Government Study Shows Benefits Costs Outpacing Wages

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Employers' spending on benefits has increased faster than employees' wages, due largely to rising costs for health insurance and retirement benefits, according to a U.S. Government Accountability Office (GAO) study released in February. These escalating health-benefits costs are threatening the sustainability of employer-sponsored benefits systems.

Sigurd R. Nilsen, director of Education, Workforce and Income Security Issues, outlined the GAO's findings in a report to Sen. Patty Murray (D-Wash.), ranking minority member of the Subcommittee on Employment and Workplace Safety Committee on Health, Education, Labor and Pensions, U.S. Senate, and Sen. Edward M. Kennedy (D-Mass.), ranking minority member of the Committee on Health, Education, Labor and Pensions, U.S. Senate.

In the report, the GAO scrutinized federal data about private employers' costs for workers and sought perspectives from 17 experts to identify recent trends in employers' total compensation costs; composition of the trends; whether employees' costs, participation or access to benefits changed; and possible implications of the changes for private systems.

"Specifically, we examined data from two federal surveys: the Bureau of Labor Statistics' (BLS) National Compensation Survey (NCS) and the Agency for Healthcare Research and Quality's Medical Expenditure Panel Survey (MEPS)," Nilsen said. "We used NCS data to determine trends in private-employer costs for wages and salaries; total benefits including those that employers are legally required to contribute to, such as Social Security; and specific employer-provided benefits-retirement income, health insurance and paid leave for 1991 through 2005."

> The change to a global business environment is causing some employers to blame compensation costs for their lack of ability to compete against foreign businesses, which traditionally have a lower cost.

The State of Benefits Costs

The GAO found private employers' average cost of wages and benefits grew by 12 percent from 1991 to 2005. Benefits costs grew by about 18 percent, while wages increased by 10 percent. Wages and benefits increased by about the same percentage until 2002, when wages began to stagnate and benefits costs grew. (See Figure 1 on page 86.)

Nilsen states in the report that availability and cost of employer-sponsored compensation such as wages, health insurance, retirement income and paid leave have a significant bearing on U.S. workers and U.S. business. He mentions the change to a global business environment is causing some employers to blame compensation costs for their lack of ability to compete against foreign businesses, which traditionally have a lower cost. As a result, he expects employers to change compensation packages accordingly and/or ask employees to take on more responsibility for keeping costs down.

According to the study, benefits costs outpaced wage growth in every private-employer category from 1991 to 2005. Employers' health-care costs grew by 28 percent from 1991 to 2005. During the same period, benefits increased 18 percent and wages 10 percent.

From 1991 to 2005, the total benefits package's cost increase was due to mounting costs of providing health insurance and retirement income. Paid leave was formerly employers' most expensive

benefit, however, by 2005 health-insurance costs equaled paid leave. Of the three benefits — health insurance, retirement income and paid leave — retirement income was the least expensive, despite growing 47 percent during the period, mostly between 2004 and 2005.

"In combination with paid leave, these three benefits represented on average almost 60 percent of an employee's total benefit package and over 80 percent of employers' costs for voluntary benefits," Nilsen wrote.

"During the time under review, employees' access to most benefits remained stable, but participation rates declined for health benefits as the real dollar amount of the premiums increased. Between 1991 and 2003, roughly half of all workers participated in employer-provided retirement plans. Holidays and vacations were generally available to most workers, but a smaller percentage of workers had access to personal and sick leave," Nilsen wrote.

He said a panel of experts from a variety of backgrounds including human resources, industries, unions and academia agreed that rising benefits costs are forcing private employers and their employees to make trade-offs between wages and benefits.

"They noted that the employer-sponsored system of benefits in its current form may be unsustainable, largely because productivity growth is unlikely to support the rising costs of some benefits, especially escalating health insurance costs," Nilsen said.

The panelists told Nilsen and his team employees saw increases in their deductibles and co-payments during the time under review. From 1991 to 2003, half of all workers participated in employer-provided retirement plans. However, he said, "the types of plans shifted more toward defined contribution plans, under which employees assume the investment risk."

Paid leave, holidays and vacations were available to most workers from 1991 to 2003, but fewer employees were able to take personal or sick leave.

Outlook on Future Employer Health Spending

The situation is not likely to improve. Nilsen cited a report in *Health Affairs* that estimates that in 10 years health spending will slow, but it will outpace Gross Domestic Product (GDP) growth. Wage and benefits costs followed the same trend for much of the study period. However, wage growth began leveling off in 2002 while benefits costs grew. Health-care and retirement benefits were the leaders.

"By 2015, the report estimates, health spending will represent 20 percent of U.S. GDP, up from 16 percent today," Nilsen wrote.

Union representatives said maintaining health care and pensions is workers' main priority. One panelist, Nilsen reported, said workers frequently choose health care over increases in salary.

The panelists recognized the shift in employer-sponsored retirement income from defined benefit to defined contribution plans.

"One expert predicted the eventual termination of defined benefit plans, a freeze or decrease in hybrid plans (those that combine features of defined benefit and defined contribution plans) and a shift toward 401(k) savings plans (which are a type of defined contribution plan)," Nilsen said.

Panelists also observed that employers are experimenting with consumer-directed health-care plans, which may shift more responsibility and risk to the employee. Nilsen explained employers are considering changing the way they offer compensation.

"Experts agreed that there has been a movement from fixed to incentive compensation, wherein employers tie cash compensation to productivity," he wrote. "It was noted that some employers are turning to stock options in lieu of wage increases. Given the risks implied for the individual in such private-sector plans, for both retirement and health care, a panelist emphasized that employees will need adequate education to make informed decisions."

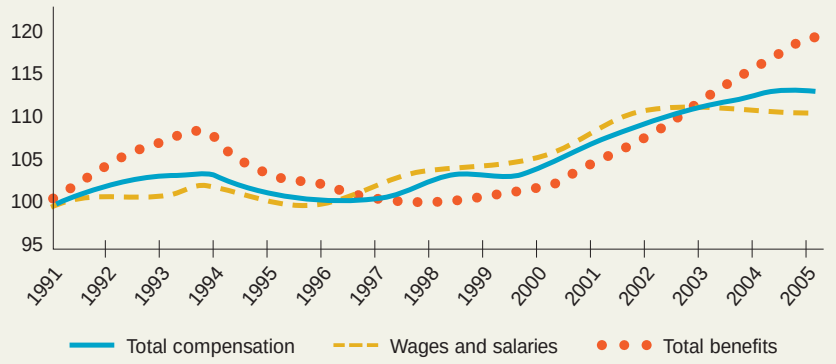
Panelists also observed the rise in compensation costs and their implications for business and for employees. One benefits expert said jobs would go elsewhere if an employer pays compensation costs that the productivity of its workers cannot support. For example, a union representative noted the garment industry has faced international competitors with lower compensation costs. That has led to decreased pay for U.S. workers and a loss of domestic jobs.

Nilsen explained that panelists noted employers may attempt to remain competitive by cutting wages and benefits for workers, sending jobs overseas and increasing the use of contingent workers, who may not be provided benefits.

Experts disagreed about how the responsibility for addressing the rise in benefits costs should rest with the public sector. A union spokesperson said such benefits amount to a social good, something that supports the well-being and overall productivity of society.

"A union representative noted that employees who have dropped out of health insurance plans, especially

FIGURE 1: GROWTH IN EMPLOYER COST



Source: GAO presentation of Bureau of Labor Statistics (BLS) data from the National Compensation Survey (NCS).

employees in lower-wage industries, have subsequently relied on public programs in which taxpayers ultimately bear the cost," Nilsen noted.

"Other panelists," he added, "expressed belief in the marketplace as an arbiter of resources and said that government or public benefit models are not a solution to employers' rising costs for compensation. These panelists suggested competition would eventually resolve the distribution of benefits by winnowing out companies that could not attract the kind of employees needed with the type of compensation they provide."

Therefore, one panelist said, the government should have limited involvement in the provision of employer-sponsored benefits. An HR representative suggested that businesses should be allowed to experiment with different means of providing benefits. It also was suggested that solutions to benefits costs would require public and private initiative and collaboration. WS

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