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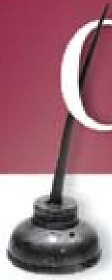

NOVEMBER 2006

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COUGHLIN & ASSOCIATES LTD.

SPECIAL EDITION: RETIREMENT BENEFITS

Retiree benefits: can your organization *really* afford them?

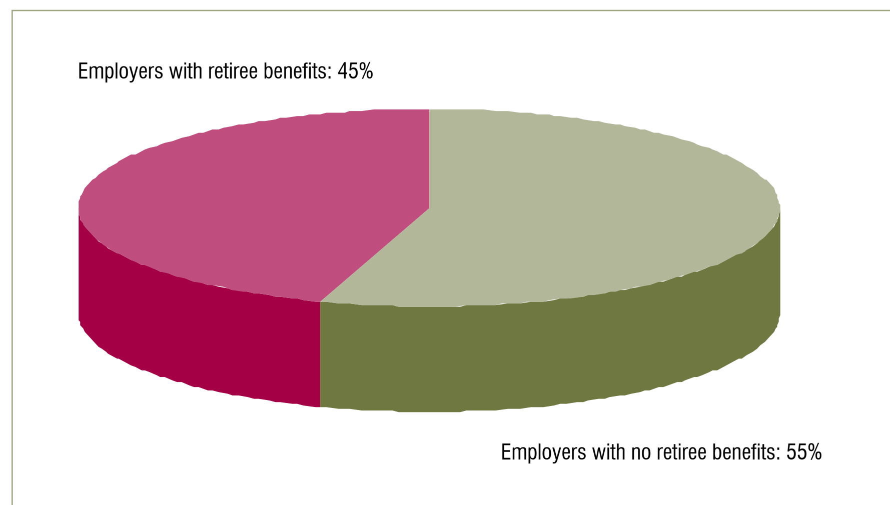
Benefits for retired employees: an expensive holdover from the past or a brave new way to attract and retain skilled workers?

Providing benefits for retired employees may sound like a simple idea but the reality can be something else again.

The commitment to provide health, medical, dental or other benefits to such a group could have serious cost implications. After all, you may be funding a commitment that may last a lifetime. Yet, with a looming labour shortage forcing many employers to try to attract or retain older, more experienced workers, the appeal of retiree benefits as a recruiting tool can't be denied.

If the pros and cons of offering these benefits leave you slightly confused, you'd be in good company.

A survey of 218 Canadian employers published by the International Foundation of Employee Benefits Plans (IF), says that the majority of employers -- 55 per cent -- do not provide benefits for retirees. The main reason according to 82 per cent of participants: rising health care costs.



The pressure of meeting a cost noted for its double-digit inflation and providing it to a higher risk group with the highest levels of major medical and drug use has prompted many of the employers that offer retirement benefits to take a serious second look at them. According to the IF, 37 per cent of surveyed employers indicated they had reduced their benefits to retirees over the past three years.

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Another 57 per cent said they planned to do so over the coming three years.

Yet, their retention value argument remains compelling. A significant portion, over one-quarter, of the same group also indicated that had made improvements in their benefits to retirees.

It should be noted that, according to the IF report, many of the reported improvements in these benefits were “modest” and likely designed to more closely align benefits of retirees with those of active employees.

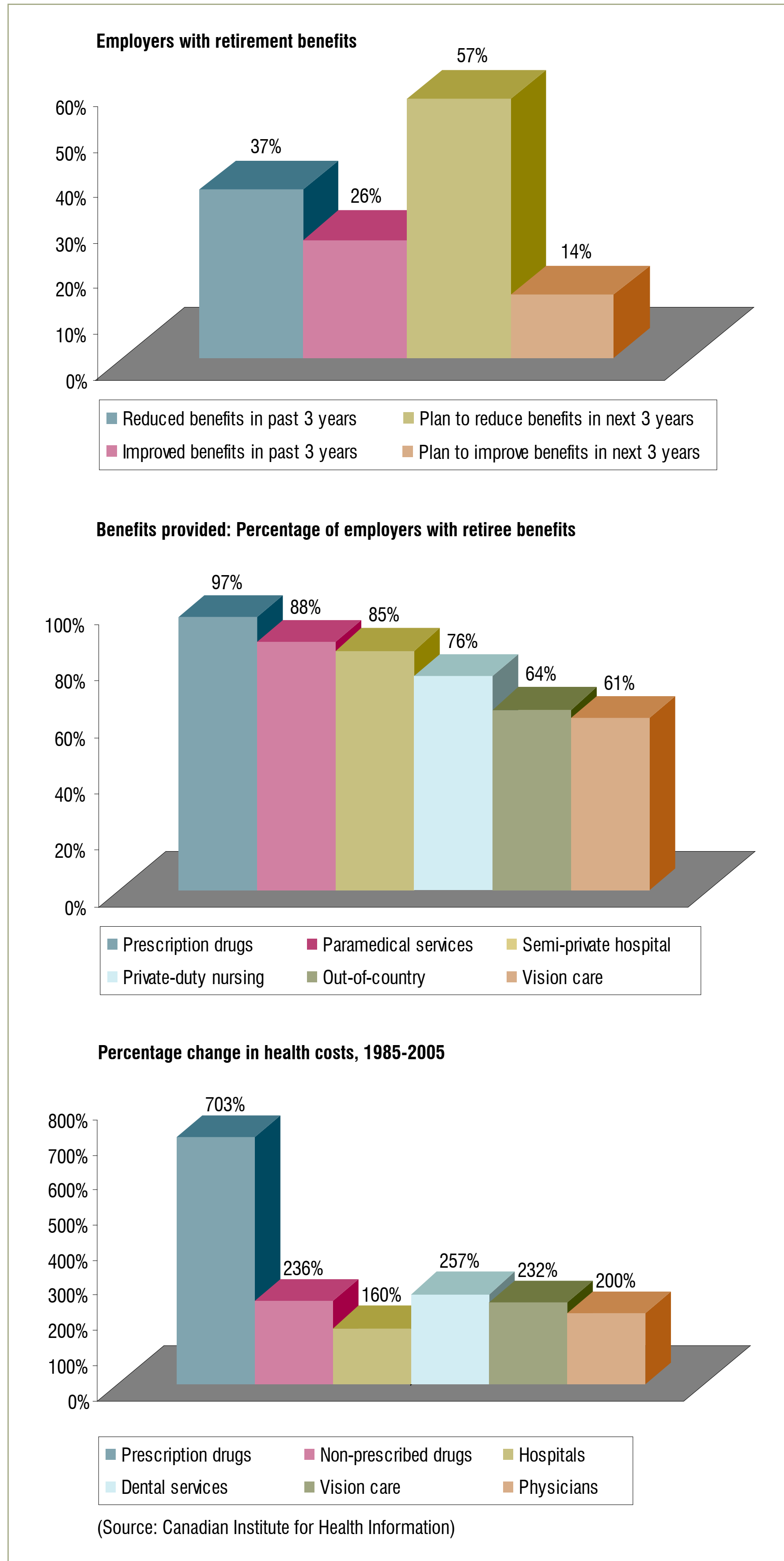
The benefit most offered by those groups with retiree plans was prescription drug coverage, the benefit that experienced the fastest and largest increases over the past few years. Virtually all those offering retiree benefits provided drug coverage. Paramedical services, semi-private hospital and private duty nursing followed, the IF reported.

A substantial commitment

With increased life expectancies, traditional retiree benefits have to provide coverage for longer and longer periods. According to the American Society of Actuaries, a 65-year-old male now has a 50 per cent chance of attaining age 85 and a 25 per cent chance of reaching age 92. A 65-year-old woman has a 50 per cent chance of living to age 88 and a 25 per cent chance of seeing her 94th birthday. It is safe to assume that a covered employee who retires between the ages of 60 and 65 will use his/her benefits for at least 20 years.

When the cost increases experienced by various health services over the 20-year period from 1985 to 2005 are considered, the long-term implications of a commitment to these benefits can be frightening. In most areas, the costs over that period jumped by 200 or more per cent. Prescription drug hikes topped the *700 per cent level.*

Can your organization afford *that* kind of commitment? Many organizations no longer can afford to do so. For



(Source: Canadian Institute for Health Information)

example, Canada's *"big three"* auto makers reported that their health benefit costs for former employees rose by 22 per cent in the three years from 2000 to 2003 to $308 million. Health benefits alone now account for eight per cent of the Ford Canada payroll.

While benefit reductions were discussed in the latest round of bargaining between the companies and the Canadian Auto Workers, the two sides skirted a clash by agreeing to cap dispensing fee reimbursements and promoting generic drug substitution.

Steps to consider

If your corporate philosophy or labour practices make the offering of retiree benefits a necessity, or if you are considering expanding your benefit offerings to that group in order to encourage the recruitment of more mature workers, there are steps you can take to contain some of the cost pressures that are inherent with this benefit. They include the following:

- **following the lead of the *"big three"* car manufacturers by capping drug or other expenses. These can include annual or lifetime maximums per member;**
- **establishing robust eligibility requirements for post-retirement benefits that include years of service, minimum age or other requirements;**
- **encouraging generic drug substitution and implementing alternative benefit clauses within benefit programs;**
- **developing cost-sharing programs that include realistic deductibles and co-pay arrangements;**
- **introducing health care spending accounts to cover a select range of benefit entitlements to specific groups of retirees; and**
- **offering cash in lieu of benefits in post-retirement settlements.**

Your Coughlin & Associates Ltd. consultant is available to review your organization's retiree benefits needs.

It's about those boomers…

The fuel behind the drive to retain older workers, develop retiree benefits and restrict early retirement options is the baby boomer.

Those born between the years 1946 and 1964 comprise the largest segment of the population. And when you're that big, you get noticed.

This year, the leading edge of the baby boom reached age 60, the time when many retirement programs, including the Canada Pension Plan, allow early retirement.

Already in workplaces across the country, the rush to the door has begun.

However, is the boomer ready to make the transition from hippie to yuppie to grumpy old man?

"The future heart health of today's boomer is looking bleak"

According to data published by the Heart and Stroke Foundation of Canada, boomers are on the cusp of facing a *"health-heart crunch"* as the combination of a poor diet, a sedentary lifestyle and age catch up to them.

Some disturbing facts about today's boomers include the following:

- **30 per cent are obese;**
- **21 per cent smoke;**
- **52 per cent are physically inactive; and**
- **57 per cent do not believe their weight has an effect on their cardiovascular health.**

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It's about those boomers…

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The "pay later" attitude of that generation will likely result in drastically increased demand for angioplasty, bypass and other surgeries, the Foundation says. The problem: one-quarter of health care professionals are also baby boomers and are in line for retirement.

"The future heart health of today's boomer is looking bleak," says Foundation spokesperson Dr. Beth Abramson.

If trends continue, plan sponsors should expect the coming "crunch" to manifest itself in much higher medical and drug claims in the years to come. While pooled employee benefit plans may offset some of these risks from the lower claims experience of younger and more healthy members, retiree plans composed almost exclusively of boomers age 60+ will likely undergo extreme cost pressures.

Early retirements of the '90s a big mistake, OECD says

The early retirement programs that stalked the workplaces of the 1990s were a mistake, the Organization for Economic Co-operation and Development (OECD) says.

In an address to Toronto business leaders this summer, OECD Director of Employment, Labour and Social Affairs John Martin said that the buyouts, forced exits and induced retirements of that decade spawned a labour shortage that is expected to grow worse in the coming years.

"Many older workers were induced to leave by very generous early retirement schemes but relatively few young people were subsequently hired in their places," he said. The result, he noted, was that employers are now grappling to find and keep experienced and skilled labour.

"In all countries, early exit from the labour force tends to be a one-way street"

With more people living longer and healthier lives after retirement, the idea of early retirement has grown in popularity. Meanwhile, those who were encouraged -- or forced -- to take the option are reluctant to return to the workplace.

"In all countries, early exit from the labour force tends to be a one-way street," Mr. Martin said.

To curb the labour loss, the OECD recommends the phasing out of early retirement programs in workplaces and the removal of early retirement incentives in private and public pensions.

"Public early retirement schemes should be gradually phased out, and public and private pensions as well as other welfare systems reformed so as to remove incentives for early labour market exit," he said.

Why older workers leave: poor health

One in five workers who leaves work in their 50s or 60s does so for health reasons, Statistics Canada says.

The September 24, 2006 report by the government agency should be sobering news for plan sponsors considering retirement benefits programs. Such plans could provide a "haven" for chronically ill and higher risk individuals to migrate to when they can no longer remain in the workforce.

While the vast majority of older workers are in good to excellent health, Statistics Canada says, conditions such as arthritis, rheumatism, high blood pressure and back problems have resulted in the exit of a half a million workers in that age range.

"For every 100 working men aged 50 to 54 in 2003, only six were not working because of ill health," the agency reported. *"By the age of 65 to 69, this ratio had tripled to 19. For every 100 working women aged 50 to 54, 10 were not working for health reasons. By the age of 65 to 69, this had risen nearly fourfold."*

Most organizations ignoring growing retention issue, Board says

Most employers expect to face labour shortages within the next five years but few are doing anything about it, the Conference Board of Canada reports.

In a survey of 137 companies across the country, 80 per cent reported that they expect to face labour shortages as members of the aging workforce begin to retire. In fact, 25 per cent are already having trouble finding skilled or experienced workers, the Board says. Yet most are doing nothing to retain those workers.

80 per cent reported that they expect to face labour shortages

"Canadian employers are doing little to tackle the aging work force from a strategic perspective" Conference Board says. *"While many large and mid-size organizations have implemented human resources policies to improve their employees' productivity, policies and programs targeted at older workers are few and inconsistently applied,"* it says.

The Board suggests *"creating a positive work environment for older workers"* in order to attract and retain senior employees including flexible hours, improved training, and special bonuses and support to encourage those over the age of 50 to remain in the workforce.

the inability to attract and retain talent was seen as the number two threat to corporate profitability

The Conference Board's findings were mirrored by a survey of 250 senior executives by Accenture, a global management consulting firm.

In its annual survey of business issues and trends, the inability to attract and retain talent was seen as the number two threat to corporate profitability and was cited by 51 per cent of respondents as a major problem. This represented a jump of 11 points from the 2005 survey results, the organization noted. The issue easily surpassed other concerns such as product development, brand equity, competitiveness or terrorism on the business threat scale.

"The workforce, including major human resources issues such as recruitment and retention, continues to be a top business challenge in Canada," says Accenture's Managing Director for Canada Bill Morris.

With the focus moving to the recruitment and retention of active members of the workforce, it may be time for plan sponsors to consider using their benefit packages as retention tools for existing workers. Your Coughlin & Associates Ltd. consultant can help your organization develop benefits programs to complement your organization's retention strategies.

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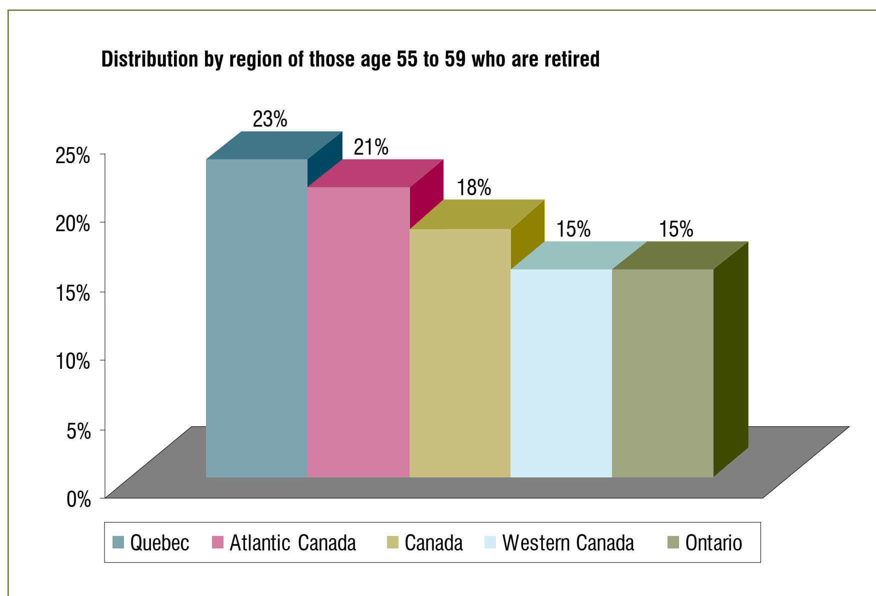
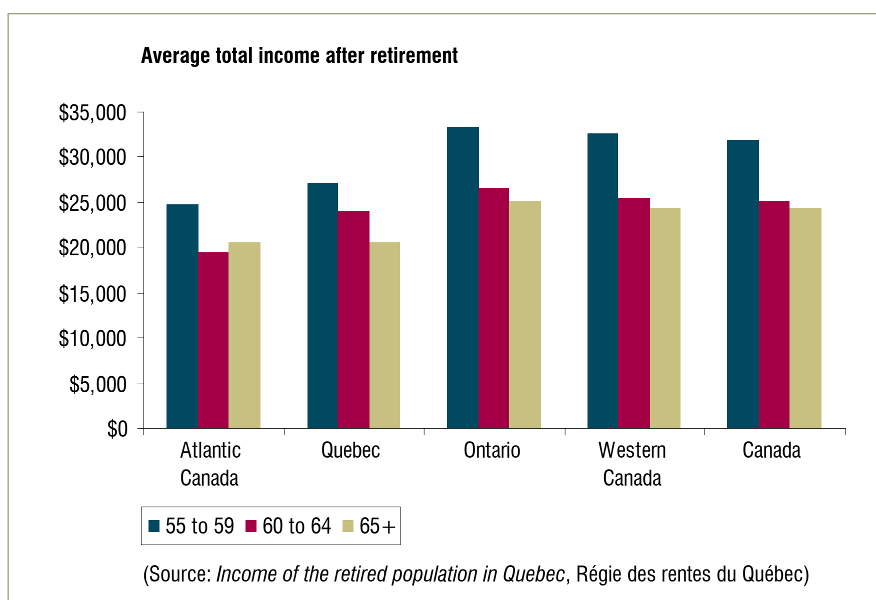
Retire early or retire rich?

If you live in Quebec, chances are you'll retire at an earlier age. But if you live in Ontario, you'll retire richer.

Quebec has the highest percentage of retirees age 55 to 59 in the country according to the Régie des rentes du Québec (RRQ), accounting for almost one-quarter of early retirees. Ontario, which has 43 per cent of the Canadian population, is tied with western Canada with the lowest portion of younger retirees. The breakdown by region is:



However, in all age categories Ontario's retirees earn more income than their counterparts across the country.



(Source: *Income of the retired population in Quebec*, Régie des rentes du Québec)

FAST FACTS

- Size of the Canadian labour force: 17.3 million. Percentage of working age population: 67.2 per cent.
- Number of workers age 55-plus who had jobs: 30 per cent.
- Median retirement age in Canada: 61. Number of people within 10 years of that age: 3.6 million, or 22.2 per cent of the workforce, according to Statistics Canada. Total percentage of the workforce within 10 years of age 61 in 1986: 10.3 per cent.
- Delta Airlines has received permission to terminate its pension plan for its pilots. The plan's termination is part of its re-organization while under bankruptcy protection.
- British Pension Regulator David Norgrove says that many UK pension funds have underestimated the life expectancies of their members and will face *"nasty surprises in the future."* Longer life expectancies will drain funds' ability to meet their obligations over the long term, he noted. He went on to urge plan sponsors to re-visit their actuarial assumptions as quickly as possible.