HR Trends and Challenges

The changing U.S. demographic, economic and social landscape of the workplace

2007
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Introduction

This study examines the impact of the changing U.S. demographic, economic and social landscape on the workplace, and the resulting challenges and issues affecting corporate Human Resources departments. The study covers two main areas of inquiry: broad socio-economic trends and trends in employee benefits. Topics include:

- rising healthcare costs;
- increasing diversity in the workplace;
- the shift toward “employee-centric” benefits that increasingly emphasize consumer choice and consumer responsibility; and
- current trends in managing employee health, absence and productivity.

The study also discusses the implications of these trends for employers:

- employers will continue to look for new strategies and tools to control healthcare costs;
- employers will need to consider offering flexible benefit packages to accommodate an increasingly diverse workforce;
- as employees are given more responsibility for making health and financial benefits decisions, employers will need to provide them with effective tools, support and educational information to assist in decision-making;
- employers increasingly will recognize the importance of tracking and managing the time and costs involved in employee absences, and will look for strategies and tools in this area.

Methodology

Unum contracted with LIMRA International to conduct a comprehensive review of secondary research, including:

- existing Unum research studies;
- LIMRA International research;
- research from the Society for Human Resource Management (SHRM); and
- a variety of business, government and trade journal studies and related articles.
I. Broad Trends Affecting the Workplace

A. Rising Healthcare Costs

The rising cost of healthcare continues to be one of the primary challenges for employers. It is estimated that in 2005, just over 16% of the gross domestic product was spent on healthcare in the United States, up from 13.8% in 1993. As baby boomers begin to retire, healthcare spending is expected to reach 20% of GDP by 2015.\(^1\)

Commensurate with the increase in healthcare costs, employment-based health insurance premiums have more than doubled since 1997.\(^2\) And while premium increases are currently decelerating from a peak in 2003, employers are still feeling the pressure after five consecutive years of increases averaging more than 9%.\(^3\) 2006 saw a 7.7% increase which, although the lowest increase since 2000, is still twice the rate of inflation and twice the growth in workers’ earnings.\(^4\) It has been suggested that, if action is not taken soon to rein in healthcare costs, health insurance costs will overtake profits for some employers by 2008.\(^5\)

Many employers consider the rising cost of health insurance to be the most important overall trend affecting them.\(^6\) Eighty-eight percent of human resource professionals responding to a 2005 LIMRA survey cited controlling healthcare costs as the top challenge for employers.
Consistent with this, a recent study from the Washington, D.C.,-based Business Roundtable revealed that, for the fourth consecutive year, leaders of America’s top companies identified healthcare costs at the top of the list of pressures facing business, with 51% of CEOs citing this as their greatest concern. 7

**Factors fueling the increase in healthcare costs and premiums**
The three primary factors contributing to increases in healthcare premiums are: 1) general inflation; 2) healthcare price increases in excess of general inflation (due to higher-priced technologies, cost-shifting from Medicaid and the uninsured to private payers, and provider consolidation/broader-access plans); and 3) increases in utilization. 8

Increases in utilization are estimated to account for 43% of the overall increase in healthcare premiums and are due mainly to increased consumer demand, more intensive diagnostic testing (due partially to the increased practice of defensive medicine), an aging population, advances in medical treatment, and deterioration in lifestyle. 9 The latter three are particularly relevant to the changing employee benefits arena.
• **Aging population:** According to the U.S. Census Bureau, the fastest growing age group is people over age 50, and the percentage of people living past age 80 is increasing at an unprecedented rate as well. Currently, 12% of the U.S. population is age 65 or older; by 2030 that figure is expected to climb to 20%. This aging of America is creating a profound cost-management challenge for employers, as each additional year adds 2.5% - 3.0% in healthcare costs. In fact, medical costs are reported to rise an estimated 25% from age 40 to 50 and 35% from age 50 to 60, although the driver of excessive healthcare costs by age is a result of the relative health risk the person has, rather than the age itself.

• **Advances in medical treatments:** With the eradication of serious infectious diseases such as mumps and measles, and great strides being made in fighting once-fatal afflictions like cancer, the overall life expectancy of Americans has increased. However, increased longevity has created its own set of issues and drawbacks, particularly the chance of developing a chronic condition or disability. Currently, chronic diseases are the leading causes of disability and death in the nation, and account for three-quarters of the nation’s total healthcare costs. More than two-thirds of all deaths are due to five leading chronic diseases — heart disease, cancer, stroke, chronic obstructive pulmonary disease, and diabetes. At the same time, medical advancements virtually ensure that cancer, heart attacks and strokes are more likely to disable an individual than to cause death before the age of 65. So while Americans may be living longer, they are not necessarily living healthier.

• **Deteriorating lifestyles:** The presence of risk factors associated with chronic disease, such as smoking, obesity, lack of exercise and diabetes, increases healthcare costs by 300% to 400%. However, many of these major risk factors are preventable and are the consequences of lifestyle choices. For example, a single behavior — tobacco use — is responsible for more than 80% of deaths each year from chronic obstructive pulmonary disease, the nation’s fourth leading cause of death.

Of particular concern is the rise in the number of overweight and obese individuals. In 2005, among the total U.S. adult population surveyed, 60.5% were overweight; of those who were overweight, 23.9% were obese and 3.0% were extremely obese. According to the Center for Disease Control the rate of obesity has more than doubled in the past two decades. Apart from the physical limitations caused by an increase in weight, there are a host of associated medical conditions, such as heart disease, high blood pressure, diabetes, arthritis-related disabilities and certain cancers. The costs associated with obesity are daunting with direct and
indirect costs, such as loss of income from decreased productivity and absenteeism, exceeding $100 billion. Even with health insurance, overweight and obese individuals tend to pay more in healthcare costs than those of normal weight.

**Impact of increasing healthcare costs on employees**

With employment-based health insurance premiums more than doubling since 1997, the proportion of Americans with access to employer-based health insurance benefits has been steadily declining since 2000. And with premiums rising five times faster, on average, than workers’ earnings since 2000, the percent of workers participating in their employer’s plan has also been dropping. The number of uninsured Americans has now reached nearly 45 million. Financial pressures, due to the high cost of health insurance coverage, are the primary reason behind the growing number of uninsured.

Given this, it is not surprising that affordable health care tops the list of employee financial concerns, with nine out of 10 employees in a recent LIMRA survey citing this as an issue. The related issues of having enough money in the event of illness, injury or disability are also key employee concerns.

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**Figure 2**

**Top Employee Financial Concerns**

- Having affordable health insurance to meet employee needs: 90%
- Having enough money to live on in retirement: 82%
- Having enough money to afford healthcare during retirement: 79%
- Having enough money if employee or his/her partner/spouse becomes critically ill: 77%
- Paying for medical care if employee or his/her family member becomes sick or injured: 75%
- Having enough money if employee or his/her partner/spouse becomes disabled: 74%
- Providing for a spouse/family if employee dies unexpectedly: 60%

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From the employers’ perspectives, the preferred cost-containment approach is to increase employees’ share of premiums as well as their out-of-pocket expenses. While this may be the preferred tactic, employers recognize that there is a limit to how much cost can be shifted to employees. Many fear that their employees will consider dropping healthcare coverage because of the increase in out-of-pocket expenses, leading to a further increase in the uninsured population.28

Government intervention
Recognizing the problem of a growing uninsured population, various government entities are beginning to take a more active role in addressing issues of healthcare access and affordability. While there is unanimous agreement on the nature of the problem, there is little consensus as to the best way to expand health insurance coverage. Since a federally funded universal healthcare system is unlikely, policymakers are debating, and in some cases, enacting different approaches to reform. Following the lead of Massachusetts and Maryland, 15 states are currently considering employer-mandated insurance plans, where employers would be required to bear at least a portion of their employees’ healthcare bills. At the federal level, tax-advantaged saving accounts have been created. The government also proposed — although it was unsuccessful — legislation that would allow employers to band together across state lines in order to receive a better deal on health insurance.

Need for consumer education
Regardless of the healthcare reforms to come, many experts believe that the only way to truly rein in healthcare costs is to increase consumers’ financial responsibility and involvement in their healthcare choices. In addition, promoting healthy behavioral choices, through education and through community policies and practices, is essential to reducing the burden of chronic diseases.29

B. Increasing Diversity in the Workplace

A number of key demographic and cultural shifts have been taking place that significantly impact both culture and economics in the workplace. These include:

- an aging workforce;
- multi-generational workforce;
- increased demand for work-life balance;
- changing household composition and definition of “family”;
- increased ethnic diversity.

These shifts are requiring employers to understand and manage an increasingly diverse array of employee expectations and needs.
Aging Workforce

Older workers staying in labor force
The aging of the baby boomers will have a profound impact on the composition of the labor force in the coming years. Between 2004 and 2014, the 55-and-older age group is expected to grow at an annual rate of nearly four times that of the overall labor market. Conversely, the proportion of youngest workers in the labor force, those age 16 to 24, as well as prime-age workers, 25 to 54, will decline.

Figure 3
Aging Workforce, 2004 to 2014
Projected Growth of Age Segments in Labor Force from 2004-2014


In addition to the natural growth of the older worker segment, a growing proportion of older workers are remaining in the workforce beyond traditional retirement years. Between 1993 and 2005, labor force participation rates for men 65 to 69 increased from 25% to 34%, and for women the rates increased from 14% in 1985 to 24% in 2005.30

Baby boomers are redefining what it means to retire. To them, retirement may no longer be seen as a time to withdraw from working life, but a time...
to find a new life balance that includes working on their own terms. The majority of workers today say they plan to work during retirement for an average of nine years. Nearly half of those who plan on working never intend to stop working completely.

For many boomers, continuing to work will be a lifestyle choice that allows them to stay active and productive. However, there will also be a significant group that continues in the labor force out of financial necessity, amid fears over cutbacks in Social Security, not having enough money to live on, and not being able to afford health care.
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Keeping older workers in the workforce

There has been much debate, to date, as to the effect baby boomer retirements will have on any potential future labor and talent shortages in the next 25 years. Some economists agree that a labor shortage is inevitable, perhaps starting as early as 2011. If that occurs, the United States could face a shortage of 35 million workers, if current trends continue. The biggest concern for employers in such a scenario is the potential loss of highly skilled workers.\(^3\)

If the projected talent shortage does materialize, it will be imperative for employers and the government to incentivize older employees to stay in the workforce. At the employer level, there will be a need for comprehensive reviews of employee benefits in order to identify and implement benefits and programs that appeal to older workers. At the government level, Social Security disincentives will need to be addressed.

Health status of older workers

Regardless of the motivations, the ability of older workers to stay in the workforce depends on circumstances beyond their control. Almost seven in 10 workers (67%) expect to work into retirement.\(^3\) However, the reality is that four in 10 retirees say they ended up having to leave the workforce earlier than expected due to company downsizing, health problems or disabilities.\(^3\)

The Unum database of disability claims indicates that workers older than 40 account for 50% of all short term disability claims and as much as 75% of all long term disability claims.\(^3\) Nearly one in four workers between the ages of 55 and 64 has a disability.\(^3\) The Unum database also shows that

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Figure 5
Reasons for Continuing to Work in Retirement

<table>
<thead>
<tr>
<th>Reason</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Will keep me mentally active</td>
<td>60%</td>
</tr>
<tr>
<td>Will keep me physically active</td>
<td>52%</td>
</tr>
<tr>
<td>The money</td>
<td>47%</td>
</tr>
<tr>
<td>Will keep me connected with others</td>
<td>43%</td>
</tr>
<tr>
<td>The health insurance benefits I will receive</td>
<td>38%</td>
</tr>
<tr>
<td>Will provide a sense of identity or self-worth</td>
<td>38%</td>
</tr>
<tr>
<td>Will provide new challenges</td>
<td>35%</td>
</tr>
</tbody>
</table>

while workers age 40 and older experience lower incidences of work injuries, short term disability and unscheduled absences than younger workers, the average amount of time they miss due to an injury or illness is greater by nearly a third.\textsuperscript{39}

Currently, the primary drivers of long-term impairments for the older worker are musculoskeletal disorders (29\%), cancer (17\%), and cardiovascular disorders (11\%).\textsuperscript{40}

\begin{figure}
\centering
\includegraphics[width=\textwidth]{chart.png}
\caption{Primary Drivers of Missed Work for 40+ Age Group}
\end{figure}


In terms of cost, heart conditions are the most costly in the over-40 age group, followed by trauma-related conditions, cancer, hypertension and other CNS disorders. Most disability cases also involve multiple medical conditions; nearly 60\% involve three or more. Cases with multiple medical episodes are significantly more expensive, costing on average 24\% more than cases with just one medical episode.\textsuperscript{41}
In terms of business costs, lost productivity associated with disability absences averages $22,800 per disability claim, compared with $13,600 for medical costs and $3,800 for disability payments. Musculoskeletal disability cases are the biggest lost-productivity driver.42

**Multi-Generational Workforce**

For the first time in history, many organizations have workforces that comprise four distinct generations:

- **Matures/Traditionalists** (ages 60 to 78) grew up in tough economic times during the Great Depression and World War II. Matures value hard work. They are dedicated — not just to doing a good job or making themselves look good, but to helping the organization succeed and getting customers what they need. They are great team players, carry their weight and don’t let others down.43

- **Baby Boomers** (ages 41 to 59) grew up during an era of economic prosperity and experienced the tumult of the 1960s at an impressionable age. Baby boomers tend to be optimistic, idealistic and good team players. They are driven, love challenge and build stellar careers. Because they have had to compete with each other at every step of their careers, they can be highly competitive.44
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- **Generation X (ages 28 to 40)** witnessed their parents’ experiences with corporate downsizing and restructuring in the 1970s and ‘80s. They value flexibility, work-life balance and autonomy on the job, and appreciate a fun, informal work environment. They are constantly assessing how their careers are progressing and place a premium on learning opportunities. They are technologically savvy, eager to learn new skills and comfortable with change at work.\(^45\)

- **Generation Y/Nexters** (age 27 and younger) tend to be well organized, confident, resilient and achievement-oriented. They are excellent team players, like collaboration and use sophisticated technology with ease. They are comfortable with, and respectful of, authority and relate well to people who are older. They want to work in an environment where differences are respected and valued, where people are judged by their contributions and where talent matters.\(^46\)

Matures and baby boomers make up well over half the American workforce, while Generations X and Y comprise approximately 44% of the labor market, according to the Department of Labor.\(^47\)

Members of each generation bring distinct sets of values, attitudes and behaviors to the workplace, largely as a result of the era in which they grew up. From an employer’s view, the biggest generational differences they see are in communication styles, attitudes about work and life, work styles, comfort with technology, views regarding loyalty and authority and acceptance of change.\(^48\) For example, baby boomers, like their predecessors, tend to believe in the value of hard work and view it as necessary for moving up the ladder of success. And genXers are more demanding of the need for balance in their lives to achieve physical, mental and financial health.\(^49\)

**Work-Life Balance**

While the demand for work-life balance has been primarily identified as an attribute of the genXers, there are growing similarities in the generations’ desire for this balance. For example, more and more baby boomers are finding themselves needing increased time for caregiving responsibilities as they become “sandwiched” between the needs of their children and those of their aging parents. Among primary caregivers defined as the “Sandwich Generation,” more than half — 58% — of those who are age 25 to 64 are employed. Of the remaining primary caregivers who are not working, 56% once worked but stopped while providing care.\(^50\) Many caregivers report arriving for work late, leaving early and taking personal or vacation time to attend to their caregiving duties.\(^51\) The National Council on Aging found that 25% of employees caring for elderly family members who lived an hour or more from the office “missed at least one day of work each month,” and 15% “took unpaid leave.”\(^52\) The indirect
costs also include the potentially heavy physical, emotional and professional tolls that this takes on the caregiver.

The importance placed on work-life balance is also increasingly crossing gender lines, as expectations related to the sharing of childbearing responsibilities have shifted. The Society for Human Resource Management (SHRM) found that both men and women rate work-life balance in the top five categories for job satisfaction.\(^5\)

**Changing Household Composition**

The composition of American households has changed. As marriage rates declined during the past several decades due to rising divorce rates and singles deciding to forgo marriage, the number of single individuals has grown dramatically.\(^5\) According to the U.S. Census Bureau, single Americans now outnumber married couples with children. Married couples currently make up only half of the population, married couples with children account for less than a quarter of U.S. households,\(^5\) and the incidence of unmarried cohabitation increased ten-fold from 1970 to 2004.\(^5\) Moreover, many Americans who are considered to be single today have similar responsibilities and concerns as their married counterparts — nearly three in 10 children were living with a single parent in 2001.\(^5\)
Ethnic Diversity

Over the next decade, the labor force will become more ethnically diverse. The Hispanic labor force currently represents 13% of the labor force; this is expected to increase to 16% by 2014, with immigration being the main driver of this growth. The Asian population as a percentage of the labor force will also grow somewhat, from 4% currently to 5% over the next decade, again with immigration as the primary driver. Immigration will significantly impact the composition of the labor force, as the demographic characteristics of the foreign-born labor force differ significantly in many respects from those of U.S.-born labor force. Foreign-born workers are more likely to be younger, male, without a high school diploma, and employed in service occupations than is the U.S.-born labor force.

Not surprisingly, this increasing ethnic diversity will be more apparent in some regions of the country than others. Nearly two-thirds of new immigrants settle in one of six states: California, New York, Florida, Texas, New Jersey and Illinois.

II. Benefit Trends/Issues

A. The Shift Toward “Employee-Centric” Benefits

An overarching trend in the employee health and financial benefits domain has been the shift toward “employee-centric” benefits that increasingly emphasize consumer choice and consumer responsibility, as well as shifting risk from the employer to the employee. This is seen most clearly with the introduction of voluntary employee-paid benefits in the 1990s, the shift in employer-sponsored retirement plans from defined benefit plans to defined contribution plans, and the rise of consumer-driven health plans.

However, a critical issue for the industry is that while employers are increasingly shifting the responsibility for their employees’ health and financial well-being onto the employees themselves, many individuals appear to be ill-prepared to accept this challenge without assistance.

Voluntary Benefits

Today, more than half (52%) of U.S. employers with ten or more employees offer voluntary worksite benefits. The most-often cited reasons for offering voluntary benefits are to improve worker morale and satisfaction without adding direct cost to the company, and to attract/retain employees. The most common benefits being offered are
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cancer insurance (29%), accident (24%), short term disability (20%) and supplemental medical (20%).

Some brokers feel that in the future, rising healthcare costs will diminish employees’ willingness to pay for additional benefits. However, others have observed employers adding voluntary benefits to offset changes being made to their medical benefits. For the most part, voluntary benefits are not intended to replace ones that already exist, but instead will provide additional types of coverage for employees. And benefits such as supplemental medical, long term care insurance, dental, critical illness and cancer benefits afford employers the ability to enhance their medical benefit at little to no cost and without fear of additional enrollment and administrative burdens.

**Voluntary benefits and the small employer market**
While larger employers are more likely to offer voluntary worksite benefits to supplement their core benefits package, smaller businesses look to
voluntary worksite benefits as a way to offer an attractive benefits package without reducing profits and to help with health costs. Because of their limited resources, small employers are more focused on managing premium increases in a world of finite benefit dollars, and are not looking to add new benefit dollars; rather their focus is on offerings that will likely benefit a majority of employees. In particular, smaller-sized firms show stronger interest in critical illness insurance, prescription discount cards and supplemental medical insurance than in other voluntary benefits. 64

However, currently the percent of small businesses (<100 employees) offering voluntary benefits is low: only 13% offer employees such programs. Two primary factors contribute to this low rate: 1) employers are not knowledgeable about these programs and the benefit to the business and employees, and 2) small businesses are not being approached by sales professionals. 65

**An emerging need: long term care insurance**

A particular area of growth in the voluntary benefits market is long term care insurance (LTC). As life expectancy increases and as the baby boom generation ages, the proportion of the population that needs long term care will also increase. Fifty-eight percent of men turning 65 will need long term care sometime before they die; for women, that percentage increases to 79%. 66 Much of the care will be provided by family members; however, the availability of unpaid, informal assistance and services from extended family will decrease in coming decades. It is estimated that by 2020, the number of elderly who will be living alone with no living children or siblings will reach 1.2 million, almost twice the number without family support in 1990. In addition, geographic dispersion of families may further reduce the number of unpaid caregivers available to elderly baby boomers. 67

Given this trend, the need for, and access to, LTC is increasing, and the Bureau of Labor Statistics surveys have shown a slow, steady rise in the proportion of employees with access to LTC. In 1989, LTC was offered to just 3% of full-time private industry employees of large employers; by 2006, that figure had grown to 20%. 68

Long term care insurance is also on the radar of the federal government, which is looking at this as one solution to Medicaid solvency and funding issues by making it more difficult to qualify for Medicaid (to reduce government expenditures), while making the purchase of LTC more attractive (thereby moving financial responsibility for long term care expenses to the private sector). Recently passed legislation underscores the government’s stance regarding where the financial responsibility for long term care expenses lie. The Deficit Reduction Act of 2006 tightens the restrictions on Medicaid eligibility by changing the transfer of assets look-back period from three to five years and replaces the unlimited home exemptions with a cap. Under the act’s partnership provision, which expands the plans to all 50 states, an individual could purchase an LTC
policy approved by his or her state and later qualify for Medicaid while protecting his or her assets on a dollar-for-dollar basis.

Also expected to incent purchase of LTC insurance, the Pension Protection Act of 2006 allows for the purchase of long term care coverage on a tax-deferred basis by including it with an annuity or permanent life insurance. And federal legislation recently introduced would allow — if enacted — for the inclusion of an LTC product in a section 125 cafeteria plan, encouraging employees to purchase LTC policies at a younger age and at a more affordable price.

Retirement Benefits

Defined benefit pensions and defined contribution plans
In recent decades, there has been a movement away from traditional defined benefit (DB) pension plans. Today there are approximately 48,000 insured DB plans compared to 170,000 plans 20 years ago. Reasons for this decline include increasingly complex and inflexible plan-funding rules, economic downturns, company efforts to “de-risk” themselves, and changes in the rules governing pension accounting. Because the trend away from DB plans does not appear to be abating, and to address the weaknesses inherent in the current pension insurance system, the 2006 Pension Protection Act was enacted. The legislation requires additional employer contributions during the next seven years and sets stricter rules to ensure appropriate pension plan-funding levels in the future. However, high plan costs, competitive pressures and frequent job turnover all signal an economic reality that is not consistent with the fundamental value proposition of a traditional pension plan.
With the decline in DB plans, there has been a commensurate proliferation of defined contribution (DC) retirement plans such as 401(k) plans. Fifty-four percent of private-industry workers have access to defined contribution plans; among those, 79% (on average) choose to participate. This compares to only 22% of workers who have access to a defined benefit plan at their place of employment. 71

Overall, however, the percentage of employees participating in any retirement plans, whether DB or DC, has declined. Ninety-one percent of full-time employees in medium and large firms participated in employment-based retirement plans in 1985; this dropped to 67% in 2004. 72 Availability of employer-sponsored retirement plans is a particular issue for employees in small businesses: financial constraints and requirements for administering retirement savings plans discourage many small businesses from offering them to their employees. As a result, less than one-third of small-business employees have a retirement plan. Only 23% of workers at firms with fewer than 25 employees and 41% of workers at businesses with 25 to 99 workers participated in an employment-based retirement plan in 2003, compared to an average participation rate of American workers of 51%. 73

**Individual retirement savings**

In general, changes to pension and retirement benefits are occurring at a time when people are saving less and charging more. The average American household maintains just $3,800 in savings\(^7^4\) and carries more than $8,000 in annual credit card debt.\(^7^5\) According to the Commerce Department, the nation’s personal savings rate for 2006 was negative 1%, the worst showing in 73 years — since the Depression.\(^7^6\) Nearly one-quarter of Americans are living paycheck to paycheck, with no money left once they have paid essential living expenses, and U.S. household debt is at a record high relative to disposable income.\(^7^7\) Given these statistics, it is not surprising that a LIMRA 2005 Employee Benefits Study revealed that 34% of employees are not saving anything toward retirement on an annual basis: this proportion translates into more than 44 million employees who are not preparing themselves for retirement.\(^7^8\) And at the present, one in five Americans nearing retirement lacks any type of a retirement fund at all.\(^7^9\)

**Consumer-Driven Health Plans (CDHPs)**

As healthcare costs have increased, employers have sought relief through various healthcare plan designs. One design offering the most promise is consumer-driven health plans, which seek to put the consumer (e.g., the employee) in charge of his or her own health by shifting some of the costs and risks associated with healthcare to him or her. The theory is that consumers use too many healthcare services because they do not have a financial stake in their healthcare. By exposing them to more of the risk and giving them the appropriate tools — such as access to cost and quality information, wellness and disease management programs, health information and coaching and financial tools — individuals will learn to consume healthcare as they consume other goods and services.

In some cases a savings account — either a health reimbursement account (HRA) or a health savings account (HSA) — can be offered to the employee to help fund care prior to reaching the plan’s deductible. HRAs are national accounts funded solely by the employer. HSAs are employee-owned and can be funded by either the employer or the employee.

A high deductible health plan with a savings option of either an HRA or HSA is the plan design most associated with consumer-driven healthcare; however, according to the latest Kaiser/HRET employer study, just 7% of all employers currently offer these plans.\(^8^0\) Most employers have been reluctant to implement these benefits due to a lack of experience with the product. It will take a few more years of data before it is known for sure if the plans save money. Currently they appear to be helping restrain cost increases, not necessarily saving money. There are also concerns that the appropriate tools that employees need to make informed decisions are not sufficiently in place, and that employees may skimp on care when they are paying for it out of pocket, impacting longer-term health trends. What is known for certain is that the concept of consumer-driven healthcare is on the radar screen of most mid-sized and larger employers.\(^8^1\)
Consumer Understanding of Benefits

While employers are increasingly shifting the responsibility for their employees’ health and financial well-being onto the employees themselves, a critical issue for the industry is employees’ lack of awareness and understanding of the benefits available to them. Research confirms a substantial lack of knowledge among consumers around even the basics of insurance benefits. Consumers struggle with understanding the different types of insurance, how insurance is relevant to them and their life situations, and knowing how much coverage to purchase, how to obtain accurate information, and who to buy from.

Employers believe that most employees do not entirely understand their benefits or the value of their benefits. As indicated in a 2005 LIMRA survey of employers, only one in three employers believe that at least half of their employees are very knowledgeable at making medical insurance decisions. For disability benefits, far fewer employers assess their employees’ knowledge even at this low level. According to employers, in many cases employees seem to overestimate their basic knowledge of benefits, and perhaps more importantly, underestimate the likelihood of a health risk becoming a reality.

Employees also lack basic knowledge around the cost of benefits. In a 2005 employee survey, fewer than two in 10 employees were able to correctly identify the annual cost of their benefits.82

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**Figure 11**

The Knowledge Gap: How Well Do Employees Understand Benefits Costs

<table>
<thead>
<tr>
<th>Benefit</th>
<th>Do not know</th>
<th>Incorrectly identified cost</th>
<th>Correctly identified cost</th>
</tr>
</thead>
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<td>STD</td>
<td>66</td>
<td>26</td>
<td>8</td>
</tr>
<tr>
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</tr>
<tr>
<td>Medical</td>
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This knowledge gap may lead to a certain amount of inertia in decision-making. It appears that employees approach the benefits decision-making process with little engagement. Choices are often limited, but even when they do exist, many employees admit they make choices more on “faith” than by any systematic examination and deliberation. In addition, it is clear that employees spend a relatively short amount of time when it comes to making decisions about benefits, and tend to focus more on the short-term than on the long-term. They also tend to view benefits within the context of their overall spending patterns, in effect weighing benefit costs against a wide variety of other “indispensable” expenses, ranging from childcare or college tuition, to new car purchases, monthly cable TV costs and cell phone bills. Only medical and dental are considered by employees to be non-discretionary benefits.

This inertia may also lead to complete inaction: nearly one-third of adults have admittedly done nothing to ensure that their finances are handled properly if they should become incapacitated or die.

Overall, while employers are increasingly shifting the responsibility for benefits decision-making onto employees, most are ill-prepared to accept this challenge without assistance. Clearly, comprehensive employee education is critical to employees’ effective use of programs, services, and benefits.

B. Managing Employee Health and Productivity

Disease Management & Wellness Programs

With estimates of total health and absence costs exceeding 20% of payroll, employers have increasingly been turning to initiatives such as disease management (DM), care management and wellness programs to help curb healthcare and disability expenses, reduce absenteeism and improve productivity and presenteeism. According to a 2004 study by the American Management Association, 80% of executives feel that corporate America has a responsibility to promote wellness.

Currently, larger employers are substantially more likely than smaller employers to offer disease management and wellness services, as evidenced in Figure 12.
Unfortunately, difficulties in tracking return on investment (ROI) and actual cost-savings of the programs are proving to be obstacles for employers, leading them to have mixed feelings about the efficacy of at least some of these programs. For example, according to a 2003 survey of employers, among those who currently offer wellness benefits, just less than half rate the effort as somewhat or extremely effective at lowering claims, improving the quality of care, reducing hospital stays, reducing trips to the emergency room or lowering the costs of absenteeism. Only one in 10 employers anticipates adding disease management and wellness services in the future.\textsuperscript{88}
Despite employer reluctance, a number of studies have shown positive ROI for disease management programs. For example, in a review of 44 studies analyzing the economic impact and ROI for disease management programs, researchers found positive ROI for programs targeting congestive heart failure, as well as for programs targeting multiple health and disease conditions. Mixed results were found for programs targeting depression, diabetes and asthma.89

Management of Absence

An additional concern to employers is the rise in employee absenteeism. According to the 16th annual CCH Unscheduled Absence Survey, the 2006 absenteeism rate was 2.5%, up from 2.3% in 2005, and the highest since 1999 when the rate was 2.7%. Nearly one-third of the companies surveyed report that absenteeism is a “serious problem,” and nearly all (92%) state that they think the problem may stay the same or worsen in the next two years.90

Managing employee absenteeism can be a substantial administrative challenge for employers. For example, in the case of the Family and Medical Leave Act (FMLA), employers need to manage the complexities of FMLA regulations in combination with potentially overlapping state leave, workers’ compensation (WC) and short term disability (STD) policies. In a recent survey, 51% of employers said they have experienced challenges in administering/granting “medical leave” under the Family and Medical Leave Act.91 Recent research findings also indicate that nearly half of all FMLA leave-takers do not provide sufficient notice before a leave is taken,92 creating substantial difficulties for employers in tracking leave and adjusting their employees’ work schedules to accommodate the leave-taker’s absence.

In addition to administrative repercussions, employee absenteeism can have a substantial financial impact for businesses. A Hewitt Associates survey found that companies that monitor sick leave costs estimate the potential impact to be between 1% and 3% of payroll. For a company with $450 million in payroll, the cost of sick leave could be between $4.5 million and $13.5 million per year. Including all types of paid leave (sick time, vacation and disability), the overall costs could reach an estimated 9% of payroll, or $40.5 million in paid leave expenses.93

However, despite the financial ramifications of employee absence, the Hewitt survey found that employers do not effectively track or manage employees’ time away from work, and most companies surveyed did not know the financial cost associated with absences.94 The 2005 JHA Absence Management Survey found similar results: only 12% of companies participating in this survey actually tracked the cost of absenteeism.95

The JHA survey also revealed that larger companies have more difficulty tracking absences than smaller companies. Forty-three percent of
companies that employ 500 or more employees reported they do not know the average number of unscheduled absences per employee, compared to 27% of companies that employ 2-99 employees. Issues such as multiple tracking systems, inconsistencies with how supervisors are reporting absences and lack of management support impact the ability of larger companies to accurately monitor lost time.\textsuperscript{96}

A corollary to employee absenteeism is the issue of employee “presenteeism,” when an employee is at work but unable to perform at expected levels due to health, family or employee relations issues.\textsuperscript{97} Presenteeism is an area of growing concern for organizations; more than half (56%) of employers surveyed in the CCH Unscheduled Absence Survey reported that presenteeism is a problem in their organizations, up from 48% in 2005 and 39% the year prior.\textsuperscript{98}
III. Summary and Implications

A. Broad Trends Affecting the Workplace

Rising Healthcare Costs

The rising cost of healthcare and health insurance premiums continues to be a major challenge for both employers and employees.

- With healthcare premiums more than doubling in the past decade, controlling healthcare costs is at the forefront of pressures facing employers. And with premiums rising five times faster, on average, than workers’ earnings since 2000, the percent of workers able to participate in their employers’ plans has been dropping. The current number of uninsured Americans is estimated at nearly 45 million.

- Although healthcare reform efforts are underway at a government level, many experts believe that the only way to truly rein in healthcare costs is to increase consumers’ financial responsibility and involvement in their healthcare choices.

Increasing Diversity in the Workplace

A number of key demographic and cultural shifts have been taking place over the past several decades that are significantly impacting both culture and economics in the workplace, and are requiring employers to understand and manage an increasingly diverse array of employee needs and expectations.

- The aging workforce: The aging of the baby boomers will have a profound impact on the composition of the labor force; not only is the 55-and-older age group growing at an annual rate of nearly four times that of the overall labor market, but a growing proportion of older workers are remaining in the workforce beyond traditional retirement years, either out of financial necessity or the desire to stay active and productive.

- Multi-generational workforce: For the first time in history, many organizations have workforces that comprise four different generations. Members of each generation bring distinct sets of values, attitudes and behaviors to the workplace, particularly in the areas of communication styles, work styles, comfort with technology, views regarding loyalty and authority and acceptance of change.
• **Attitudes about work-life balance**: Although different generations in the workforce have traditionally had different attitudes toward work-life balance, the desire for balance is now crossing both generational and gender boundaries. As more and more baby boomers are finding themselves caregivers for both their children and their aging parents, and as expectations related to the gender roles in child-rearing have shifted, the need for work-life balance has become salient for an increasing proportion of workers.

• **Changing household composition**: The number of single individuals has grown dramatically over the past several decades; with rising divorce rates and declining marriage rates, the number of single people is almost equivalent to the number of married people. However, many individuals who are considered “single” have similar responsibilities and concerns as their married counterparts — nearly three in 10 children were living with a single parent in 2001.

• **Ethnic diversity**: Over the next decade, the labor force will become increasingly ethnically diverse as Hispanics and Asians become a greater proportion of the labor force. Immigration is the primary driver of this growth, and also impacts the age distribution of the labor force, as immigrants tend to be in the younger age categories.

**B. Benefit Trends/Issues**

**The Shift Toward “Employee-Centric” Benefits**
An overarching trend in the employee benefits arena has been the shift toward “employee-centric” benefits that increasingly emphasize consumer choice and consumer responsibility, as well as a shift risk from the employer to the employee. This is seen most clearly with the introduction of voluntary employee-paid benefits in the 1990s, the shift in employer-sponsored retirement plans from defined benefit plans to defined contribution plans and the rise of consumer-driven health plans.

• **Voluntary benefits**: Today, more than half of U.S. employers currently offer voluntary worksite benefits to their employees — voluntary benefits represent a way to satisfy increasingly diverse employee needs, control costs and shift risk from employer to employee. The most common benefits offered are cancer, accident, supplemental medical and short term disability insurances.

Not surprisingly, larger companies are more likely to offer voluntary benefits than smaller companies, and the percent of small businesses (with fewer than 100 employees) offering voluntary benefits is quite low: only 13% offer employees such
programs. Two primary factors contribute to this low rate: 1) employers are not knowledgeable about these programs and the benefit to the business and employees; and 2) small businesses are not being approached by sales professionals.

An emerging need in the voluntary benefits arena is long term care insurance; as life expectancy increases and the baby boom generation moves into its elder years, an increasingly large portion of the population will need long term care. There has already been a steady rise in the percent of employers offering long term care insurance, and the need for this insurance will continue to increase. Long term care insurance is also on the radar of the federal government as one solution to Medicaid solvency and funding issues.

- **Retirement benefits:** In recent decades, there has been a movement away from traditional defined benefit pension plans toward defined contribution retirement plans. Reasons for this decline include increasingly complex and inflexible plan funding rules, economic downturns, company efforts to “de-risk” themselves and changes in the rules governing pension accounting.

However, while the percent of workers participating in defined contribution retirement plans is increasing, the overall percentage of employees participating in at least one employer-based retirement plan has been steadily declining. Changes to pension and retirement benefits are occurring at a time when consumers are saving less and charging more. The average American household maintains just $3,800 in savings and carries more than $8,000 in annual credit card debt, 34% of employees are not saving anything toward retirement on an annual basis and, at the present, one in five Americans nearing retirement lacks any type of a retirement fund at all.

- **Consumer-Driven Health Plans (CDHPs):** As healthcare costs have increased, employers have sought relief through various healthcare plan designs, including consumer-driven health plans, which seek to put the employee in charge of his or her own health by shifting some of the costs and risks associated with healthcare to him or her. However, data is not yet available demonstrating the extent to which these plans save money, and there is concern that employees will skimp on care when they are paying for it out of pocket, impacting longer-term trends. What is known for certain is that the concept of consumer-driven healthcare is on the radar screen of most mid-sized and larger employers.

- **Consumer knowledge of benefits:** Perhaps one of the most critical issues for the industry is that while employers are increasingly shifting the responsibility for their employees’ health and financial well-being on the employees themselves, many
employees appear to be ill-prepared to accept this challenge without assistance. A growing body of research demonstrates that there is a substantial lack of knowledge among consumers around the basics of insurance and other benefits. Consumers struggle with understanding the different types of insurance, how insurance is relevant to them and their life situations, knowing how much coverage to purchase and knowing how to obtain accurate information.

Consumers also demonstrate a fair amount of inertia in benefit decision-making, spending a relatively short amount of time making benefit-related decisions and focusing more on the short term than the long term. They tend to view benefits within the context of their overall spending patterns, in effect weighing benefit costs against a wide variety of other “indispensable” expenses. Only medical and dental insurances are considered by employees to be non-discretionary benefits. This inertia may also lead to complete inaction — for example, nearly one-third of adults have admittedly done nothing to ensure that their finances are handled properly should they become incapacitated or die.

Managing Employee Health and Productivity

- **Disease management and wellness programs:** With estimates of total health and absence costs exceeding 20% of payroll, employers have increasingly been turning to initiatives such as disease management, care management and wellness programs to help curb healthcare and disability expenses, reduce absenteeism and presenteeism, and improve productivity. Unfortunately, difficulties in tracking ROI and actual cost-savings of the programs are proving to be major obstacles for employers, and employers are of mixed feelings about the efficacy of at least some of these programs.

- **Management of Absence:** The rate of employee absenteeism is on the rise, and one in three companies reported in 2005 that absenteeism is a “serious problem.” Despite the fact that absenteeism has a substantial financial impact on businesses — one study places the costs of paid leave as much as 9% of payroll — most companies do not effectively track absenteeism or know the financial costs associated with employees’ time away from work.

A corollary to employee absenteeism is the issue of employee “presenteeism,” when an employee is at work but unable to perform at expected levels due to health, family or employee relations issues. Presenteeism is an area of growing concern for organizations.
C. Implications

Controlling healthcare costs will continue to be of primary concern to employers, and will continue to significantly impact how employee benefits are evaluated, purchased, administered, and managed. Employers will need to be more strategic in both managing costs and finding employee-valued benefit offerings, and they will continue to look for new strategies and tools to manage this.

As the workforce grows older, employers will need to consider a number of changing corporate realities, including increased medical costs, increased demand for unique transitions from work to retirements (e.g., part-time work, job sharing and flexible schedules) and increased attention to the prevention and management of critical illness, chronic disease and impairment.

The workforce of the future will be diverse — from age to ethnic group to family status — and employers will need to have a clearer understanding of the composition of their workforces for effective recruiting, motivation and retention. Employees at different life stages and with different cultures and family situations will have different and changing benefit needs, and employers will need to have a flexible range of benefits to accommodate this. The one-size-fits-all benefit plans will no longer work for a diverse population.

Employees are being increasingly asked to bear responsibility for making decisions about benefits related to their health and financial well-being. However, employee misperceptions and lack of knowledge are major roadblocks to appropriate decision-making. Employees require ongoing education, informational tools and support to truly understand their benefits, understand how the benefits are relevant to them, and feel comfortable making purchasing decisions.

As employers increasingly recognize the financial costs of employee absence to their businesses, they will look for new strategies and tools for efficiently tracking time and costs, reducing the administrative burden of absence management, reducing lost time and increasing employee productivity.
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