

The employee benefits system

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All indications are that, without intervention, these outcomes will continue to deteriorate. Imminent reforms may help to some extent but action from other stakeholders is required to unlock the full potential of the employee benefits system.

We firmly believe that employee benefits have a future and that the employer remains the natural channel through which employed South Africans can save for their retirement, buy insurance cover, join a medical scheme and maintain control over their financial well-being throughout their working life. Employee benefits systems can be designed to deliver value to employers, employees and society at large.

However, an increased focus on highly interdependent relationships between everything and everyone in the employee benefits system is required. This book gauges the current state of the employee benefits system and sets out suggestions for its improvement.

We have laid out the discussion in three parts:

[The first section, the employee benefits system](#), explores the complex relationships in the employee benefits system and assesses significant employee benefits in greater detail.

[The second section](#) delves into detail on practical issues that may cause poor benefits outcomes if not well managed. Many stakeholders may be unaware of these issues.

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Foreword by Alexander Forbes Group Chief Executive, Edward Kieswetterer

When I first joined Alexander Forbes in 2010, what really struck me was the extraordinary depth of information and insights the Group had been able to build up over the years.

As such I've made it a priority to find ways in which Alexander Forbes could share that wealth of knowledge.

This book represents an important milestone in that knowledge-sharing with those who are faced with the challenge of ensuring that individuals maintain some level of financial viability throughout both their period of employment and their post-retirement years.





This book had three specific objectives for Alexander Forbes:

- > As a **THOUGHT LEADER**: to share the insights we have developed over many years.
- > As an **INFORMED VOICE**: to contribute to one of the most critical dialogues that will lay the foundation for social security reform by the government.
- > As a **RESPONSIBLE CITIZEN**: to raise the awareness of the important need to improve our savings culture as a nation.

The last 30 years have been significant in the development of employee benefits. We have seen a shift from defined benefit (DB) to defined contribution (DC) arrangements, where individuals have greater input and accountability for their structures. There has been a development of more equitable and inclusive employee benefits systems that reach a far greater population of South Africans than ever before. And more recently, employees are being given greater choice and flexibility in their benefits. As such, South Africa now stands as one of the few countries globally with such breadth and depth of experience around DC arrangements. This means that the lessons we have learned, and the lessons we continue to learn, should be of critical interest to any number of other economies, both developing and developed. We know the world is watching with interest.

The questions this book addresses are: “How effective have these programmes been?” and, more importantly: “What should we do to make these outcomes more impactful?”.

Without doubt we have made progress. But in truth, we still have some way to go before we can translate any gains we may be making into a more financially stable world for our workers. Despite the advances, South Africa still has one of the lowest savings rates in the world.

But, if we can create a more effective linkage between employee benefits, employee wellness, and engagement between employer and employee, then all parties stand to benefit financially.

If we can begin to recognise the place of employment as being the natural environment for advancing financial education and effective budgeting and financial planning for the individual, we can begin to address the challenge that has seemed almost unachievable: “How can we get South Africans to save?”.

The problems demand that we understand the complex social and cultural fabric underpinning the South African work environment. Our fragmented approach does not help to resolve these challenges

Our research shows unequivocally that the problems go beyond purely financial issues. They demand that we understand the complex social and cultural fabric underpinning the South African work environment. Our fragmented approach does not help to resolve these challenges.

The research highlights the critical interconnectedness of a number of defining considerations:

- > The need to balance current needs with future needs.
- > The need to balance contributions at the right levels to provide for retirement benefits, healthcare and risk benefits as part of a total rewards system.
- > The need to balance behavioural factors such as individual preference, age, culture, upbringing, educational background and lifestyle.
- > The need for a system that balances individual choice with certain minimum default options on design issues such as contributions and preservation.
- > The need to balance the interests of the employees, employers, trade unions, all taxpayers and the government through greater financial literacy and better benefits design.

A more effective delivery to South Africans demands that the key stakeholders actively engage in dialogue and collaborate more constructively with the right people at the table, focused on the right issues, with a collective resolve and unified sense of purpose, we will get to the right answers.

We invite you to join us at that table. The time is now!

Editorial: Remembering the human face of the employee benefits system

What is the difference between 45 and 46? If we are referring to the number of people who died at Marikana, it is someone's son, brother, husband or father. If we are referring to the age at which a construction worker is forced to stop work because of a back injury, it represents an additional year of financial hardship. If we are referring to thousands of rands in a retirement fund of a 25-year old office worker, it can mean a dignified retirement in a future he cannot even imagine for himself.

The industrial action in the second half of 2012 highlighted to us all the impact that remuneration and employee benefits can have on our country, our employers and our workforce. But there is another side to employee benefits. If designed appropriately to address employees' needs, they can unlock productivity and profitability through a happy, healthy workforce. If interests are aligned, we all win. If they are not, the consequences could be dire, now and in the future.

Aligning these interests requires careful consideration of all stakeholders including trade unions, employers, workers and the government.

The Benefits Barometer provides a comprehensive overview of the employee benefits system. It highlights the key problems as we see them and identifies some principles for addressing them. However, it also acknowledges the practical problems that arise when trying to apply these principles in the real world. So an analysis of the problems, principles and practicalities is presented at an economic sector level.

This is not intended to be the definitive work on the issue. It is intended to be the catalyst for a national and inclusive discussion on how to use employee benefits in a way that benefits all stakeholders.

Every effort has been made to ensure that the material presented is thoroughly researched and substantiated. We recognise that there may be various ways of interpreting data and material and would welcome any comments, criticism or queries that would further this national debate.

However, even using the most high-level macro-economic view, it is important to remember that at the heart of this issue are real people working in real organisations, for whom the difference between 45 and 46 is very real indeed.

Megan Butler
Johannesburg
January 2013

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Executive summary

The Employee Benefits System

There is a growing recognition that employee benefits should meet the needs of individual employees and not a hypothetical average employee. The financial services industry has applied some of its best thinking to the delivery of a new generation of needs focussed benefits, and some progress has been made. However, for the employee benefits system to reach its full potential, the complex relationships between the issues, benefits and stakeholders need to be more deeply appreciated. Unless this is done, the outcome will remain ineffective in terms of meeting members needs, enhancing business imperatives and safeguarding the government from having to address the shortfall.

The major employee benefits of healthcare, risk benefits, retirement benefits and financial education could provide an effective catalyst for boosting employee well-being and stimulating employee engagement.

Alexander Forbes believes that the employee benefits system still represents one of the most effective formal channels for creating a savings culture in South Africa, as well as ensuring that individuals have sufficient protection in place for events that put their earnings potential at risk. The focus of this book is to identify sources of inefficiency and slippage. More importantly, it sets out the framework for a dialogue that must occur between all stakeholders in the delivery chain if we are going to extract the best results for all concerned.

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Healthcare benefits

Contributions to medical schemes have been increasing faster than salaries due to rapid increases in the costs of healthcare. Very few employers still offer post-retirement medical benefits and individuals may find the ever-increasing contribution rates on medical schemes to be unaffordable.

Employers should reconsider the current ways of communicating the importance and structure of medical scheme benefits to ensure that employees choose to participate in the most appropriate benefit options.

Risk benefits

Members' risk benefits needs will differ according to their circumstances and over the course of their lives. However, the typical bundle of group risk benefits is static and structured for the average employee, not tailored for the individual. We propose that schemes offer choice in risk benefits or else set defaults that better match the members' needs as they go through life.

Retirement funding

The current retirement savings environment is characterised by low contributions, low expected investment returns, climbing annuity prices and a culture of low preservation rates. The fact that emphasis is typically placed on asset returns and not on managing assets to deliver a reasonable retirement income has exacerbated the problem. The result is a retirement benefit that is insufficient to meet the needs of pensioners, and that many savers perceive as having little value relative to the satisfaction of their immediate needs.

The contribution rates, investment strategies and preservation strategies all need to be re-examined. In addition, where choice is offered, employees should be nudged towards more responsible decisions. However, even with the best efforts of the trustees and the employer, the retirement fund may not be able to deliver levels of savings that will see employees through their retirement years. Where this is anticipated, employers should offer 'financial wellness' programmes that help members develop effective budgeting skills and financial literacy before they require debt counselling.

We propose an integrated approach to employee benefits that is focused on what employees need, with a benefit structure that reflects the employer's values. The benefits should be communicated effectively to employees and reviewed regularly.

Financial education

Low and declining household savings rates illustrate the lack of engagement that individuals have with their future financial needs. This is a good indication of a lack of engagement with employee benefits generally. At the heart of the problem is the lack of financial advice relating to effective planning and budgeting on offer at the right place, and at the right price. For many individuals, the workplace will offer the best

opportunity for receiving financial advice. Employers should be more actively involved in finding the right medium of delivery and the right messages.



What can be done to improve benefit outcomes?

Recognising the inter-connectedness of benefits and managing them holistically

The current fragmented approach to employee benefits does not lend itself to getting the best outcomes for employees or employers, as it does not take account of the connections between:

- > The various financial services products and safety nets that an individual may have privately, through the employer, through the union or through the government.
- > Physical, mental and financial health and employer profitability.
- > Employee benefits, employee engagement and employer profitability.

We propose an integrated approach to employee benefits that is focused on what employees need, with a benefit structure that reflects the employer's values. The benefits should be communicated effectively to employees and reviewed regularly. The approach also needs to take account of practical issues. This kind of employee benefits system will also benefit employers by increasing employee engagement and organisational commitment – two essential ingredients to boosting productivity. In addition, improving the well-being of employees should have direct and indirect impacts on productivity.

Ensuring benefits meet individual needs more effectively

For various reasons, the employee benefits provided are often different to what the individual needs. One reason this arises is a 'one size fits all' approach to the benefit design as opposed to tailoring benefits for the individual over their lifetime. In addition, the benefit structure should recognise that basic needs should be met first.

Improving financial engagement at all levels

A key finding of our research is that individuals are typically not engaged with financial issues ranging from savings to ensuring sufficient protection of their earning capacity from risk events.

Over the years, the industry has tried to improve financial literacy through education programmes. Although it takes many years to see if these kinds of programmes work, indications are that the industry needs to do more to help improve financial awareness and behaviour.

This publication sets out some changes that can be made to incentives, education, communication and access to advice to help improve individuals' engagement with these critical issues and ultimately help them to make the right choices.

The Issues

Any solution has to be grounded in the practical reality in which employees and employers find themselves.

ISSUE	IN THEORY...	THE PRACTICAL REALITY IS THAT...
Unhealthy finances	Employees should focus on work in the workplace.	They are often distracted by their personal financial problems.
Low-income earners	Employees who earn enough should save for retirement and those who do not earn enough, should not.	It is sometimes difficult to tell who will benefit from saving and who won't.
Absenteeism and incapacity	Employees who are able to come to work must do so and employers should take care of those who are unable to work due to ill-health or injury.	Employees often abuse sick leave, and the disability management processes are often inefficient. Employers seldom plan for workers being forced to retire early.
Incentives	People will save more if we incentivise them to do so.	They're unlikely to behave any differently, particularly if the value of the incentive is not clearly understood.
Temporary and informal workers	Everyone has a job with benefits.	Many South Africans don't, particularly temporary and informal workers.
Choice	Providing people with choice allows them to tailor solutions to meet their own needs.	People seldom choose at all and when they do, those choices rarely address their long-term financial needs. Financial education doesn't always help.
Bricks and books	Everyone has a place to live and access to education for their children.	Many people need their employer to help them.
Strikes	You can always avoid industrial action.	Not always and when there is a strike, employees lose benefits coverage.
Young workers	Employees start saving early and get into responsible habits.	Young workers don't appreciate benefits or get an opportunity to set those responsible habits.
Pensionable pay	If employees do all the right things, they will replace a reasonable percentage of their take-home pay in retirement.	If employees do all the right things, they might replace some of their pensionable pay in retirement – and too often this is much less than they need.
High salary inflation	High salary increases are a good thing.	They create shortfalls in retirement funding relative to salary at retirement.
Mass exits	No one is ever forced to leave their job.	Industries shut down, companies liquidate and when companies retrench, employees lose both their jobs and benefits.
Longevity	The right retirement age is 60, 63 or 65.	The choice between 60, 63 and 65 is typically arbitrary and with increasing longevity, this is too early for some workers, unnecessarily reducing their benefits.

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