MMA
ENTERPRISE
1902 - 2002

Newsmagazine for Members of the Michigan Manufacturers Association

November/December 2002

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MMA Compensation, Benefits Survey Reports Reveal Challenges for 2003

By Edmund B. Ura

Blame the economy, blame increasing health care costs or blame anything you'd like — the fact is, the rate of pay increases dropped in 2002, and early indicators suggest the same lower level of increases are planned for 2003. Continuing pressure from health care has driven up employers' benefits costs sharply, resulting in reduced benefits to employees, and while the reduction in benefits has offset some of the increases, Michigan manufacturers are still paying a third more for employee health insurance than they did in 2000.

The 2002 edition of the *MMA Cash Compensation Survey Report*, the barometer for employee compensation among Michigan manufacturers, presents the findings of this year's pay study and gives state employers direction on planning for the upcoming year. Its biennial companion volume, the *2002 MMA Employee Benefits Survey Report*, provides extensive detail on the type and nature of benefits provided to employees. The findings show that the challenge for executives and human resource management will be to craft a compensation program that is competitive yet holds labor cost increases to a tolerable level. The survey reports, sponsored by MMA, are conducted by Management Resource Center, Inc., of Plymouth.

Trends show more conservative increases than in the previous year

Overall, the average increase at the "middle" of the labor market was 2.5 percent, compared to an increase of more than four percent from 2000 to 2001. The market rates for production-related jobs actually statistically decreased over the last year, with only clerical and administrative positions showing significant increases at the middle of the market.

Manufacturing held the line longer than any other part of the economy, particularly in Michigan; the 2001 edition of this survey showed that manufacturers had continued to increase their employees' pay at higher levels through 2001, even as other industries showed their lowest rates in years. In 2002, however, manufacturers took a step back and paid their employees much less than was planned. In 2001, Michigan manufacturers were planning on 2002 increases of 3.5 to 4.0 percent. Actual increases reported this year were 2.6 to 2.8 percent. Rates of pay increases in 2003 look to be similar to those in 2002, reflecting the expectation that financial resources from 2002 company performance will be limited.

More participation — and less reward — in variable compensation programs

The percentage of employees participating in some type of bonus or incentive plan has increased once again. In 2001, for the first time, more than half of surveyed employees participated in plans. Even more dramatic increases occurred in 2002, with 20 percent more employees in plans; the total now exceeds 60 percent of the employees in the survey as "bonus eligible." More than three-quarters of managers participate in incentive programs, and all but a scattered few of the hundred-plus jobs in the survey have eligibility over 50 percent.

While participation increased, incentive rewards dropped sharply, reflecting the financial performance of many of Michigan's manufacturers. Decreases range from one-third to one-half of the payouts from the 2000 to 2001 bonus years (incentive data represents the last completed fiscal year). Beyond financial performance, some of the decrease in payouts can be attributed to new plans, which typically offer more conservative rewards.

As health insurance costs grew, employers cut benefits and charged employees more

There was more change in benefit plans over the past two years than in any other two-year period since the early 1990s. More than two-thirds of survey participants changed their benefits programs in response to rising health care costs. More than half increased their health insurance co-pays and deductibles. Coupled with a dramatic change in the "mix" of program types, it's clear that the typical employer is paying more for a program that costs their employees more and provides a lower level of benefits.

Premiums increased for Preferred Provider Organization (PPO) insurance by more than 35 percent over the two-year period, consistent for all levels of coverage (individual, couple and family). Median monthly premiums for these three levels of coverage are $226, $510 and $579, respectively. Exacerbating the problem is that these dramatic premium increases do not even represent comparable coverage. For example, median deductibles for "non-office visit" care increased by 20 percent from $200 individual/$400 family to $250 individual/$500 family, and there were comparable changes to many other features of the plans. It's clear that more and more employers are picking higher deductible and co-payment plans, and even these changes are not keeping cost increases down to a tolerable level.

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Health Maintenance Organization (HMO) costs increased at a lower rate of about 22 percent from 2000, with employers paying $227, $518 and $581 per month for individual, couple and full family coverage respectively. Benefit levels remain comparable, with typical plans maintaining their $10 office visits. Hospital visit co-payments increased somewhat to an average of about $38.

Employers have passed along some of the costs of health insurance increases to their employees, although less than might be expected. The percent of employers requiring employees to contribute to the cost of HMO coverage increased from 58 to 61 percent, and the actual percentage of the premiums paid by these employees dropped somewhat, to about 10 percent of the cost of individual coverage. More employees are paying more for their PPO coverage, however; the percent of employers requiring that employees pay part of the premium for individual coverage increased from just over half to more than two-thirds.

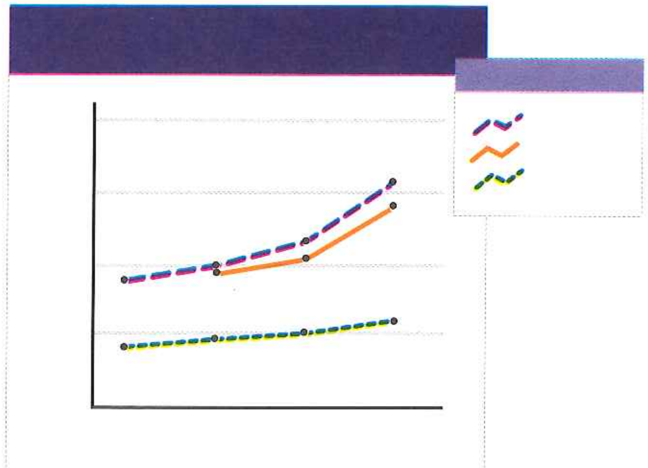
Brand name drugs are now a much more expensive choice for employees

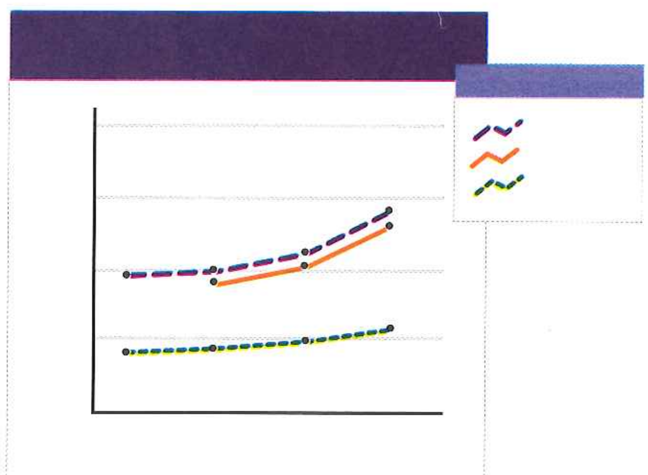
Even more dramatic than the changes in health coverage was the response by employers to skyrocketing prescription drug costs. Nearly 70 percent of survey participants reduced their prescription drug benefits because of cost increases. Most of the changes involved significant increases to the employees' cost for brand name drugs. In the 2000 survey, there was actually very little difference between the co-payment for generics and brand name drugs; median co-pays were actually the same for most employers at $10 per prescription. While the employees' cost for generic drugs remained the same, the median co-pay for brand name drugs has doubled to $20 in 2002.

Be careful about lumping pay and benefits together into a single line item

Crafting a response to recent developments is a challenge. There is a strong temptation to lump the costs of employee compensation, government required payments and voluntary benefits programs into a "total compensation cost" that can be managed as a single line item in the budget. However attractive that may be, it is not realistic. Employee compensation and benefits can not be handled in such a simple manner, as they involve both actual cost and perceived value.

Many employers try to make government-ordered payments, such as workers' compensation and social security contributions, look like "benefits." While these legally-required programs may





eventually have a "benefit" to employees, simply following the law is generally not perceived by employees as something employers give "out of the goodness of their hearts." Since they are required of virtually all employers anyway, they cannot be used to suggest either that a company has a competitive advantage, or that increases in these costs can offset other types of employee compensation.

Benefits costs must also be analyzed separately from base compensation and should be compared, not based on cost, but on benefit levels. Because benefit and pay competitiveness is measured differently, they are not "additive." That is, simply adding together the cost of all the employer's programs does not provide a company a good way of showing how it takes care of its employees and rewards them for their performance.

Base compensation is the most psychologically important part of the total compensation program, because it is what people rely on in order to maintain their standard of living. Base pay and incentives should be compared to competitive base pay levels; benefit levels should be compared to competitive benefits levels. Employees will generally not respond favorably to learning that they will be getting a lower than expected pay increase because the employer's health insurance premiums increased sharply. It is simply not possible to consistently argue that an increase in insurance premiums provides an increased return to the employee.

Frankly, most people don't appreciate health insurance until they need it, just as young people don't appreciate the value of a high benefit pension plan. It's not that employees can't appreciate the employer's increased cost, it's simply not something they can control, and the "cost" of the benefit is not the "value" the employee sees. The value of any benefit program, as perceived by the employee, depends on their need for whatever the benefit provides and that varies with every individual.

While the "cost" of benefits is a poor measure for selling employees on the attractiveness of the workplace, the "level" of benefits does provide a possible competitive advantage. To have the kind of impact that will cause an employee to take a lower level of pay to work for you, your benefits do not simply need to be better, they must be *much* better, and they must be much better as perceived by that employee. ▶

What should an employer do?

Employers must remain competitive from both a base pay and benefits perspective if they are to attract, motivate and retain the employees they need to remain financially viable and competitive in their markets. The results of the two new MMA studies can help employers understand where they are and where they need to go. I suggest the following process:

Base Compensation

Compare your organization's current pay with the data in the *MMA Cash Compensation Survey Report*. Be careful to select the data that is most relevant to you for each job. The appropriate data will be a function of the geographic area in which you recruit, the nature of your industry and the types of companies you compete with. There may be several pieces of data for each job that are relevant, and each one should be considered.

It is also important to set a "target" position in the market. Most employers look at the mean, or median, because it represents the "middle" of the market. While this is the typical practice, it is important to understand that if you are at the middle, half of the employers are paying more, and these other employers are a threat to hire your best employees. Also, just as a "C" grade is considered only "satisfactory," being in the middle is not exactly an exciting message to send to employees.

Benefits

Use the results of the *MMA Employee Benefits Survey Report* to analyze each type of benefit. Before comparing your actual benefit levels, consider the nature of your workforce. It is *not* essential to have the highest level of every benefit program to be competitive. What is most important is that you have the best possible levels of the benefits that are most important to your employees. There are many general "rules of thumb" that most employers learn on their own, most often from frustration when their cherished benefit programs are not appreciated. If you do not know what your employees value, ask them. But if you ask them, plan on delivering what they want, because surveys or interviews raise expectations that you intend to follow through on the findings.

Look at each benefit type separately. Pay close attention to how common the program is. For example, if you have a low level of a benefit that is typically not provided to employees, you have a competitive advantage even if your benefits levels are below the average. On the other hand, for a benefit that is both common and crucial to your workforce, you may want to consider a higher benefit level if the cost is affordable.

As any experienced human resource manager can describe from experience, there is no simple solution. The most important resource an organization can have is information, because decisions made on solid ground make more sense and are more defensible. The information in the MMA HR InfoSeries survey reports, including the *Cash Compensation* and *Employee Benefits Reports*, provide the type of data that Michigan manufacturers need to make their crucial human resource decisions and stay competitive.

Edmund B. Ura is president of Management Resource Center, Inc. (MRC), in Plymouth. MRC is an independent consulting firm offering business and compensation strategy and planning, and research and management consulting. He may be reached at 734-454-2500 or e-mail him, ebura@mrc-consulting.com.