Understanding the Real Risks of Changing Employee Benefit Plans

by Jon Kane and Jeffrey St. Amour

In an environment of constant change, corporations are looking to alter employee benefits programs to make them more responsive to employee and business needs. A complete risk assessment process is the key to preparing for changes to employee benefits programs by providing employers with an analysis of cost savings against the potential negative ramifications of change. This article outlines the steps involved in a complete review of risk assessment. It then discusses how employers can develop successful change management communication strategies if, after conducting a risk assessment, employers decide to move forward with alterations to their employee benefits programs.

Recently, the chief financial officer (CFO) of a large corporation was frustrated at the number of unanswered questions about his company's proposed changes to employee benefits. The CFO had heard about some of the disasters that other firms had experienced when they made similar changes. But his benefit consultants assured him that many other firms had experienced much smoother transitions. The CFO was not convinced. "I wanted specific information about the risks involved for our firm," he said, "the risks associated with employee morale, productivity and litigation, and no one was providing me with anything more than their best guess."

In an environment of constant change, corporations are looking to alter employee benefits programs to make them more responsive to employee and business needs. Employees take these changes very seriously. In our experience, employees consider changes in employee benefits as changing the culture of the firm and their lives. They look at employee benefits as part of the "deal" they made when they joined the company. The question in today's business environment is how much is too much change? What will employees accept or reject? How will unhappy employees respond? Today, companies have invested millions of dollars in developing risk management processes, and most believe that not fully understanding business risk is unacceptable. But no one has a crystal ball and risk is often time-specific to each individual company.

A COMPLETE REVIEW OF RISK

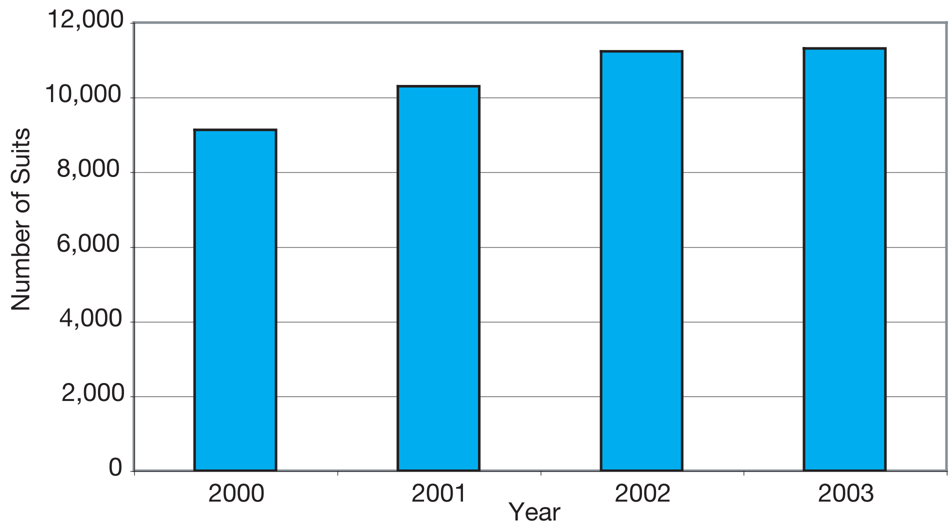
A complete review of risk assessment helps identify and quantify the risks of changing employee benefit plans. It clearly gauges the anticipated level of employee acceptance for change and provides a strong understanding of the risk associated with change. The process of a complete risk assessment review provides employers with specific insights on the climate of their employee population and ways to reach their employees with complex benefit information.

In addition, a complete risk assessment review helps employers understand the legal consequences of

FIGURE 1

UNDERSTANDING THE COST OF RISK

INCREASED LEVEL OF EMPLOYEE LITIGATION OVER CHANGES TO BENEFIT PLANS OVER THE LAST FIVE YEARS



Source: Suits filed under ERISA; data from Administrative Office of U.S. Courts.

poorly managed change. Understanding what triggers employee unrest and litigation, and what can be done to avoid such situations, puts real rigor to the risk assessment process (see Figures 1 and 2).

A complete risk assessment process is the key to preparing for change. The assessment provides the company with an analysis of cost savings against the potential negative ramifications of change. One CEO put it best: "Before the assessment, I knew what we could save; once the assessment was completed, I knew what change could potentially cost."

The following is an overview of the steps necessary to conduct a complete review of risk assessment.

Step 1. Conduct a "point in time" review of the existing employee relations environment. This includes reviewing all changes implemented in the last two years including any increased employee costs for benefits, the performance of employee 401(k) and profit-sharing plans and other changes in compensation or in human resource policies. A color-coded system is helpful in rating the level of existing employee satisfaction for each area.

Step 2. Review the proposed changes in detail; document the employer's employee relations litigation history and compare it to other companies that have gone through similar changes. The color-coding system can be used to rate the level of relative risk associated with the change based on the experiences of a group of peer companies.

Step 3. As a way to validate the first two steps, conduct employee and manager focus groups to gauge the employees' appetite for change. The system can then code the reaction of the focus groups.

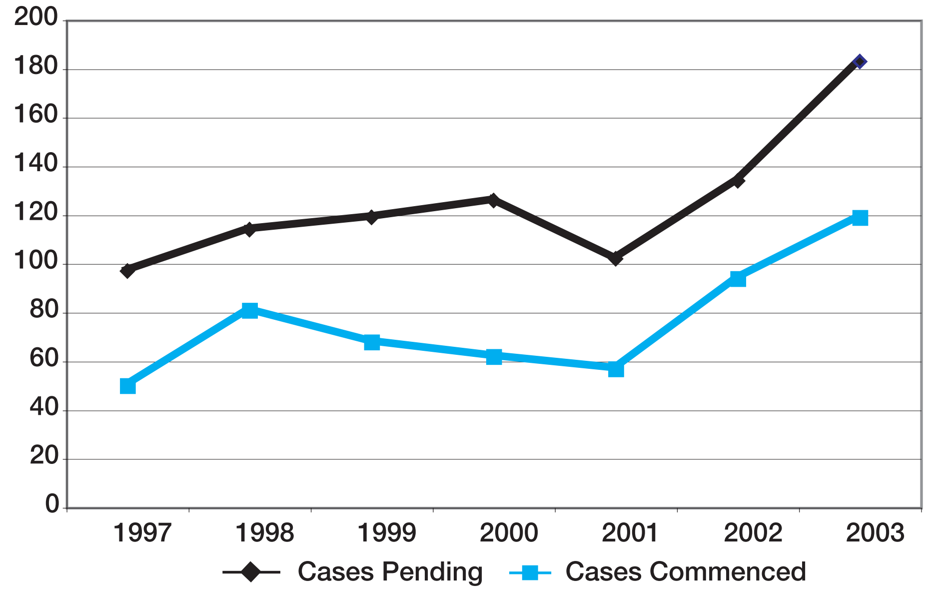
Step 4. Develop a financial model to validate the benefits to both the company and the employees. An essential part of this step is challenging the monetary assumption. It is sometimes easy to inflate the company's potential cost savings in the short term, without being fully aware of the potential long-term cost in employee talent. The proposed gain vs. the potential loss can be coded as an advantage or disadvantage.

Step 5. Based on the coding system for the first four steps, develop an overall rating for the proposed change. A green coding would mean that the risk assessment recommends moving forward with the change. A yellow coding would mean that the company needs to move cautiously, and a red coding would mean that the risk associated with the change may be too great compared with the benefits to the company.

In many cases, firms will find themselves with a yellow cautionary ranking. At this stage, employers must develop a strong change management communication strategy to make the change work. The process of conducting a complete review of risk assessment gives em-

▶ **FIGURE 2**

ERISA CLASS ACTIONS



ployers the information they need to build a strong strategy.

A vice president of a large hospital system found the complete review of risk assessment approach outlined above to be a better way to get a clear picture of the risks involved in change. He said, "We received a more comprehensive look at the employee relations risks associated with our proposed changes; for us, the risk assessment we used was clearly superior to what we have seen in the past." His hospital system was a very good candidate for a complete review of risk assessment. The organization was going through an enterprisewide organizational improvement initiative. Consultants were working with every department to identify areas of improvement and cost efficiency.

Human Resources was no exception, and they were working with no less than four different consultants who were looking at all of the employee benefit programs. Before the complete review of risk assessment was performed, they had four major change proposals they were considering: changes in medical plans for employees, wholesale changes to the employees' paid-time-off program, changes to human resource policies and major changes to their defined benefit pension plan.

When the complete review of risk assessment began, it was clear that the potential cost savings were paramount to the organization. The focus was very short term, and there was no enterprisewide impact study or employee relations review under consideration. For Human Resources, the overall savings from all of the proposed changes was projected at $7 million. The complete review of risk assessment was conducted and uncovered a number of key issues that caught the senior management team by surprise:

- The employees of the hospital system were some of the best in the industry. As the hospital system was presently in a profitable mode, supervisors and employees were anticipating that the corporatewide organizational improvement initiative would bring about new quality and efficiency programs that would allow them to offer patients even higher quality care.
- Employees were not, by any means, under the impression that the result of the study would be cuts in their benefits.
- Many of the proposed changes had caused major disruption at other similar hospital systems. Turnover, employee unrest and litigation had increased based on the introduction of similar changes.
- The proposed cost savings based on the changes in employee programs was inflated. A total savings of about $5.5 million was more realistic.

When the assessment was completed, the hospital system received a "red" rating. The complete review of risk assessment indicated that employees would not accept the magnitude of the proposed changes to their benefits, when they believed that the focus of the enterprisewide study was to be on quality improvement. Results of the complete review of risk assessment strongly suggested that, if the employer implemented the changes as proposed, it would most likely be unable to avoid a subsequent loss of key talent, employee unrest and litigation. In addition, because the vast majority of its employees worked in the local area, the employer's great reputation in the community would be damaged.

Finally, the complete review of risk assessment showed that the potential loss that the hospital system could incur if it went through with its proposed changes could be as high as $7 million over the next four years.

Once members of the senior management team read the assessment report, they sought to identify what level of change could be implemented and accepted by the employees. Having undertaken the complete review of risk assessment, management had the information necessary for its human resource and employee relations departments to modify the changes, develop a change management communication strategy and implement the changes. The implementation went very well and there was very little employee disruption.

THE CHANGE COMMUNICATION PROCESS

Once a firm has decided to move forward with its benefit change, it can develop change management communication strategies based on what it has learned by undertaking a complete review of risk assessment. Each solution is different, but some of the basics that are found in each strategy include:

- **An understanding that the firm is dealing with cultural change.** This puts a large premium on how well and sensitively information is communicated throughout the company.
- **A strong business case that describes the "why of change" must be developed and communicated enterprisewide.** If managers and employees do not believe that change was necessary in the first place and instead believe that status quo is best for the company and employees, they will not accept the details of the proposed change.
- **Although the subject is benefits, cultural change demands an explanation from the top of the company.** Communicating cultural change means that the CEO is the spokesperson. The entire senior team, as well as managers and supervisors, must be educated, trained and convinced that the change is right and fair for everyone involved. If they are not convinced, they will not support the change.
- **Use a multimedia approach.** Do not select media that is convenient for management to produce; select media that works with each different employee group. Much of this information can be gathered in the focus groups conducted as part of the risk assessment.
- **Define and test messages.** Do not finalize messages based on how they sound to management. Messages must be tested to see if employees understand and accept the key points.
- **Monitor, monitor, monitor.** Set up monitoring systems so that management knows if communicated messages are being accepted or rejected. Employers need formal channels for information to get back to them and employers need flexible processes to change the focus of their message and message delivery.
- **Expect messages and media to change throughout the process.** Resistance levels change, so an employer's response to the resistance must change as well.

Today, companies need risk assessment information to make decisions. Disrupting an entire employee population, without any real financial gain, can put a company years behind its competition. And, it may take years of work to regain the respect and trust of its employees.

In business, change is constant, and is necessary. Knowing the risks and rewards associated with change allows smart companies to make change part of their winning formula. ◀

▶ THE AUTHORS

Jon Kane is a partner and the chair of the Labor Relations and Employment Law Group at Pepper Hamilton LLP, a multipractice law firm with 400 lawyers in six states and the District of Columbia. Mr. Kane has represented management in all aspects of strategic counseling, labor relations and employment law.

Jeffrey St. Amour is a partner and the national practice leader for Strategic Communication and Change Management for PricewaterhouseCoopers' Global HR Services Practice. Mr. St. Amour has over 20 years of both corporate and consulting experience in change management, research, advertising and organizational communications.