

# Employee benefits: how to manage them properly



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**T**here is no doubt that in today's highly competitive market place, the management of people is one of the primary keys to organisational success.

Unfortunately, for a number of reasons – like the constant struggle for recognition as a legitimate organisational function – too little attention was paid in the past to the effective management of human resources in South Africa.

The awareness of inadequacies in HR management only came about as we started to compare our success with that of organisations in other countries where human resources were considered critical to success.

In this regard, for example, we can only look at the World Competitiveness Yearbook to really see how weak our position is regarding the management of our people.

It is not enough to stay on top of the latest developments within this rapidly changing discipline. Managers in organisations must also realise that people are human resources to be managed effectively just like capital, machinery and other organisational resources.

In addition, organisations and managers must also be aware that the proper management of human resources can be a major source of productivity improvement and growth. Something which South Africa as a country desperately needs.

According to Ulrich, Brockbank and Yeung, HR practices are central to improving an organisation's capability and thus its competitive advantage – enabling it to compete more successfully for markets and profits.

A vital HR practice in companies is that of com-

pensation management. According to Casio, an organisational compensation system includes both financial and non-financial rewards.

Financial rewards include direct payments as well as indirect payments. Non-financial rewards include everything in a work environment that enhances a worker's sense of self-respect and self-esteem.

Carrell et al also support this view and refer to compensation as a system consisting of extrinsic rewards such as salary and benefits as well as intrinsic rewards such as achieving personal goals, autonomy and more challenging job opportunities. Thus, compensation broadly includes all forms of payment (financial and non-financial) in exchange for employee contributions.

An important component in compensation management is that of employee benefits. These benefits constitute as much as 40% of the total payroll costs and is rising constantly. A question that needs to be addressed by management therefore is whether employee benefits are managed as efficiently and effectively as possible.

In a recent investigation in a large institution, it became evident that the management of employee benefits in this organisation was a neglected management activity and that this situation was not unique to such organisations, but prevalent throughout companies in South Africa.

In this article a number of these issues will be addressed:

- ❖ the reasons for the growth in employee benefits,
- ❖ the value of employee benefits and
- ❖ key issues in the management of employee benefits.

## **Reasons for employee benefit growth**

Since World War II there has been a marked increase in the number and types of employee benefits offered and an equally dramatic increase in their costs.

Employee benefits have not always played a crucial role in the life of workers. During the depression years of 1929 to 1933, workers were grateful just to have a job. During this time benefits constituted less than 1% of a worker's salary.

The benefits were usually limited to only a short vacation. It is because these benefits were financially so insignificant that they were called 'fringe benefits.'

As time passed, additional employee needs developed such as education, medical care, pension, housing and transport. A further development in recent years has been the introduction of a flexible

compensation approach.

This has been prompted by the fact that we have moved away from an era in which large sections of the work force were assumed to be similar to an era in which it was composed of many different individuals e.g. more female workers and dual income families, an increase in ethnic diversity and the employment of people with disabilities.

#### Value of employee benefits

There are various reasons that promote the establishment of employee benefit plans in organisations as opposed to simply giving employees larger salaries. Rosenbloom and Hallman and Averett and Hotchikise list the following:

- ❖ *Concern for the employee's welfare:* most employers are genuinely concerned about the wellbeing of their employees. Although they may be managing these benefit plans in a paternalistic way, employers also display a social consciousness in this regard.
- ❖ *Improved corporate efficiency:* although it is impossible to determine the exact results of an employee benefit programme, most believe that efficiency and business profits are enhanced in the following ways:
  - *Morale:* a sound employee benefit programme illustrates management's concern and relieves employees' anxiety and fears.
  - *Facilitation of work force reduction:* retirement plans can be used to encourage voluntary early retirements when a reduction in the work force is necessary.
  - *Employee identification with profits:* benefits such as deferred profit sharing and employee stock plans help employees to identify with and have an interest in the efficiency and profits of the company.
  - *Attracting and retaining competent staff:* when competing for employees in the labour market, a sound employee benefit programme can provide the organisation with a competitive advantage to recruit and retain the employees it requires.
  - *Favourable tax incentives:* the favourable tax treatment of certain benefits has become an important reason for employers to provide such benefits rather than just paying higher wages.
  - *Demands in labour negotiations:* since employee benefits are within the scope of collective bargaining, the employer is legally obligated to negotiate with the union over such demands. The employer does not have to agree to the union's demands, but it may be to his advantage to make compromises regarding benefits rather than granting salary increases.
  - *Social and governmental pressures:* subtle social pressures in employers' communities can force organisations to take responsibility for social programmes. If employers do not provide adequate employee benefits, governmental or social insurance programmes will be enforced by legislation.
  - *Advantages of group insurance:* most employee benefits are provided through group insurance or group plans. Certain cost savings and other advantages arise from providing cover under a group plan compared to buying similar cover individually.

According to Griffes, a fundamental feature of benefit theory is that employees' perceptions of the value of benefits result from personal economic circumstances and personal social values. Since these change over time, employee perceptions also change.

The concept of ever changing employee perceptions about employee benefits is fundamental to benefit planning and management. A benefit plan installed under cer-



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*Benefits management has traditionally been characterised by a crisis atmosphere, paste and patch tactics to deal with each crisis and extraneous pressures from promoters and strong power centres in the organisation. That structure is crumbling under the weight of social change, government actions and the critical need for control and order in the organisation.*

tain economic and social circumstances may become outdated and inappropriate as the socio-economic environment changes as has been the case in South Africa. The wide range of needs and preferences of a diverse work force and the need to update employee benefits continuously have become a major management challenge for organisations in South Africa.

In the past benefit/compensation managers were not involved in planning, objective setting and decision making. This was mainly because of the traditional view of being 'giveaways' without a measurable return on the investment.

Employee benefits are now in transition to a new role. Heightened expectations of employees, the need to manage benefits in a more cost effective way as well as using employee benefits as a competitive advantage, are the main reasons for viewing employee benefits as an important part of an employee's total compensation package.

The need for a new approach towards the management of employee benefits is highlighted by the following statement by Griffes: "Benefits management has traditionally been characterised by a crisis atmosphere, paste and patch tactics to deal with each crisis and extraneous pressures from promoters and strong power centres in the organisation.

"That structure is crumbling under the weight of social change, government actions and the critical need for control and order in the conduct of the business enterprise."

The following factors pose the main challenges to the management of employee benefits:

- ❖ enabling employees to make choices and to customise their benefits package,
- ❖ providing information to enable employees to make long term choices,
- ❖ making employee benefits portable,
- ❖ communicating the true value of employee benefits to employees.

*Enabling employees to make choices and to customise their benefits package*

Most organisations have a rather paternalistic approach to the structuring of remuneration packages. This means that employees are to a significant degree tied to cash/benefit mixes as prescribed by the organisation.

Little discretion exists for the individual to shape benefit coverages to suit individual needs or circumstances. This probably results in the organisation wasting money on benefits that have no or limited value to a significant number of its employees.

Individual employees are also generally unable to achieve optimal cash flow from their remuneration packages. The ability of individual employees to achieve optimal cash flow from their remuneration package is dependent on the existence of the following two conditions:

- ❖ the remuneration package should have a sound selection of tax efficient benefits,
- ❖ employees should enjoy significant freedom in determining the cash/benefit mixes of their remuneration packages.

A remuneration strategy that allows employees to achieve optimal cash flow from their remunera-

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tion packages is the flexible benefits plan (also known as the cafeteria plan). The key features of this plan are:

- ❖ the employee is rewarded with a total package value based on the value of the job and job performance,
  - ❖ the employee is provided with a number of flexible benefit options from which he or she may choose those that are the most appealing,
  - ❖ the cost to the employee is minimal, with the cost being deducted from the employee's gross pay, resulting in a net cash savings.
- By offering a flexible benefits plan, the employer is responding to the needs of the employee, which would otherwise be unmet.

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