Strategies for Bolstering Your Employer Value Proposition

A Discussion on Total Rewards

Arthur J. Gallagher & Co.
BUSINESS WITHOUT BARRIERS™

TR/Strategy – Mid-South Benefits (Nashville) — May 15, 2015

It's All About *Talent*

Strategies for Bolstering Your Employer Value Proposition

A Discussion on Total Rewards

Arthur J. Gallagher & Co.
BUSINESS WITHOUT BARRIERS™

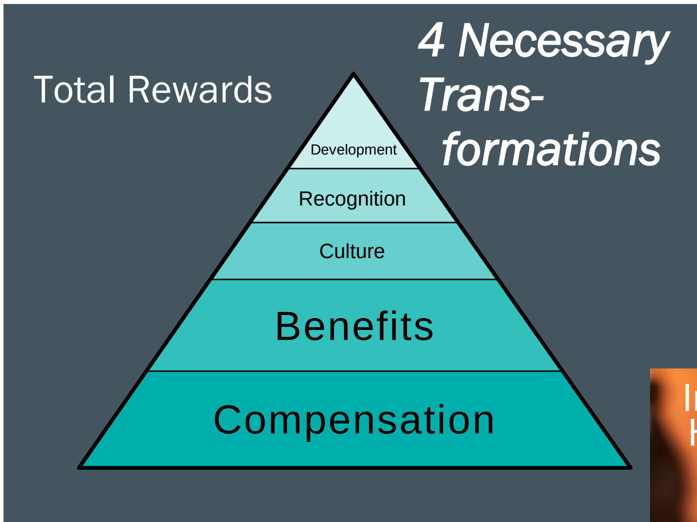
Keith A. Friede
Area V.P., Talent & Organization Development
North Central Region Practice Leader
3600 American Boulevard, Suite 500
Bloomington, Minnesota 55431
952.356.0700
keith_friede@ajg.com
www.linkedin.com/in/keithfriede
@keithfriede

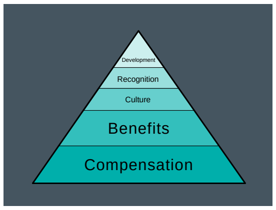
5205 Maryland Way
Suite 300
Brentwood, TN 37027
615.244.8484
www.ajg.com
www.ajg.com/locations/tennessee/brentwood

TR/Strategy – Mid-South Benefits (Nashville) — May 15, 2015

Four Areas of Focus

Session Agenda

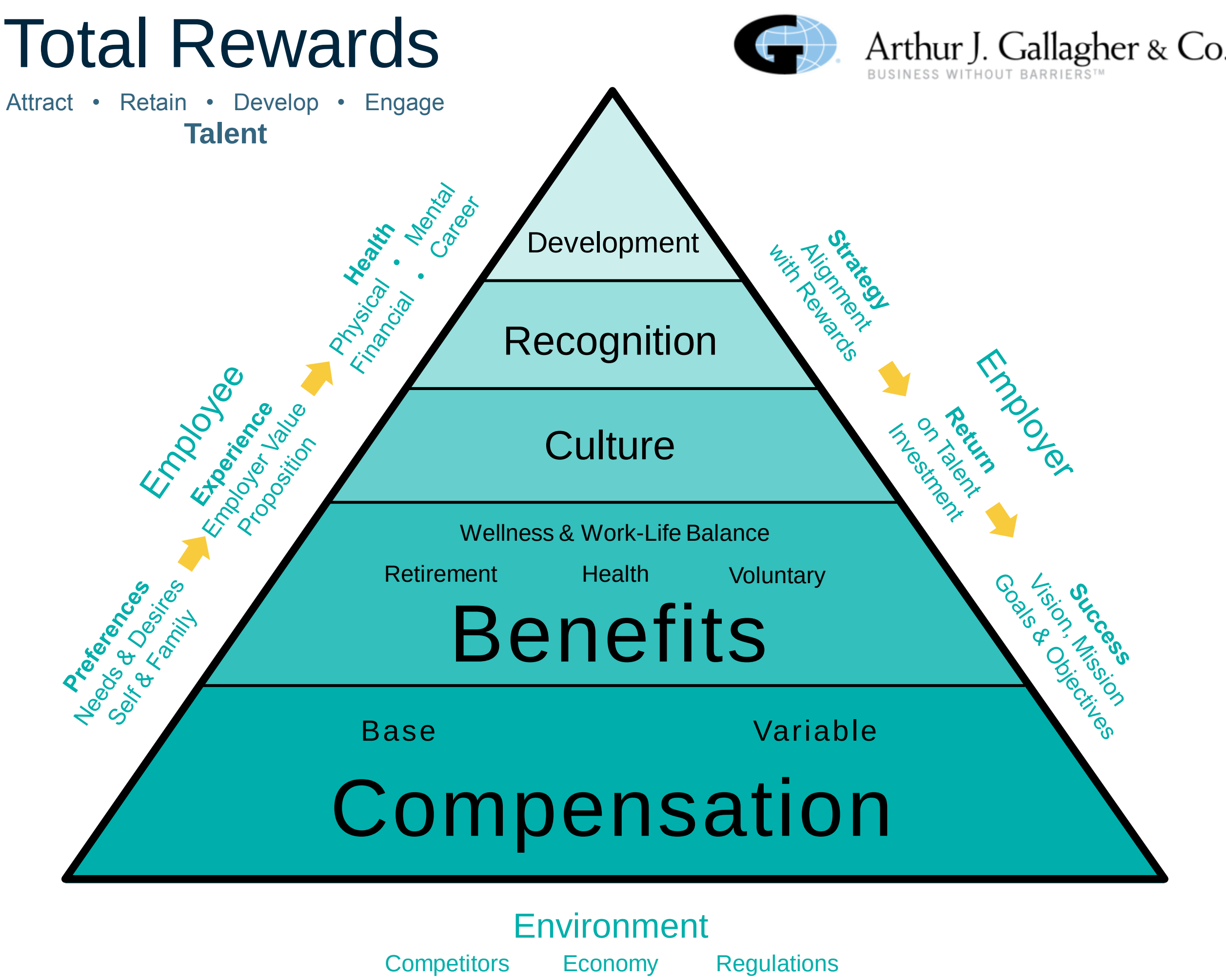




Total Rewards

Developing the Most Cost-Effective Employer Value Proposition

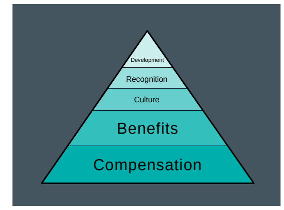
A strategically-oriented organization develops the most cost-effective employer value proposition it can . . . one that allows it to achieve its strategic organizational objectives effectively, without spending more than necessary. At its core, this is a ***total rewards*** issue.



Right mix

Right talent

Right price



Four Transformations

Traditional siloed rewards management process → Integrated ***total rewards*** process

Traditional benchmarking ("sameness") → Rewards & employer value proposition ***distinctiveness***

Myopic focus on singular rewards budget line items → Integrated, ***ROTI***-focused rewards ***portfolio*** that delivers strategy

Budget-driven rewards strategy → ***Strategy-driven*** rewards budget

Influence of Healthcare Reform

*Objective #1 — Assessing **All** Areas of Risk*

Legal Risk

- Plan eligibility, plan terms and plan documentation
- Sec. 6056 & 6055 reporting, and other government reporting requirements
- EEOC lawsuits & guidance, and wellness programs
- Prohibited reimbursement of individual premiums
- **Litigation exposure (individual cases)**

Financial Risk

- Medical trend and inflation
- Design-driven costs
- Taxes and fees
  - PCORI fee
  - Reinsurance fee
  - Health insurance tax
  - "Cadillac" tax

Operational Risk

- Talent management and execution of strategy
- Hours, scheduling and tracking
- Section 1411 notification management
- Collective bargaining agreement(s)

Strategic Risk

- Employer shared responsibility requirements

See also pages that follow!

Influence of Healthcare Reform

Objective #2 — Going Beyond a Singular Focus on Penalty Avoidance

A trend. Over the past several years, a fascinating trend has emerged for many employers subject to the Employer Shared Responsibility Requirement – an almost singular focus on avoiding ESR assessable payments, a.k.a. penalties. There are a number of possible reasons we can think of for this phenomenon:

- Misperception that assessable payments are punishment for violating the PPACA statute?
- Budget line-item myopia?
- Organizational silo bias?
- Organizational metathesiophobia?

No exposure for some. For any organization requiring employees to pay $90 or less per month to purchase individual coverage under the employer's lowest cost health plan, there is virtually no possibility that an assessable payment will be incurred in 2015 – as long as the employer qualifies as an "offering employer." This is not necessarily a good thing!! A strong case could be made that such an employer may be allocating more of its rewards dollars to health insurance than it should.

Cost-shifting to health benefits from other rewards? For many organizations with a legitimate exposure to ESR assessable payments, their preferred, or obvious, path to penalty avoidance is to provide more health benefit subsidies to all or a large proportion of lower wage employees. This amount could well be in excess of their likely dollar exposure to assessable payments. For some employers, especially those with collective bargaining agreements, this would entail providing greater subsidies to ***all*** employees! And the additional amount expended would likely have to be "made up" by paying less in other rewards categories -- wages and salaries, variable compensation, retirement benefits, recognition programs, professional & organization development initiatives, etc. – which could result in a misallocation of resources vis-à-vis employee preferences, making the employer value proposition weaker and return on talent investment lower.

Other cost-shifting? Other employers may attempt to shift employee contribution requirements from employees purchasing employee-only coverage (requiring such employees to pay less) to employees purchasing "single-plus-one" or family coverage (requiring such employees to pay more). This would result in a reduction of overall compensation/rewards for employees wanting to cover spouses and dependents, and an increase in overall compensation/rewards for employees wanting only to cover themselves. Again – this would likely be a misallocation of resources vis-à-vis employee preferences and a reduction in ROTI. It could also result in lower income employees who want to cover spouses and dependents losing eligibility for federal subsidies for the expanded choice provided by a public marketplace, and ultimate purchase of coverage there.

There are of course other approaches employers may make to avoid ESR assessable payments – many of which may result in misallocation of resources, compromised employer value proposition, lower ROTI, etc.

The question must be asked — what, really, is the concern with a group of employees purchasing coverage on the public marketplace and generating a few months' worth to 12 months' worth of assessable payments?

The objective is not to avoid ESR assessable payments.
The objective is not to reduce rewards expenditures or even to
reduce the rate of rewards expenditure growth.

The objective is to maximize overall return on talent investment, just like any other portfolio of investments!

Rewards Asset Allocation

Portfolio Evolution

"Simple" Illustration:
Cash Compensation vs. Health Subsidies

"Play": Higher ER Subsidy

Higher underlying health plan cost to employer

Fewer \$260/mo. federal assessable payments

Lower (taxable) cash compensation

Movement ***to*** the plan **increases** aggregate cost to employer & changes the risk profile

Tax & FICA effects

"Play": Lower ER Subsidy

Lower underlying health plan cost to employer

More \$260/mo. federal assessable payments

Higher (taxable) cash compensation

Movement ***from*** the plan **decreases** aggregate cost to employer and changes the risk profile

Tax & FICA effects

"Play": Limit Coverage (Actuarial Value)

Lower underlying health plan cost to employer

Fewer \$260/mo. federal assessable payments

Higher (taxable) cash compensation

Movement ***to/from*** the plan changes costs and risk profile

Tax & FICA effects

"Pay": Abandon ER-Sponsored Health Benefits

No health plan cost to employer

\$173.33/mo. federal **assessable payment** for each FTE (after first 30)

Much higher (taxable) cash compensation to replace lost benefit purchasing power

Tax & FICA effects

This simple analysis includes only two rewards categories – base (cash) compensation and health insurance benefits (subsidies), and assumes just one health plan option.

A truly comprehensive analysis would include ***all*** rewards components and more health plan options.

Note:
Assessable payment amounts shown above are based on the expected 2015 indexed payment amounts:

- **\$260** for each month a FTE of an "offering employer" is covered under a subsidized public marketplace plan (**\$3,120** for a FTE so covered for 12 months)
- **\$173.33** per month for each FTE, after the first 30 FTEs, employed by a "non-offering employer" presuming at least one FTE is covered under a subsidized public marketplace plan (**\$2,080** for a FTE employed for a full year)

Rewards Asset Allocation

Portfolio Evolution

Evolutionary Steps

Executive-driven One Size Fits All

Rewards portfolio determined based on what one or more executives feel is "right" (or what they want for themselves!)

Data-driven One Size Fits All

Rewards portfolio influenced by data:

- Talent requirements
- Demographics
- Preferences
- Engagement
- Other

Limited Choices and Options

Available choices and options influenced by data (see points at left)

Personalization: Significant Choices & Options

- Greater variable compensation
- Some compensation earmarked for personal choices
- Private exchange
- Defined contribution for health and other benefit choices
- Employer contributions "at risk" based on performance

Total Personalization

Administrative and regulatory restrictions make this unlikely or impossible.

(Where are you in this evolution?)

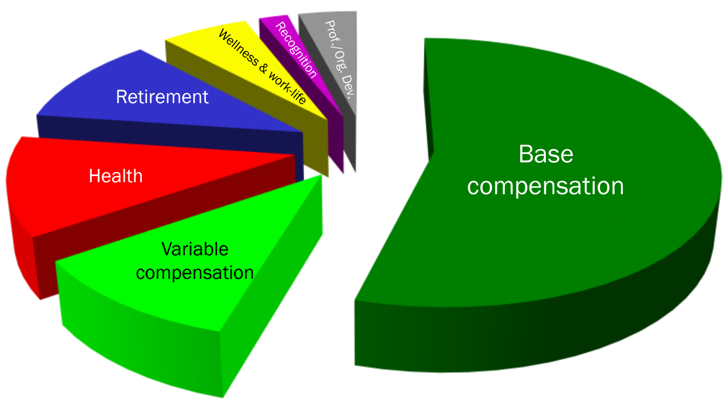
Rewards Asset Allocation

Portfolio Evolution

Next "Generation" Rewards Asset Allocation: "Optimal" One-Size-Fits-All

Once you've accurately assessed the demographic makeup of your employee population and the relative rewards preferences of various segments — both extremely important exercises — you may find that different groups have particular preferences that differ from other demographic groups.

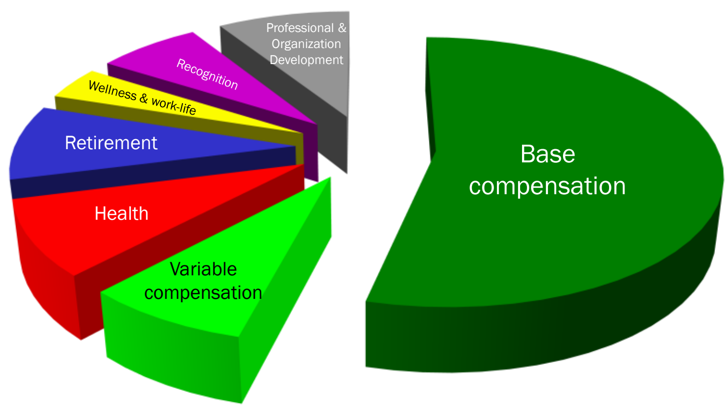
Boomers



Should you then offer a different rewards package for each demographic group — a "boomer package" (late career), a "GenX package" (mid career) and a "GenY" package (early career)?

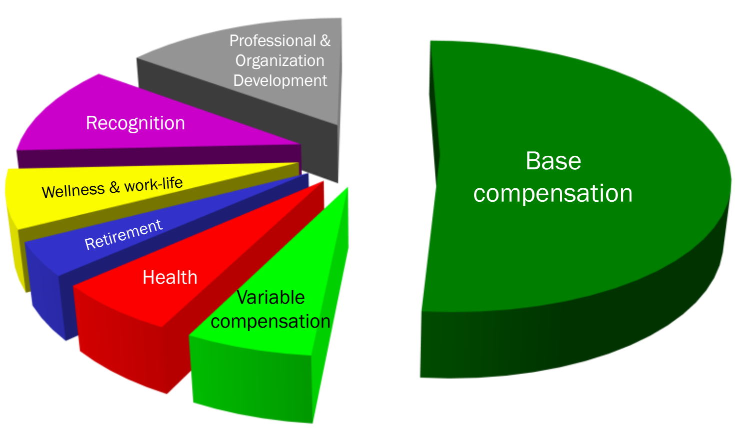
Probably not!

Gen X



But do you realistically expect to attract, retain and engage a high-performing, diverse workforce that values individual ***choice*** with a one-size-fits-all rewards package?

Gen Y



So can you find an "optimal" one-size-fits-all rewards allocation given an extremely diverse workforce?

This may be a reasonable early step in the portfolio evolution process.

Rewards Asset Allocation

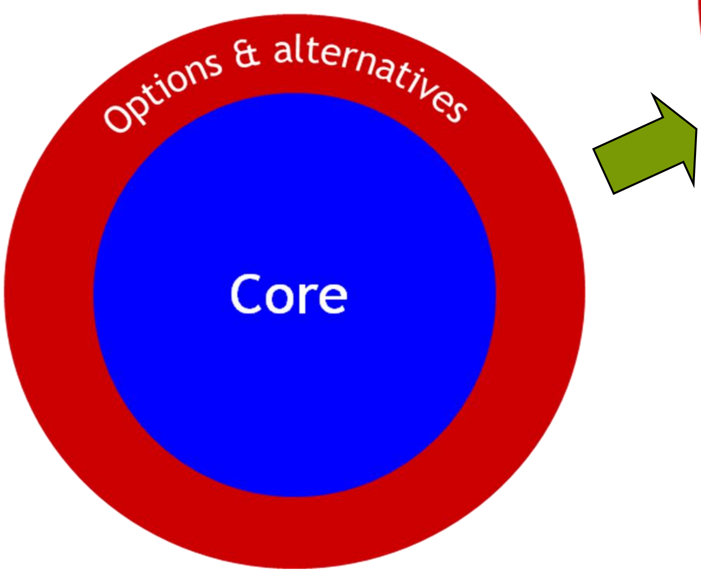
Portfolio Evolution

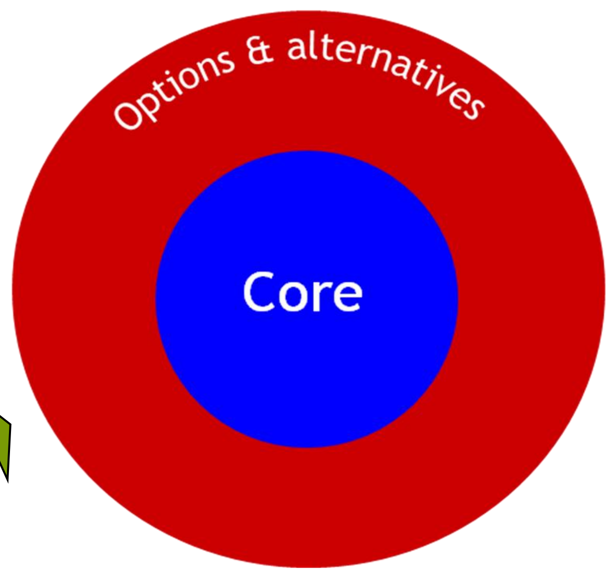
Maximum Personalization Drives Much of Allocation

The logical extension of rewards allocation is to allow each employee to choose as much of the allocation for himself/herself as is possible & reasonable. This approach would maximize the employer value proposition and ROTI. (As we discussed earlier, there are legal and administrative challenges to a ***pure*** personalization approach.)

Establishing a core, or baseline level, of compensation and benefits, and expanding the options and alternatives available to employees enables them a greater degree of personalization of rewards. More rewards "at risk" based on individual, team and organizational performance can incent strategically-focused behaviors and outcomes?

These objectives can — and should — be sought out by organizations that truly seek to create a distinctive employER value proposition in an era where choice "rules."

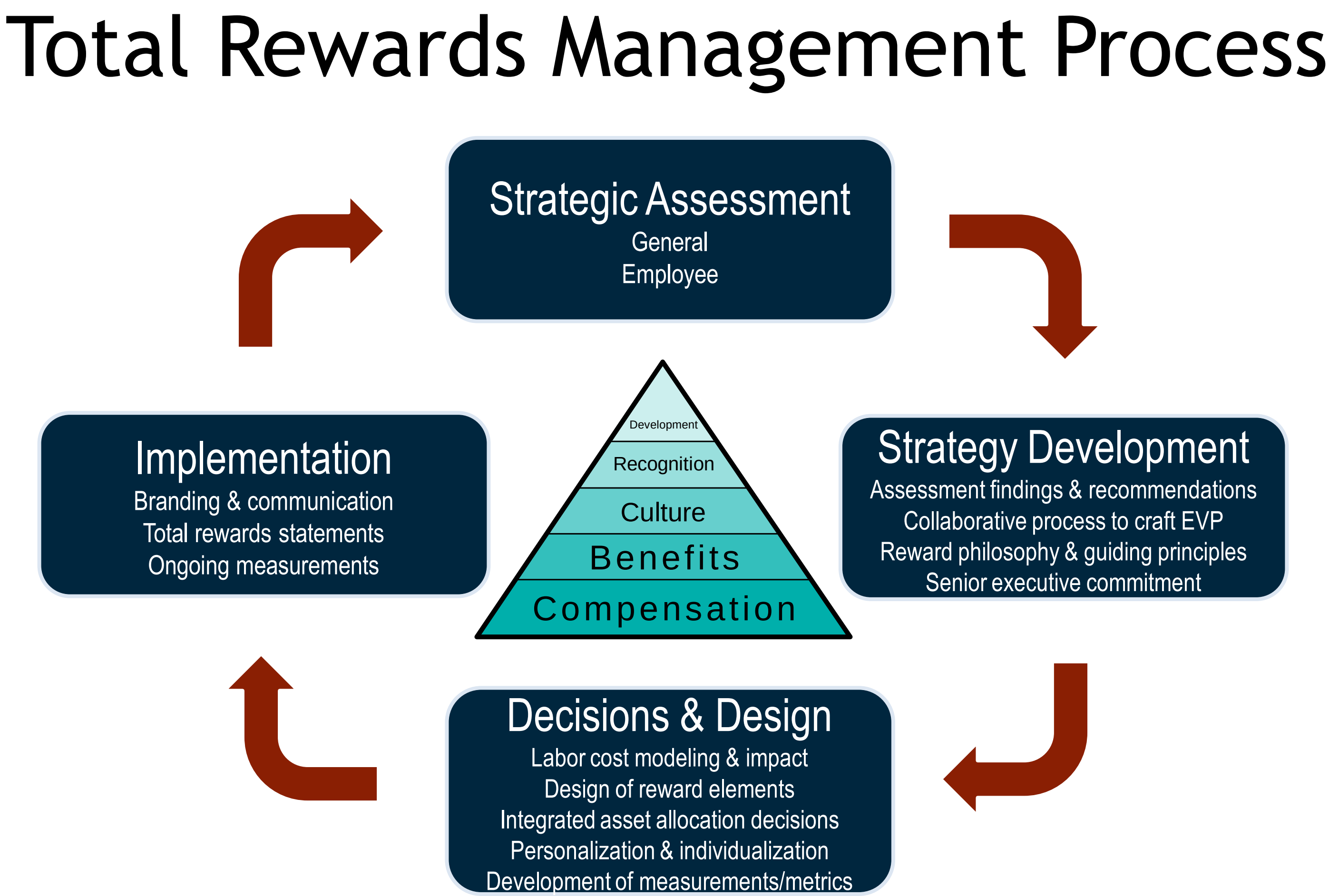




Important note: A private exchange can assist significantly in this part of your rewards evolution.

Total Rewards Management Process

A Comprehensive Process



Total Rewards Management Process

*Eight Actions You Can Start Taking **Now***

Strategic Capabilities

The first element of developing a strategically sound total rewards program & employer value proposition is to identify the organization's key strategic capabilities.

What is it from a talent perspective that makes your organization unique & distinctive (and competitive) now?

What talent segments are particularly challenging in terms of attraction, retention and engagement now? What do you anticipate that your talent requirements will be in the next 5 years? 10 years? Is there a talent segment that, if you "cornered" the market over the next few years on it, would make you invincible?

Intended EmployER Value Proposition

What do you ***want*** your employER value proposition to be? How do you want to be viewed internally and externally as an employer organization? Your employer value proposition is a brand. And just like any other branding process, this should be an intentional process, not an accident. If you don't actively manage and communicate your EVP brand, the outside world will make it up for you – and it may not be what you want.

The EVP brand needs to be authentic and realistic, while still reaching for your organization's aspirations. A clearly inauthentic EVP brand will strike dissonance, be seen as inaccurate, and have negative reputational consequences.

As a focal point for attraction, retention and engagement, your EVP should also move beyond "sameness" and a drift to the benchmarking midpoint, to achieve strategic distinctiveness.

Assessments

High-performing organizations commit to an ongoing dialogue with employees regarding interests, satisfaction and ***preferences***. Accurate data-gathering is key.

- What elements of your total rewards program are working? What elements are not working? What elements are working better than others (ROTI)?
- What elements of your total rewards program are most preferred/valued by your employees? What elements are not highly valued?
- This will require sophisticated data collection and analysis.
- External benchmarking should be only one of many types of data compiled – and benchmarking should be done in an *integrated* fashion (benchmarking one rewards element without the balancing effects of other elements is incomplete).

Organizational assessment is also important. Are you doing ongoing cultural assessments? Engagement assessments? How is the organization's employer value proposition viewed by existing employees? How does the outside world assess your organization's employer value proposition?

Asset Allocation/Integration

One of the most important aspects of strategic total rewards management is the integration of the various reward components through targeted asset allocation. Some considerations:

- Optimal "mix," considering talent and organizational objectives, and budgetary limitations.
- Internal equity and key talent differentiation.
- Greater focus on performance-based pay and intrinsic drivers.
- Alignment with organizational strategy and influence on desired organizational outcomes.
- Key objective: moving beyond "sameness" and a drift to the midpoint, to achieve strategic distinctiveness.

Total Rewards Management Process

Eight Actions You Can Start Taking ***Now***

Diversification & Personalization

Recognizing the increasing diversity of talent within organizations, a number of key elements should be incorporated into your employER value proposition:

- Involvement by and choices for employees whenever possible.
- Core reward elements (available to all).
- Flexibility (options – some available to all employees, others only available to certain employee groups).
- Differentiation of rewards elements and process to appeal across demographic groups, including age & generations, life stages, gender, income, tenure, etc.
- Private health plan exchanges
- Greater personalization of rewards packages.

Strategically Key Talent Differentiation

This is an emerging and increasingly critical element to total rewards and talent management. Executed effectively, it can result in dramatic long-term strategic impact for your organization. It includes:

- Identifying key strategic competencies
- Identifying key "strategic impact" positions
- Identifying "A" players in these positions
- Differentiating rewards by making a disproportionate investment in the "A" players in strategic impact positions

Internal Partnership: HR, Finance & Managers

In order to achieve a truly strategically-distinctive, differentiated, and cost-effective total rewards-driven employer value proposition, human resource and finance professionals must forge a true partnership.

The role of the line manager should include formal and informal assessment, assisting in rewards decision-making and management, and communicating rewards issues to employees. For many organizations, this may be a big change. It also may be the key difference between a rewards program and EVP perceived as really great versus just average.

Metrics

As you design and evaluate rewards components individually, and the total rewards program in its entirety, you will need to have objective measurements that drive your decisions and are good indicators of rewards success or failure. Rewards must be matched with business goals and strategic objectives. How do ***you*** measure return on talent investment? Here are some possibilities:

- High level indicators, such as revenue ÷ FTE or EBITDA ÷ FTE
- Trend indicators, such as labor (total rewards) cost growth as a function of EBITDA growth
- Labor cost indicators, such as dividing FTEs into total labor cost, salary costs, benefit costs and/or retirement costs
- Metrics focused on human resource goals:
  - Turnover impact indices (i.e., turnover and/or turnover costs as a function of other goals
  - Workforce planning metrics
  - Engagement