and future benefit cost increases. Benefit plan sponsors can:

- Lower administration costs, perhaps through technology solutions that streamline and automate HR operations
- Diversify financial portfolios in the hope of minimizing volatility while maximizing returns
- Shift benefits from those that are payable after a worker leaves employment, such as pensions, to account-based programs, such as defined contribution plans that accrue during the employee’s active working lifetime
- Make sure employees understand the true value of medical benefits through consumer-driven communication and pricing strategies so they’re not requesting expensive but unnecessary treatments
- Rein in costs by actually reducing the value of the benefits they offer.

All these tactics are likely necessary, but they’re probably not sufficient. And achieving cost reductions by reducing—or even appearing to reduce—benefits carries its own risks. An organization might be able to dramatically cut costs, but at the expense of impeding its ability to compete and succeed.

What’s needed is a global, holistic approach to managing benefit plan risk. While efforts to reduce benefit plan risk must be centrally coordinated, typically under the guidance of HR, the overall risk and approach is best defined through a cross-functional team. The responsibility for assessing and dealing with this risk should reside in various areas of the organization, including HR, finance, tax and legal, and internal audit.

Context Counts

Managing benefit plan risk begins with understanding the overall business context. What are the organization’s strategic objectives, and how do its benefit plans contribute to them?

An organization should start by assessing the types of employees it needs to achieve its operational goals. For example, does the organization require highly experienced employees, or can the job be done with younger employees who don’t highly value pension benefits? Which employees are critical to the business?

The next step is to determine what needs to be done to attract, retain and engage those employees. For example, does the organization operate in an industry in which retirement benefits are sacrosanct? Do key employees value benefits, or is cash king? Do benefits need to be competitive or just sufficient? Are there internal equity issues with employee groups?

What level of benefits can the organization afford to offer? Being stingy with benefits can render an organization uncompetitive. But benefits professionals must work within financial realities to offer benefit plans that won’t break the bank. Is the organization in a regulated industry that allows it to pass on benefit costs to customers? Does the cost of benefit programs inhibit the organization from retaining future business contracts?

Setting a Strategy

Once the business context is understood, a global benefits strategy can be defined. The strategy should be specifically designed to support the organization’s strategic objectives.

Because benefits are an important part of the contract between employer and employee, the benefits strategy must also align with the overall education:

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benefit plan risk

Like Politics, Benefits Are Local

It’s important to design and deploy a global benefits strategy that applies to all operations and locations. But individual benefit plans will have to be tailored to local markets. Each country will likely have different regulations that affect benefits, and regional culture will also dictate which plans best support strategic goals.

For example, in countries like France and Italy, the government historically has provided excellent social security benefits. As a result, companies are likely to be less generous with pension plans. But in other countries, companies must offer more robust pension benefits to remain competitive.

Likewise, some countries require that certain benefits be offered. And, particularly in certain European countries, works councils represent the interest of employees and have strong negotiating power when it comes to benefits.

Best-in-class organizations define a global benefits strategy and centrally document and monitor their benefit programs while working with their local HR teams to fine-tune the actual plans delivered in each location. Many shoot for an 80/20 balance, in which 80% of plans are standardized across the enterprise and 20% are tailored to each location.

But depending on the industry, the 80/20 balance may not be viable (see the sidebar, “Halliburton: A Disciplined Approach”). An organization may need to allow for more flexibility to accommodate local laws and practice. What’s

Halliburton: A Disciplined Approach

With more than 64,000 employees in 80 countries around the world, Halliburton has its share of benefits plan risk to manage. The company is among the world’s largest providers of products and services to the energy industry. It is an established company in a mature industry.

“We found benefits programs that hadn’t been reviewed in many years,” said Gilbert Chavez, senior director of total compensation at the company’s Houston, Texas headquarters.

In 2000, Halliburton recognized that benefits administration in its various operations and locations was too independent. The company decided it needed more rigorous and centralized management of its benefit plan risk.

“We started by creating a repository of information for all our programs around the world,” Chavez explained. “That gave us a clear picture of our current state. And it provided a foundation that we could maintain and continuously update.”

The next step was to implement a disciplined governance program to define a global strategy, revise it as appropriate, and act on it around the world. A global benefits committee has been key to that program. The committee reviews and decides whether to approve benefits plans proposed by local country offices.

“There’s some flexibility for each country to proceed, as long as they’re working with the global benefits committee to have the program ratified,” Chavez said.

He added that flexibility is crucial to a company that operates in highly diverse environments. The governance committee applies knowledge from lessons learned and makes recommendations on best practices, such as technology that can streamline plan administration. But the actual plans implemented are tailored to each market.

“The good news is that the local HR administrators now recognize the expertise of the central committee and seek us out for guidance,” Chavez said.

At the employee level, the company tailors communiques to reflect local culture. “Everything needs to be transparent, because in today’s world employees communicate with one another across regions on a real-time basis,” he said.

The payoff for Halliburton’s disciplined approach is better funding for benefits programs, better use of HR resources, significantly improved compliance with local regulations and reduced administration fees.

“Our approach isn’t always easy, and it’s not a silver bullet,” Chavez said. “But our efforts have resulted in a better employee experience, and that ultimately helps us attract and retain the best talent.”

Rewards-and-recognition program, which includes compensation, professional development and corporate culture.

Once a strategy is defined, an organization can design and implement individual benefit plans across its operations and locations. However, rather than trying to develop plans indiscriminately around all employees, it is preferable to focus on the types of employees that are key to achieving strategic goals. Offerings should be fine-tuned in ways that enable an organization to best attract and retain those specific employees.

Also, plans should be designed in ways that maximize their perceived value to employees. For any plan, some types of employees will value the benefit more than others.
important is not to simply let local HR administrators develop their own customized, one-off plans. That’s a recipe for runaway costs and weak governance.

**Review and Improve**

Strong governance is crucial. It’s the only way to both control costs and ensure that benefit plans continue to align with strategic goals.

The best-in-class approach is to establish a cross-functional governance committee that oversees benefit-plan design and implementation. The committee should have global authority and should include HR, finance, tax and legal, internal audit and, possibly, procurement.

The governance team should have a clear picture of which benefit plans are offered in all locations around the world. The authors have worked with companies that had documented only what was necessary to comply with U.S. Generally Accepted Accounting Principles reporting requirements. In the meantime, they had no idea which benefits they offered on a country-by-country basis. It’s hard to manage what can’t be seen.

The governance team should meet at least quarterly to ensure alignment among all functions. It should receive reports more often—probably monthly—from the country offices where the individual plans are administered.

Note that lack of effective governance can have serious consequences. Noncompliance with regulations can result in fines and damaged reputation. And what happens when an organization faces an acquisition or merger? Are the information and structure in place to assess the benefit plan risk of a target organization or integrate the plans of merging enterprises?

**Talk the Walk**

Finally, all stakeholders must have the benefits information they need. That requires two types of communication. One is among the functions responsible for governance, including HR, finance, tax and legal, and internal audit. That communication also needs to extend to HR administrators at the country level so that everyone’s always on the same page.

The other type of communication is between the organization and benefit plan participants. An organization is spending money on these programs, and should get a return on that investment. That means ensuring that employees understand and appreciate them, so that the organization can at-
tract and retain the talent it needs. If employees don’t perceive the value of their benefits, perhaps the money being spent on them could be better spent elsewhere.

Bear in mind that if the organization isn’t communicating with employees about their benefits, they’ll fill that void by communicating with one another. That opens the door to confusion and misinformation, which again threatens the return on the benefits investments.

Taking this five-step approach is straightforward but not necessarily easy. It requires corporate will, which probably requires an executive sponsor. But even relatively small changes can begin to make a big difference. For example, creating a central repository of plan data can provide a better picture of the current state of benefits and enable the plan sponsor to identify the gaps that are keeping the organization from best-in-class status. More automated reporting or consolidation of vendors can streamline processes and reduce costs.

By following the steps outlined here, organizations have an opportunity to improve plan governance, reduce costs for plan administration and compliance, improve participant satisfaction and better manage benefit plan risk. Ultimately, they’ll be better positioned to attract, retain and engage their workforce to achieve strategic goals.

Authors’ note: The views expressed are those of the authors and do not necessarily reflect the views of Ernst & Young LLP.