BANKING ON PRODUCTIVITY:
MANAGING EMPLOYEE HEALTH COSTS

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MORNEAU SHEPELL

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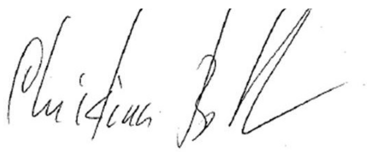

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EXECUTIVE SUMMARY

More than half of Canadian financial leaders in a recent survey say employee health, drug and disability costs have increased significantly or are expected to rise. Yet only 15% of those surveyed have considered a funding strategy to address the impact of future cost drivers such as an ageing workforce, drug plans, disability plans and legislative changes. According to the results of an online survey conducted by the Canadian Financial Executives Research Foundation and sponsored by Morneau Shepell, recruitment challenges and employee engagement issues stand out as the greatest threats to work productivity over the next five years. Survey respondents rated these two issues as their top challenges. (56% rated employee engagement as the first or second greatest threat to productivity, while 50% of respondents rated recruitment issues as a number one or two issue.)

53% of respondents said health benefit costs were significantly increasing, and 37% said they had increased somewhat over the past two to five years, due to inflation and population changes. Disability benefits costs were also seen as increasing, although not as quickly as health benefits costs. 20% said they were significantly increasing and 54% said they had increased somewhat.

From a cost perspective, health benefits were deemed of greatest concern to most respondents (62% ranked this issue as 1 or 2 on a scale of one to five, with 1 being most significant). Short term disability was also on the radar of survey respondents concerned about cost, with half (51%) rating short-term disability as a 1 or 2. This was followed by long-term disability (33% rated it as a 1 or 2), pension plan sustainability (27%) and workers' compensation (27% also gave this a rating of 1 or 2.)

From a risk perspective, when survey respondents were asked to rate the risk of a series of health and pension issues, drug costs were identified as a leading concern by 64% of respondents, who deemed the issues to be a significant or very significant risk, indicating a concern that drug costs will rise in future. Stress and mental health issues were second, with 55% of survey respondents rating them to be a significant or very significant risk.

How do organizations respond to these threats? Survey respondents say their companies offer the following: 61% invest in supporting employees to obtain care through employee assistance programs and health benefits, 35% promote early return to work for employees on disability leave with mental health issues through mental health supports such as counselling, as part of disability case management. 34% address stress management in their wellness program, while 19% said they invest in a mentally healthy workplace to promote engagement and performance. One in five (22%) said they do not address mental health issues directly.

Despite the obvious need for many survey respondents to stay on top of looming costs, many of them lacked the analytic tools that would be useful to help them meet this goal. For instance, 12% said they did not have any analytic tools to help them with projecting, planning or tracking costs. An additional 3% said their tools were insufficient, while an additional 12% said their tools provided an understanding of current cost drivers, but lacked projection capabilities.

The research study also indicates that Canadian financial executives should be aware of several emerging demographic and health trends which will have a substantial impact on the bottom line of Canadian businesses.

> “Employee retention is a key element in our long term profitability and that’s why we attach such an importance to it.”
>
> **Stephen Massel – CFO, Hotspex**

These trends include:

- an expected exponential increase in drug plan costs;
- a new standard on employer accountability with respect to mental health;
- an ageing workforce, the end of mandatory retirement, and their impact on absence and disability; and fiduciary responsibility and a rethink of the recent direction toward defined contribution employee pension plans.

A full understanding of these issues is important for CFOs and other business leaders, given that a sizeable number are responsible for these areas of concern. For instance, nearly four in ten (38%) of financial executives surveyed by CFERF said they were accountable for HR in the reporting structure of their organization. In addition, 59% of respondents said they guide decisions related to strategic human resource management issues, 34% said they monitor results of HR management issues and take action as needed, and 19% said they actually make the decisions. (15% said they had no role in HR and 11% said they select the decision maker and review decisions.)

Drug costs in particular are a sleeping giant. Cost increases have been mitigated by a high number of drugs which have recently become available in generic forms. But this cost reduction is only temporary as a new wave of specialized medications and therapies come onstream.

Mental health has always been an issue in the workplace, but the potential risks to companies of not being proactive on this issue are becoming increasingly apparent. The impact is seen in absenteeism, productivity and engagement. The role of the workplace in mental health is also becoming clearer. On January 16, 2013, The National Standard for Psychological Health and Safety was released.[1] It provided a framework to reduce risks and potential liability related to workplace mental health, and to promote a mentally healthy workplace. Although the standard is voluntary, employers should also be aware of the existing legislative accountability landscape that specifically relates to mental health. These include regulations relating to occupational health and safety, worker's compensation, human rights, law of torts, employment standards, employment and labour relations, as well as standards with respect to employment contracts. In short, the responsibilities employers have with respect to physical health and safety,[2] also apply to mental health and safety. However, only a minority are aware of their risks in connection with this legislative accountability, and 67% said the issue is not well understood.

As drug costs increase, so is the average age of the workforce. The baby boomer bulge is now nearing retirement, so a higher percentage of workers will be older, and thus more in need of health care and medication. Absence from work as well as short and long-term disability claims as a result of illness is also expected to grow as workers get older. This trend will only increase with the end of mandatory retirement.

[1] The National Standard of Canada titled Psychological Health and Safety in the Workplace - Prevention, promotion and guidance to staged implementation is available at www.csa.ca

[2] Shain, Dr. Martin. Tracking the perfect legal storm. Mental Health Commission of Canada (MHCC). 2010

Organizations surveyed presented a variety of perspectives on their confidence and ability to manage their pension plan. For instance, 60% of large organizations said their strategic planning and cost management is strongest in the area of pensions, while only a minority of medium-sized companies (36%) and small companies (29%) said pensions were their strongest area when it came to strategic planning and cost management. In fact, only 10% of large companies said pensions were their weakest area, compared to medium-sized companies (36%) and small companies (35%).

Employers must also think carefully about risk transfer as the shift continues from defined benefit to defined contribution pension plans. While defined contribution plans reduce the burden of risk on the employer, they move the risk to the individual employee who may be ill-equipped to administer, for instance, their own self-directed RRSP. This in turn creates a risk for the employer if the employee loses retirement funds and argues the employer should have been responsible. In fact, employers who encourage employees to switch from DB to DC plans can leave themselves vulnerable to a lawsuit if the DC plan underperforms expectations.[3]

Organizations facing these and other HR challenges should take advantage of the specialized skill sets of their CFOs to help with HR costs related to pensions, drugs, health benefits, absence and disability and other drivers. CFOs in turn should reach out for additional support in obtaining advice and tools to effectively measure, forecast and predict the impact of the demographic , economic, legislative and regulatory trends outlined in this study. In this way, CFOs can help keep both their organizations and their employees healthy.

“We have two DB plans and a DC plan. The DB pension obligation is the biggest financial exposure that we have. We're trying to understand the relief measures that are available, in terms of amortization of the obligation over a longer period of time. . . . We have taken some of those measures and it's relieved some of our cash flow impacts going into 2013 and beyond. But it doesn't detract from the fact that we still have this DB obligation that's hanging around our necks, which is tough to get out of.”

Roger Rees – CFO, SCI Group

“In a smaller organization, the CFO and HR must work collaboratively, each bringing their respective expertise to the table to help a company understand and analyse the implications of rising employee costs.”

Rod Ancrum – SVP Finance, HR & CFO, Credential Financial Inc.

[3] Gray, Jeff. Pension conversion fallout lands in court. The Globe and Mail. August 23, 2012.

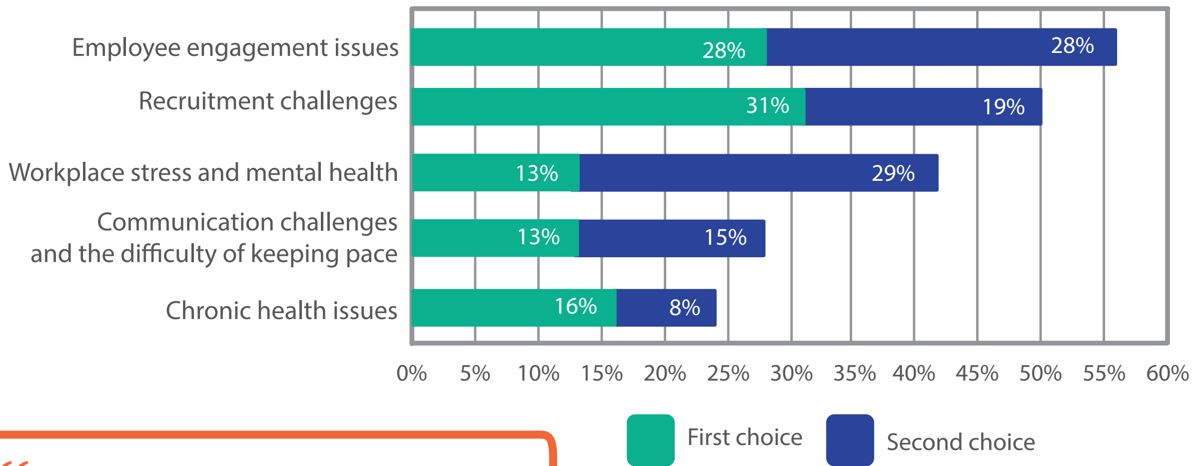
METHODOLOGY AND DEMOGRAPHICS

Perspectives from senior financial executives across Canada were gathered through an online survey, which was completed by 95 respondents. A wide range of industries were represented, including agriculture, forestry, fishing and hunting; mining, quarrying, and oil and gas extraction; utilities; construction; manufacturing; transportation and warehousing; finance and insurance and other sectors. Respondents worked for organizations with operations in various parts of the country, including Alberta (53%), Ontario (51%), British Columbia (47%) and Quebec (31%). Further insights were gathered at an executive round table, which was held simultaneously in three cities (Vancouver, Toronto, Montreal and Calgary) on March 4, 2013.

OVERALL COST RISKS

Recruitment challenges and employee engagement issues stand out as the greatest threats to work productivity over the next five years, according to survey respondents, who rated these two issues as their top challenges. (56% rated employee engagement as the first or second greatest threat to productivity, while 50% of respondents rated recruitment issues as a number one or two issue.) Workplace stress and mental health are also leading concerns (rated one or two by 42% of respondents.) This was followed by communication challenges and difficulty keeping pace, and chronic health issues (rated one or two by 24%). Please see Chart 1.

CHART 1 – WHAT DO YOU BELIEVE WILL BE THE GREATEST THREAT TO WORK PRODUCTIVITY OVER THE NEXT 5 YEARS?



> "Chronic health issues relate not just to employees, but also to family members, all of which could have an impact on the productivity of the employees, even though they themselves are perfectly healthy."
>
> **– Survey respondent**

When survey respondents were asked to rate the risk of a series of health and pension issues, drug costs were identified as a leading concern by 64% of respondents, who deemed the issues to be a significant or very significant risk. Stress and mental health issues were second, with 55% of survey respondents rating them to be a significant or very significant risk. See Chart 2. Issues identified as a risk or significant risk by large companies were pensions (78%), drug plan costs (60%) and stress and mental health (60%).[4] In comparison, medium-sized companies were more concerned about drug costs, with 73% deeming these to present a risk or significant risk, and 54% most concerned about stress and mental health. Small companies were also most concerned about drug plan costs (60%) and stress and mental health (53%). See Chart 2 and Appendix A.

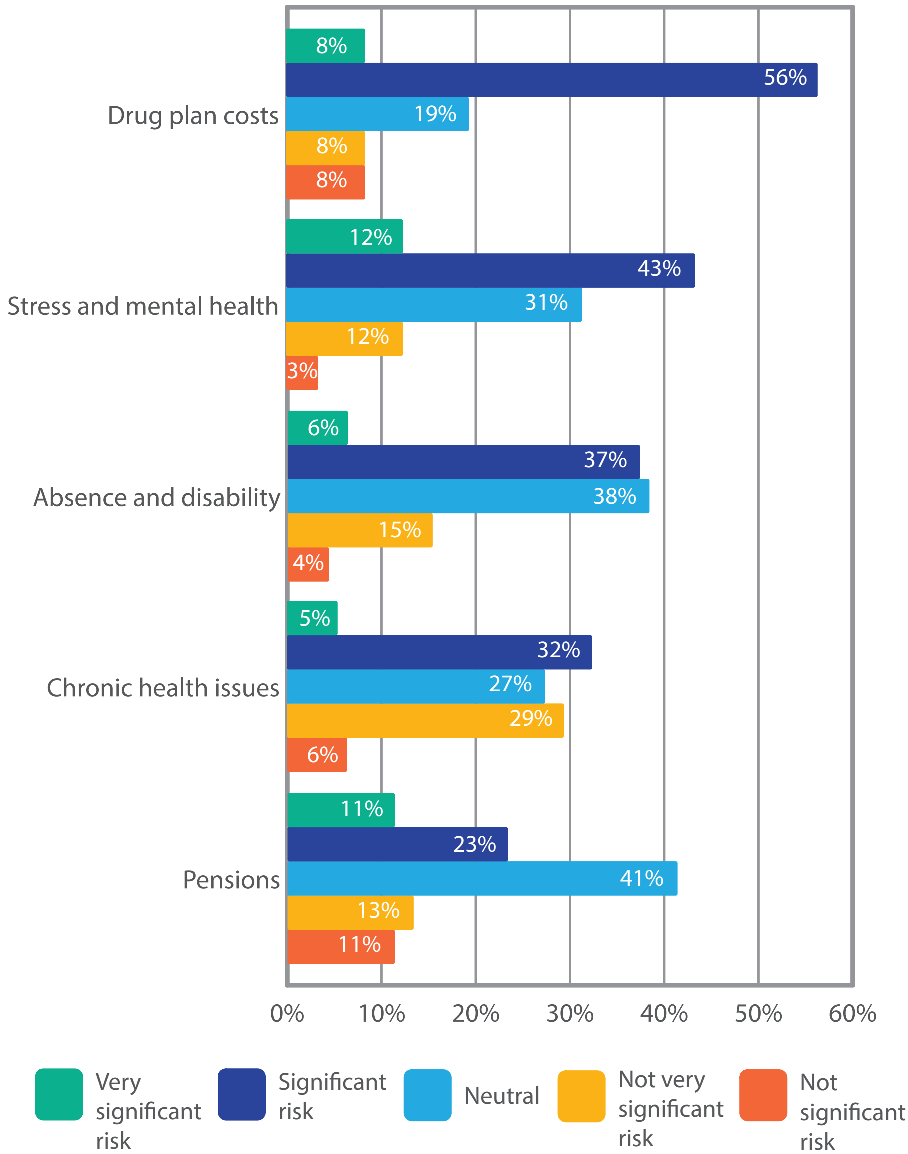
"At a former company, there was an attempt to cut our cost of benefits by limiting dental visits to every nine months from six. And it caused grief – people were in and out of my office complaining about it. At that time a lot of people had little kids and every time they went to the dentist, they had to shell out. They were just not prepared to go through that pain. People actually left over it, and for really insignificant savings to the company, we lost some good people."

Bill Cromb – VP Finance, Maha Energy Inc.

[4] See Appendix for pie charts by company size.

OVERALL COST RISKS

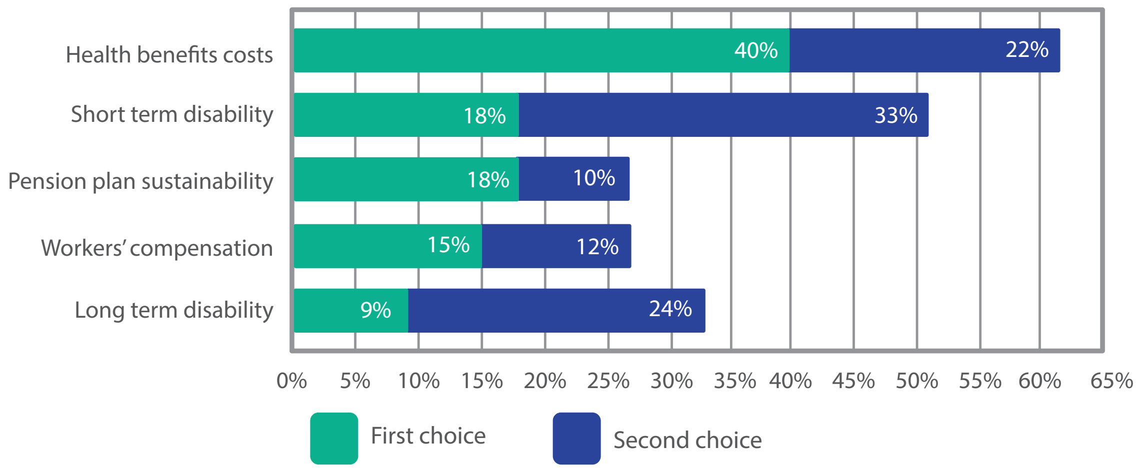
CHART 2 – RATE THE LEVEL OF SIGNIFICANCE OF THE FOLLOWING EMPLOYEE COST RISKS FOR THE NEXT 5 YEARS



From a cost perspective, health benefits were deemed of greatest concern to most respondents (62% ranked this issue as 1 or 2 on a scale of one to five, with 1 being most significant). Short term disability was also on the radar of survey respondents concerned about cost, with more than half (51%) rating short-term disability as a 1 or 2. This was followed by long-term disability (33% rated it as a 1 or 2), pension plan sustainability (27%) and workers compensation (27% also gave this a rating of 1 or 2.) See Chart 3. For respondents from large companies, short term disability was considered the greatest cost worry (deemed 1 or 2 on a scale of 1 to 5) for 70%. This was followed by pension plan sustainability (60%). For medium-sized companies, the greatest concern was health benefits costs (63% rated them a 1 or 2), followed by short term disability (60%). Small companies with revenues under $99 million were more worried about the costs of health benefits (65%) and somewhat concerned about short term disability (40%).

CHART 3 – WHAT DO YOU BELIEVE IS YOUR ORGANIZATION'S MOST SIGNIFICANT COST CONCERN?

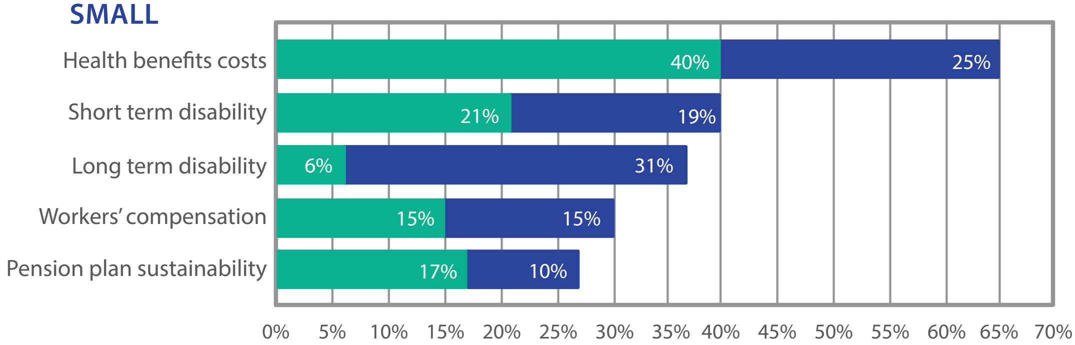
ALL RESPONDENTS



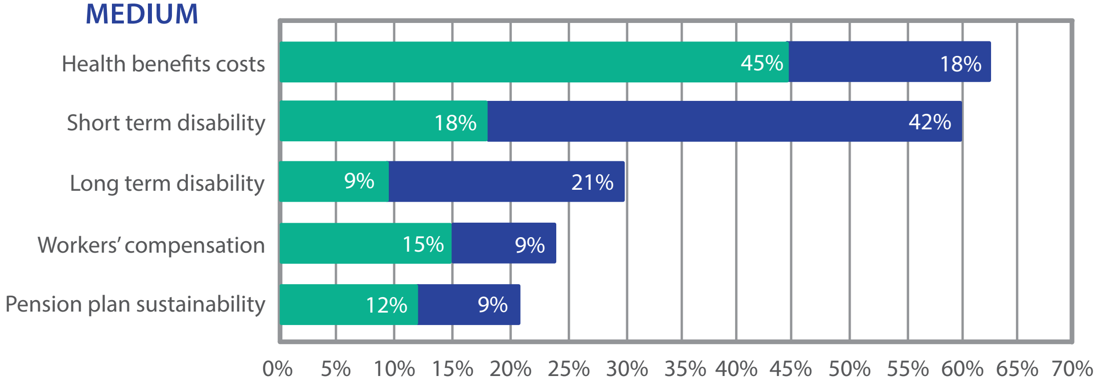
OVERALL COST RISKS

BY COMPANY SIZE:

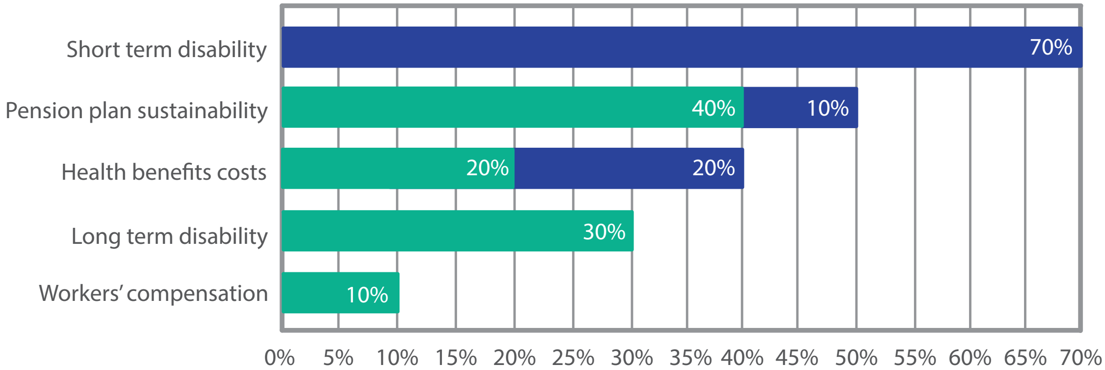
SMALL



MEDIUM



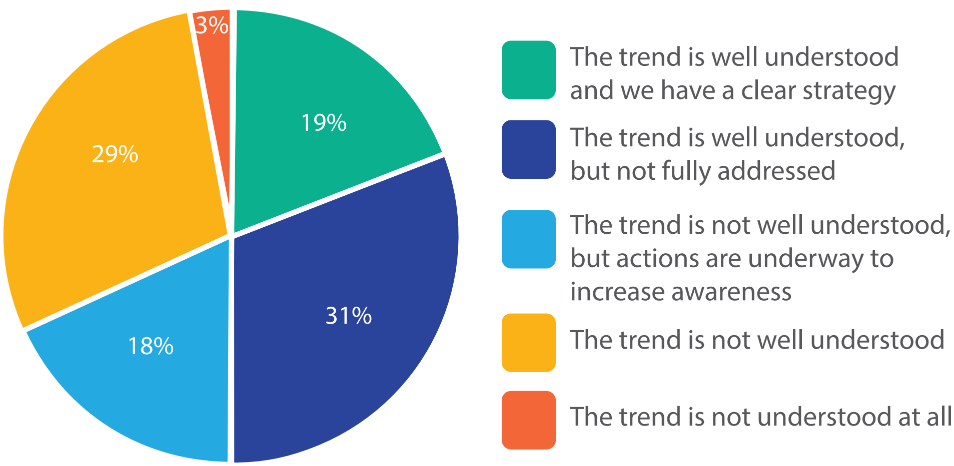
LARGE



DRUG COSTS AND HEALTH BENEFITS

As noted above, drug plan cost increases were considered by 64% of survey respondents to pose a significant or very significant risk. Only 19% of all respondents said the trend was well understood by the company, and that it had a clear strategy. However, large companies were far more likely to say they had a clear understanding and strategy (60%), compared to only 16% of medium-sized companies and 13% of small companies.

CHART 4 – HOW WELL PREPARED DO YOU BELIEVE YOUR ORGANIZATION IS TO MANAGE THE COST RISKS RELATED TO PROJECTED SIGNIFICANT INCREASES IN HIGH COST MEDICATIONS IN YOUR DRUG BENEFITS PLAN? (E.G. WHERE ONE CLAIMANT MAY INCUR $20,000 TO $35,000 PER YEAR)?



According to Paula Allen, Vice-President, Health Solutions and Practice Leader, Consulting, for Morneau Shepell, employers are taking many different approaches to reduce waste, defined as health costs which do not directly improve the health of employees or families. Obvious examples include delivery costs and dispensing fees. Employee behaviour can also affect costs, such as not taking medication appropriately, filling scripts but not using them, lifestyle choices that make medication less effective, choosing brand name drugs instead of generic, or taking an expensive medication when a cheaper equivalent in the same class of drugs would have the same result.

Increases in total drug costs over the past few years have been moderate, but Allen warned that price increases have been mitigated by a large number of medications which have seen their patents end. Generic costs have also decreased, she said, but that decrease has masked an increase in the cost and availability of specialty biologic medications. "The increase started the exponential curve and is expected to continue," Allen said, adding these newer, more costly medications for major illnesses cost an average of $7,000 to $42,000 dollars annually per claimant, while some run into six figures. "These medications are really taking up the majority of the pipeline for new medications coming on the market. The increased utilization is expected to grow at a faster rate. They're also highly effective for managing quality of life, so the demand by the employee population is expected to be considerable," Allen said, pointing out that there is also little likelihood of significant cost reductions when these newer medications come off-patent.

"In a relatively small company of 250 staff, benefit expenses can be significant. In order to manage our costs at Credential, we aligned our benefit programs with our shareholder group so that together our costs are reduced."

Rod Ancrum – SVP Finance, HR & CFO, Credential Financial Inc.

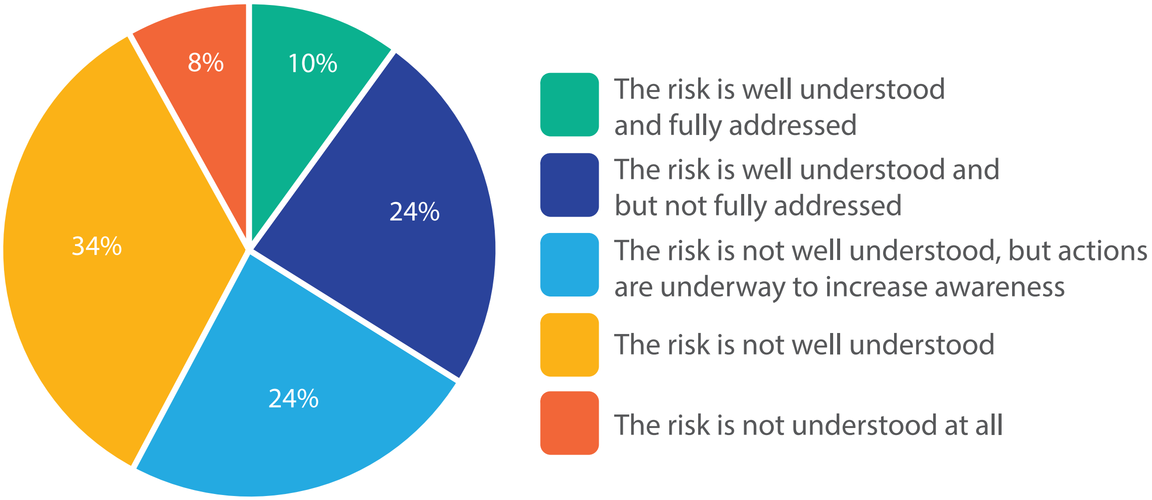
MENTAL HEALTH

As noted above, stress and mental health issues were considered by 55% of survey respondents to pose a risk or very significant risk, but only 10% of all respondents said the issue is well understood and fully addressed. See Chart 5.

Mental health was considered by respondents to be one of the most significant components of overall health and disability costs (50% rated it a 1 or 2 on a scale of 1 to 5, with one as most significant). Mental health came second only to cardiovascular conditions, which was rated a 1 or 2 by 53% of respondents.

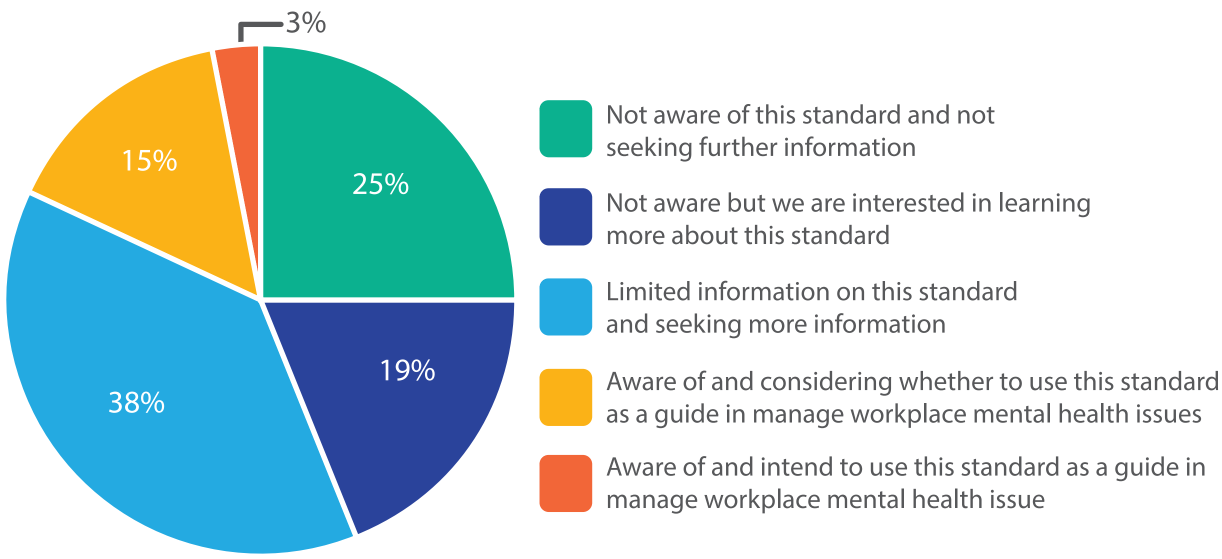
In response to these risks, survey respondents say their companies offer the following: 61% invest in supporting employees to get access to care through employee assistance programs and health benefits, 35% promote early return to work for employees on disability leave with mental health issues through mental health supports in disability case management. 34% address stress management in their wellness program while 19% said they invest in a mentally healthy workplace to promote engagement and performance. One in five (22%) said they do not address mental health issues directly.

CHART 5 – HOW WELL DO YOU BELIEVE YOUR ORGANIZATION MANAGES MENTAL HEALTH RISKS RELATED TO EMERGING LEGISLATION IN WORKERS' COMPENSATION AND OCCUPATIONAL HEALTH?



Financial executives were also asked about their awareness of the new workplace psychological health and safety standard, which was released in early 2013[5]. Implementation of this standard is currently voluntary, yet addresses current liabilities that employers bear, and is expected to form the basis for more specific emerging legislation in the future. The majority of survey respondents said they were not aware of or had limited information about the new standard.

CHART 6 – AWARENESS OF WORKPLACE PSYCHOLOGICAL HEALTH AND SAFETY STANDARD:



[5] The National Standard of Canada titled Psychological Health and Safety in the Workplace - Prevention, promotion and guidance to staged implementation is available at www.csa.ca The key topics covered in the standard include:

- Establishing commitment, leadership and participation
- Understanding the diverse needs of the organization's population so they can be appropriately addressed
- Maintaining confidentiality
- Establishing a policy and planning process to implement the system
- Identifying the organization's PHS hazards, assessing risks, and implementing preventive and protective measures
- Ensuring infrastructure and resources are in place to support the system
- Providing education and awareness, and ensuring key people are trained and competent
- Having processes in place to be prepared in the case of a critical event
- Collecting data, monitoring and measuring success

According to Morneau Shepell's Paula Allen, mental health is the single largest cost driver in benefit plans. "From an employee absence point of view, long term and short term disability, there is no single diagnostic category that has the same impact as mental health," she said. "Not only from a primary diagnosis point of view, but also a secondary point of view where mental health issues are either acquired or are underlying some of the reasons why people are off work or utilizing drug benefits."

In addition, some provinces are expanding the definition of compensable disability to include mental health. Allen observed employers are paying for mental health issues that arise as secondary to an injury, because they pay not only for the absence but all healthcare costs under worker's compensation.

Employers should also be aware of the legislative accountability landscape that specifically relates to mental health. These include regulations relating to occupational health and safety, worker's compensation, human rights, law of torts, employment standards, employment and labour relations, as well as standards with respect to employment contracts. In short, the responsibilities employers have with respect to physical health and safety, also apply to mental health and safety.[6] However, only a minority are aware of their risks in connection with this legislative accountability, and 67% said the issue is not well understood. See Chart 5, on page 14.

Recent efforts to address these responsibilities have resulted in a new national standard for psychological health and safety in the work place. Launched in January, 2013, the voluntary standard is the first standard of its kind in the world. "The purpose is to help reduce costs and risks, and to help organizations promote performance by building a psychologically healthy workplace," Allen said.

"You have to make sure you have a healthy workplace that's not toxic or difficult. You've got to have measures and feedback to tell you whether you've got a healthy workplace. You need third party assistance to provide to your employees because I don't think the employers really do that well and you need the highest level of confidentiality. All they can do is make that available through third party services. I think it comes down to doing it because it's the right thing to do."

Laurie Tugman – Executive Chairman, Nexterra Systems

[6] Shain, Dr. Martin. Tracking the perfect legal storm. Mental Health Commission of Canada (MHCC). 2010

MENTAL HEALTH AND PRIVACY

Personal health information is considered one of the most sensitive pieces of information that an employee has, according to Allen. "The employee has a tremendous right to not disclose what their personal health condition is, whether it's a cold, HIV or mental health issue," she said. According to her, knowing an employee's health concern puts employers at risk. "If you don't have it, then you can't be accused of discriminating against the employee using that information," she said. In addition, employers need to know whether an employee needs to have accommodation under Human Rights, or in order to help them to return to work while absent under a disability claim. In this kind of situation, the employer simply needs to establish what the worker can and can't do in terms of job duties, as seen in workers' compensation. Mental health and addictions are exceptions, Allen notes. "If you see somebody behaving in a way that's well outside the norm and you don't do anything about it, then you could be hit on the other side for being negligent because the person themselves might not have the faculty to tell you that they need accommodation," she said. "If a person deteriorates in front of you and you ignore that, you could still be held liable. So it's best when you see that type of situation just to refer them to a third party, your EAP provider or refer them to a consultant, a disability management provider, and wait for that individual's advice."

Employers wondering how to prevent or reduce liability should realize that everything they should do to foster mental health is the same as what they should do for a high performance workplace, according to Allen. For instance, training supervisors to recognize behaviour changes and how to have conversations about them is positive for performance, but also helps mental health. If somebody is returning to work from a Worker's Compensation claim or because they had surgery, a supervisor can help that person re-integrate and be productive in the workplace. "If they have a mental health issue it's an essential practice to structure the workplace so it's not going to cause undue stress. If people do the right things in terms of health overall, it'll cover off mental health, and if you have a provider who can help you manage those sticky situations, then you're probably well off in managing 99% of the situations that can get employers into trouble."

AGEING WORKFORCE/DISABILITY

As noted earlier in this report, absence and disability were deemed a significant or very significant risk by 43% of survey respondents. Over the past two to five years, due to inflation and ageing demographics, 53% of all respondents said health benefit costs were significantly increasing, and 37% said they had increased somewhat. 11% said they were stable. Disability benefits were also seen as increasing, although not as quickly as health benefits. 20% said they were significantly increasing and 54% said they had increased somewhat. About one in four (26%) said disability costs were stable. Worker's compensation costs were seen as the slowest growing, with only 11% of respondents stating costs were significantly increasing, and 34% stating they had increased somewhat. More than half (55%) said worker's compensation costs were generally the same.

When asked what was driving the increases, respondents attributed them to a range of drivers, including ageing population, an increase in drug use and drug costs, particularly in biologics, greater awareness of employees of their benefits, and increased employee stress resulting from a faster pace of work.

When asked about their current risk tolerance for costs in this area, 64% of survey respondents said the tolerance level was restricted to increases of less than 25%. An additional 15% said their tolerance level could be as high as a 30% increase, while only 6% said their risk tolerance could accommodate up to a 50% increase.

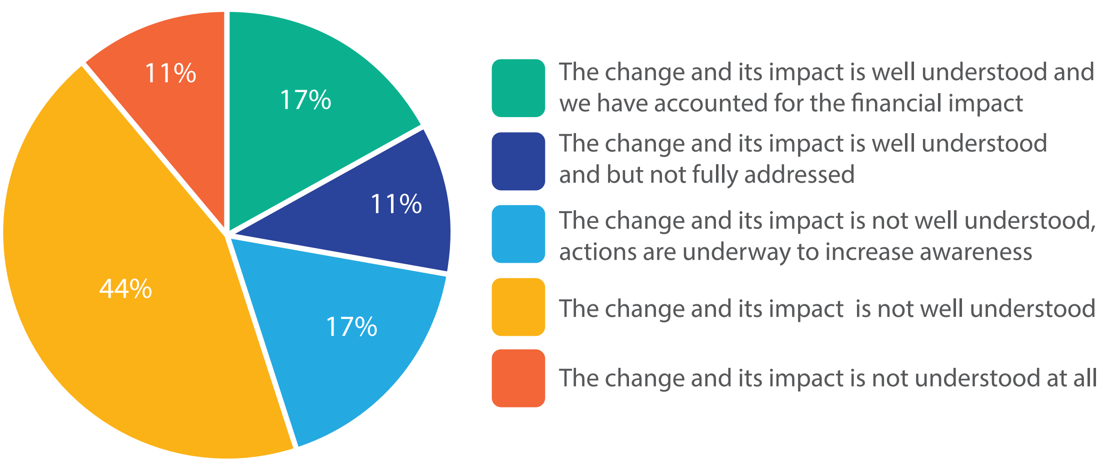
"The challenge we have is 15% of our 85 people are over 60, 40% over 50 and 75% over 40. Last year our medical usage went up by 50% and we have no caps on medical coverage. There has not been and there will not be any usage fee when you go to the store to pick up a drug. We have caps on dental, but our real issue is prescription drugs with our ageing population. It is driving prescription costs through the roof."

Wayne Braun – CFO & Corporate Secretary, Glenbow Museum

Cardiovascular conditions, a health risk that increases with age, was perceived by respondents as a leading component of overall health and disability costs. 53% rated heart and circulatory issues as a 1 or 2 on a scale of 1 to 5, with 1 as the most significant. In general, other issues were deemed less significant, including musculoskeletal conditions, cancer and administration costs related to the health and disability costs. Other issues mentioned by respondents as costly include respiratory ailments, dental plans, diabetes, accidents in the workplace and the health issues of family members of employees, including children.

Of concern for Ontario-based companies are actuarial changes at the Workplace Safety and Insurance Board. Only 17% of all companies affected reported that the changes and their impact are well understood and the financial impact accounted for. See Chart 7. Large companies were most likely to say they understood the issue well and had prepared for the impact (60%).

CHART 7 – ONTARIO BASED COMPANIES: HOW WELL PREPARED DO YOU BELIEVE YOUR ORGANIZATION IS REGARDING THE ACTUARIAL CHANGES AT WSIB (WORKPLACE SAFETY & INSURANCE BOARD), WHICH WILL INCREASE SURCHARGE AMOUNTS AND DECREASE REBATES IN THE CURRENT YEAR?



One third of disability claims are mental health related, according to Morneau Shepell's Paula Allen , who noted mental health disability claims are approximately a third more costly than physical health claims, and are more likely to become long term disability claims, which also are significant cost drivers. Another significant one is musculoskeletal conditions, which is almost exclusively related to the age of the workforce. The ageing workforce trend is accompanied by another twist which affects costs related to long term disability. While in the past long term disability benefits ceased to be available to employees when they turn 65, retirement is no longer mandatory at age 65.

Workers' compensation is another area where there is a trend. In Quebec, the Commission de la santé et de la sécurité du travail has since 1996 had an expanded definition of mental injury to include cumulative stress. B.C. and Alberta also have that expanded definition.[7] Claimants can now get workers' compensation benefits as a result of cumulative stress arising during the course of work, not just traumatic stress. Virtually every other province in Canada is also looking at an expanded definition.

> "Every province is increasing cost projections simply as a result of the ageing workforce, because injury is something that's most aligned with advanced age, not in terms of the prevalence, but the longer recovery time. We can expect after years of decreasing workers' compensation costs, these two drivers will start to get increased costs in the near future."
>
> **Paula Allen – Morneau Shepell**

[7] Stressed out B.C. workers to get expanded benefits. CBC.ca, Nov. 4, 2011.

PENSIONS

> "There's a lot of cost associated with pensions. They sit in that sweet spot of cost, risk and talent management. It makes sense to think about your objectives, not only from a cost management perspective but in terms of retirement income and supporting some of your broader objectives, engagement and retention."
>
> **Nigel Branker – Partner and Actuary, Pension consulting practice, Morneau Shepell**

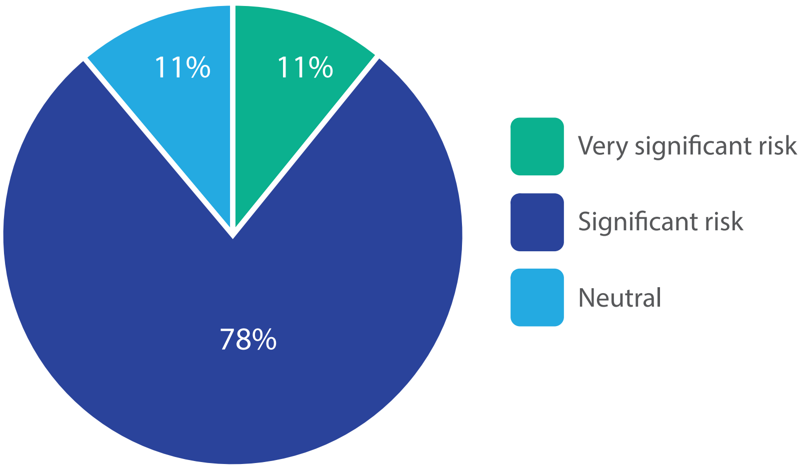
Pensions are an area that at least some employers seem to have in hand, relative to other issues addressed in this study. Pensions, as has been noted previously in this report, were considered by 34% of survey respondents to pose a risk or significant risk to the organization. When respondents were asked how well they believe their organization manages the full fiduciary responsibilities of its pension plans, two-thirds said the responsibility is well understood and fully addressed. A significant minority said the issue is well understood but not fully addressed (19%). A smaller group (13%) said the issue is not well understood but actions are underway to increase awareness nonetheless. The remainder said the issue is not well understood.

Half of survey respondents offered a defined contribution plan (47%) and 28% did not offer a pension plan at all. "We are currently not contributing to a pension or RRSP plan," said Suzanne Bedford, SVP, Finance & Operations, Colliers International. "We did have a contributory RRSP plan up to 2008. The recession hit and Colliers has not yet reinstated that contribution. Currently, we are at a key defining point in our employee benefits strategy in looking at how we fund either an employee RRSP or pension contribution. It is a critical satisfaction factor we are finding in surveys and through interviewing staff. … The younger generation, possibly don't care as much about their pensions just yet. But with the average age of our existing workforce at around 42, people are planning for their retirement and are asking 'What is the company doing about my pension strategy?'"

Only 15% offered defined benefit pension plans, and 7% offered both DB and DC plans. 2% used to offer a pension plan but no longer do. Those companies currently supporting retirees (about two-thirds of the full group of respondents) said 59% offered a defined contribution plan, 26% a DB plan, and 15% both plans. The vast majority of respondents said they planned to continue their pension plans during the next two years.

Not surprisingly, large companies with revenues of more than $1 billion were more likely to offer defined benefit plans (50%) and less likely to offer defined contribution plans (20%) than the group overall. Large companies were also more likely to offer a defined benefit pension plan to current retirees (67%). None of the large companies planned to discontinue their pension plans in the next two years. Given that so many large companies have defined benefit pension plans, it is also not surprising that 78% of them rated pensions as a "significant risk" and an additional 11% said they were a "very significant risk". See Chart 8.

CHART 8 – RATE THE LEVEL OF SIGNIFICANCE OF PENSION COST RISKS FOR THE NEXT 5 YEARS:[8]



"We have two types of pension plans. There are still a significant number of employees in the defined benefit plan; retirees or people with more experience, getting closer to retirement. We shouldn't forget that a lot of plans are underfunded and the impact it has for our employees. Regarding the DC plan, we're surprised that despite offering all these investment vehicles, a lot of employees are in the default plan because they haven't made a choice on asset allocation. Education is important. We are offering yearly seminars on the DC plan where we have our service provider with a booth in the cafeteria who can discuss asset allocation or other pension matters with the employees."

Pierre Van Gheluwe – Treasurer, Yellow Media Inc.

[8] For all risk ratings for all size categories, see Appendix A

"We have an employer-matched group RRSP. This is a significant value to us from a retention perspective, as well as it's a strong selling point when recruiting. As the average age of our employees is in their mid-thirties, long term financial security becomes a high priority for them. When we do our employee engagement surveys, every year this comes in very clearly as one of the strengths of our compensation plan."

Rod Ancrum – SVP Finance, HR & CFO, Credential Financial Inc.

When asked about future plans for their pensions, nearly half of respondents said they were intending to maintain the plans indefinitely using in-house resources, while 36% said they were going to wind up the plans as soon as the funding situation improved. One in five, or 21%, said they would maintain the plans indefinitely using outsourced resources.

For those with plans that fall under collective bargaining agreements, more than half (55%) said they plan to maintain the plans as DB with negotiated improvements, and 36% said they were planning to maintain the plans as DB but were trying to negotiate cutbacks in ancillary benefits such as retirement subsidies. 9% plan to convert the plan to a target benefit plan, with fixed employer contributions.

According to Paula Allen of Morneau Shepell, corporate Canada is going through a period of change in terms of pension structures. With defined benefit plans, organizations had poor asset returns and changes in accounting standards. "We had an issue where those benefits continued to be misunderstood and undervalued by members," Allen said, noting now there is a change in whether those benefits are even going to be available to members. According to her, the shift from defined benefit to defined contribution plans is accompanied by an emerging issue in terms of potential litigation, given to the shift of responsibility onto employees and possible concerns with respect to insufficient financial education to assist those employees. In the future, she predicted a more blended approach, including target benefit plans or cost sharing.

"Demographics plays such a huge role in this. People that are on the plus side of 45, defined benefit plans are very important to them. The defined benefit plan obviously has the advantage of lower administrative costs, and the investment risks that you can take can provide better long-term value than defined contribution. The issue is the company can't be burdened with all of the risks. If this is the case, does the pendulum swing too far that everybody goes to defined contributions simply because they can't manage the risk associated with defined benefits? We need to find a balance between the two."

Laurie Tugman – Executive Chairman, Nexterra Systems

SOLUTIONS AND CURRENT APPROACHES

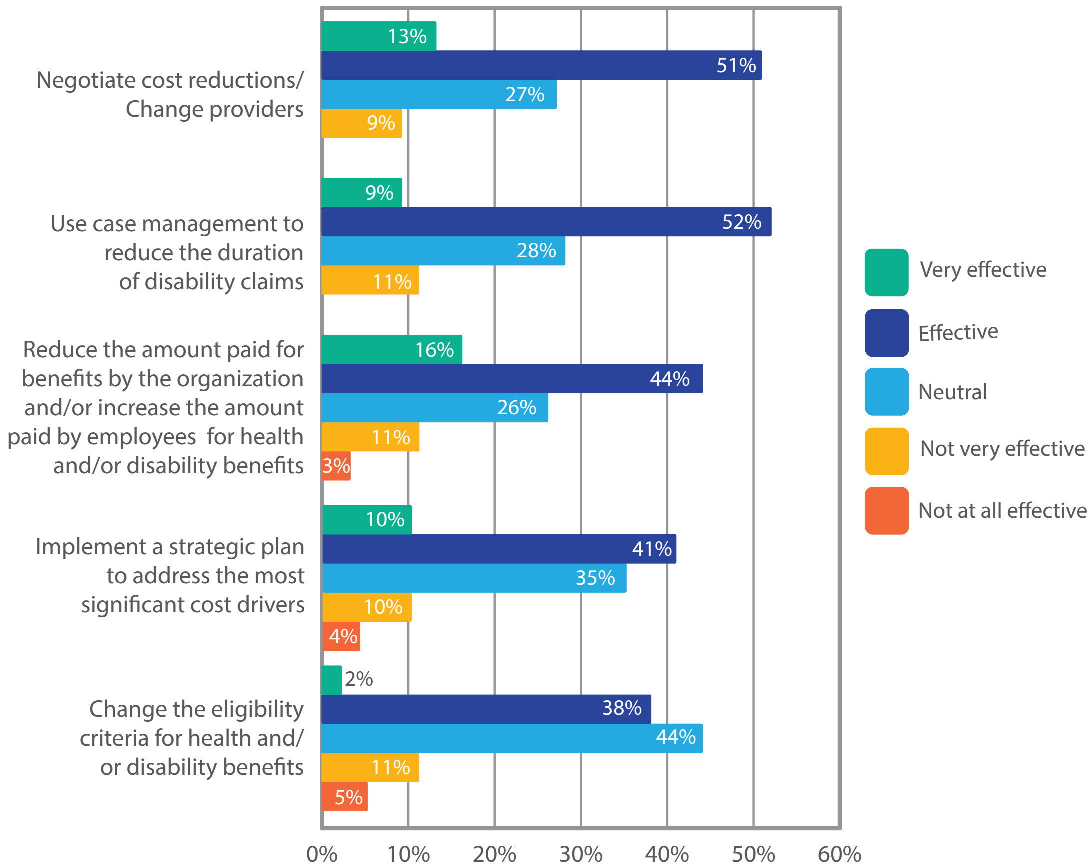
Despite the looming impact of the cost increases facing employers in the areas of drug benefits, ageing, disability plans and other health related costs, the vast majority of survey respondents have not considered a funding strategy to address the impact. Only 15% said they had done so. However, large companies were more likely to have considered the issue (40%) compared to medium-sized (12%) and small companies (12%).

> “We monitor the risk of staff turnover using a series of report cards to measure stresses in our organization. We look at actual and projected business volumes, service levels and other key metrics to identify where turnover risks may be elevated. The results help to identify where we may be short-staffed or where we are putting too much pressure on an individual group. It enables us to be more proactive.”
>
> **Rod Ancrum – SVP Finance, HR & CFO, Credential Financial Inc.**

Survey respondents have employed a range of strategies to control employee health costs. The leading tactic was to negotiate cost reductions with the health coverage provider, or change providers (deemed effective or very effective by 64%). 61% used case management to reduce the duration of disability claims, while 60% reduced the amount paid for benefits by the organization and/or increased the amount paid by employees for health and/or disability benefits. See Chart 9. Other strategies included ensuring drugs are generic when available, using a benefit consultant, emphasizing prevention and wellness in the workplace and training supervisors.

Costs related to productivity loss and absences caused by health issues were effectively managed by using case management to support a productive return to work, according to half of survey respondents. Other useful approaches included promoting an employee and family assistance plan, promoting health communications in the workplace, and implementing a strategic plan to address the significant drivers of absence and productivity loss. Also mentioned were increased vacation time, more flexibility of hours, introducing “fit for work” testing, requiring better medical documentation for absences, and offering a performance dependability bonus.

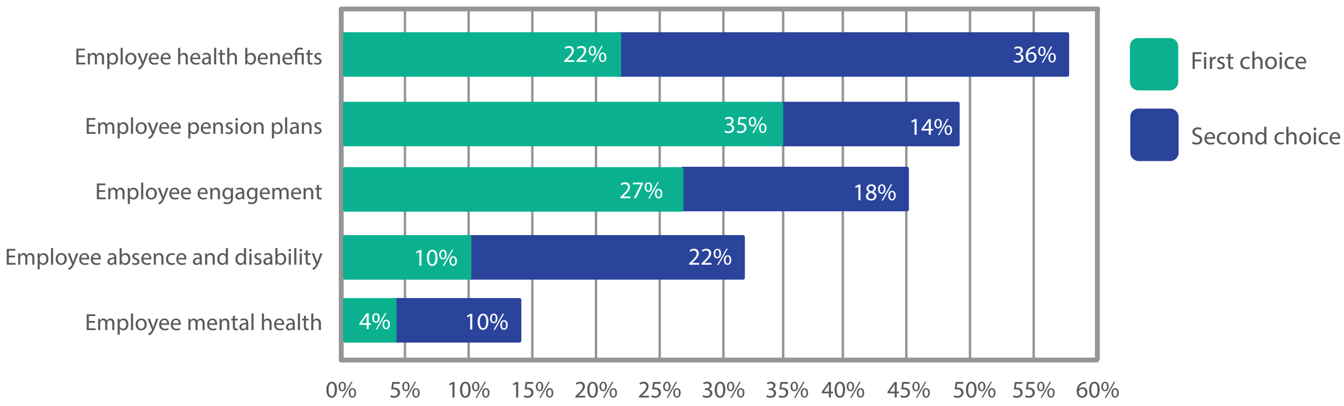
CHART 9 – WHAT ARE THE MOST EFFECTIVE APPROACHES THAT YOU HAVE IMPLEMENTED TO DATE REGARDING EMPLOYEE HEALTH COSTS?



As noted earlier in this report, health benefits were seen as an increasing cost. On page 10, Chart 3 shows that health benefits costs were deemed of greatest concern to most respondents and 62% ranked this issue as 1 or 2 on a scale of one to five, with 1 being most significant. However, companies also saw their strategic planning and cost management as being strong in this area with 58% rating the issue a 1 or 2, with 1 being a strong area for the company. See Chart 10.

Organizations surveyed presented a variety of perspectives on their confidence and ability to manage their pension plan. For instance, 60% of large organizations said their strategic planning and cost management is strongest in the area of pensions, while only a minority of medium-sized companies (36%) and small companies (29%) said pensions were their strongest area when it came to strategic planning and cost management. In fact, only 10% of large companies said pensions were their weakest area, compared to medium-sized companies (36%) and small companies (35%).

CHART 10 – WHICH AREA DO YOU FEEL YOUR STRATEGIC PLANNING AND COST MANAGEMENT IS THE STRONGEST?



> “In the past two years, with our focus on employee benefits and taking care of employee mental health, we have certainly seen reductions in absenteeism. . . . What we're trying to do is look at what is going to drive down absenteeism and increase employee engagement in the workforce.”
>
> **Suzanne Bedford – SVP, Finance and Operations, Colliers International**

"Absenteeism is very low for people in client-facing and non client-facing roles. Our non client-facing teams have created mission statements that include a definition about who their customer is. They embrace that their customer is the person that's actually servicing our customer, and so it's very important that they are available to serve their internal customers so that our clients are well served."

Stephen Massel – CFO, Hotspex

When asked about approaches to manage emerging cost risks, most survey respondents said new strategies are required to improve employee health and self-management (57%), while 37% said new strategies are required to share the accountability of cost and health with employees. One in four (24%) said new strategies are required in financial planning and funding. Only 12% said current strategies are the most effective approaches for managing emerging cost risks.

One potential cost management strategy proposed to survey respondents was reducing the number of vendors related to health service and administration. 42% of survey respondents said this move would offer high or good value, to either increase efficiency and accountability or to reduce time spent on vendor management. One in four said reducing vendors would offer only a moderate value, with inconsistent benefits, and 12% were not interested in the idea.

While analytic tools can be useful for projecting costs, 12% said they did not have any analytic tools to help them with projecting costs, planning or tracking. An additional 3% said their tools were insufficient, while an additional 12% said their tools provided an understanding of current cost drivers, but lacked projection.

On the upside, about half (47%) of those surveyed said they had tools to provide either a comprehensive or at least reasonable understanding of current and projected cost drivers, with enough details to support some planning and tracking. However, one in four (26%) said their analytic tools provided only a basic level of understanding of current and projected cost drivers, and lacked enough details to support effective planning and tracking.

"We rely on the HR function to provide us with details around health and safety, attendance, turnover, recruitment and the demographic age profile of the company. We're investing to automate a lot of those processes. It's a manual exercise today but we are looking to automate those HR processes and to integrate them into our financial planning process."

Roger Rees – CFO, SCI Group

Case study in tracking, technology and incentives

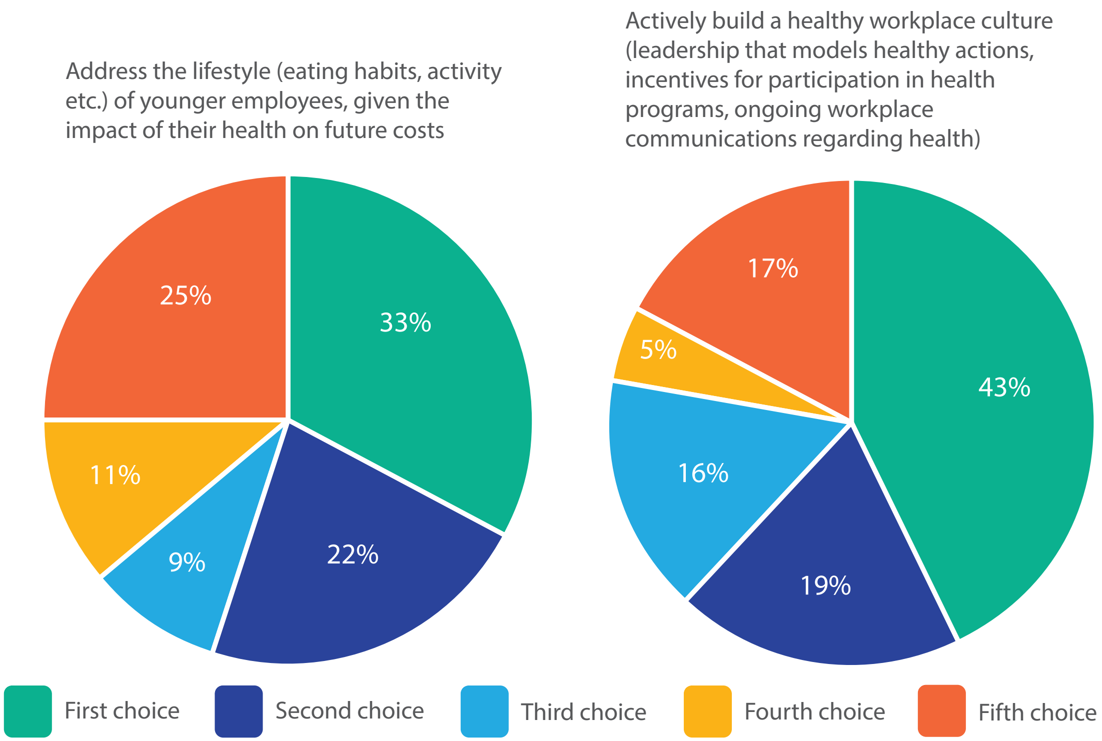
We track turnover and safety in different ways. We track our statistics for safety, available positions, turnover, and we put it all on a dashboard. It's a great program. Your manager or GM pops up their dashboard, they see the turnover statistics, year to date and month to date. They see their open requisitions that they've got to fill. They see both personal and business information and that's been a really good program for us to make it visible. Specifically with absenteeism, we've had a couple of instances where it has become a major problem for us. In one location, we had about 6-8% a day, with about 200 employees, so this is a pretty big deal. We put in a productivity premium program. And we reduced the cycle times of the rewards that we provided to the employees. Then we made the statistics visible. This took our absenteeism down from 6-8% to less than 1%. Turnover was dramatically reduced, and we still continue to see benefits from that. The two things that made it worthwhile was making it visible and getting it on a short term 30-day cycle. That made all the difference in the world. The benefit translates to about $2.00 an hour, and we split payment. For example, if February hits the productivity premium, on March 15th everybody will get a dollar per hour on their paycheck and then the other dollar gets banked and paid, at December 15. We pay right before our Christmas holidays. And it's been a fantastic program for us. It's been a big investment, but the investment looks very minimal now in comparison to what we're saving on turnover.

Kirk Duffee – SVP, Lodging Services, Clean Harbors

TECHNOLOGY

64% of survey respondents said technology could be used to support employee health and engagement. They said it could play either an important role, offer credible information and build awareness or a fairly valuable role, much in the same way technology is used for other workplace initiatives. One in four (23%) said technology could play a central role to manage personal health information, organize resources, guide action and provide programming. Only 1% said technology plays a negligible role, with not much potential to have an impact on health.

CHART 11 – WHAT DO YOU THINK WILL SUPPORT IMPROVED HEALTH FOR EMPLOYEES AND REDUCED HEALTH COST FOR ORGANIZATIONS?



EMPLOYEES

Most survey respondents said the best way to support improved health for employees and reduce health costs for the organization is to actively build a healthy workplace culture (leadership that models health actions, incentives for participation in health programs, and ongoing workplace communications regarding health). See Chart 11. "We offer every employee up to $750 a year for a health club membership. The pickup rate on that is very low, but we're trying to encourage more of that," said Stephen Massel, CFO of Hotspex.

ROLE OF MANAGEMENT

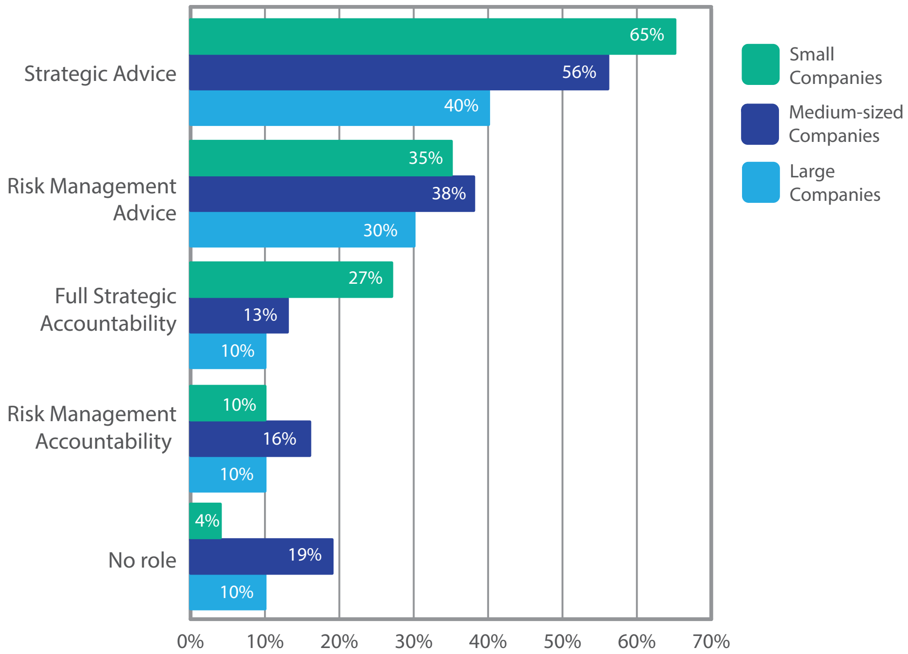
A full understanding of HR issues is important for CFOs and other business leaders, given that a sizeable number are responsible for these areas of concern. For instance, nearly four in ten (38%) of financial executives surveyed by CFERF said they were accountable for HR in the reporting structure of their organization. HR was the third most common area of accountability for CFOs, outranked only by the leading responsibility of finance (95% of respondents) and information technology, or IT (47%). In addition, 59% of respondents said they guide decisions related to strategic human resource management issues, 34% said they monitor results of HR management issues and take action as needed, and 19% said they actually make the decisions. (15% said they had no role and 11% said they select the decision maker and review decisions.)

Financial executives at smaller companies have a far greater likelihood of being involved in making decisions around HR management issues than at larger companies. 60% of survey respondents at large companies said they had no role, while 30% said they guided the decisions. 56% of financial executives at medium-sized companies said they guided the decisions, while 65% of respondents at small companies guided the decisions. See Chart 12.

“The human resources department reports to me. Staff costs including salaries, benefits and training are our biggest expense. It creates a good balance to have HR working closely with the finance team as it gives everyone a better understanding of the cost implications of decisions, benefit programs and of the competitiveness of our salaries. We have much better insight into this than we did before. Because HR’s primary responsibility is employee engagement, it can sometimes contradict with finance’s goals of managing costs and driving profitability. This reporting relationship allows both HR and Finance to better understand each other and to push back so that the right balance between the needs of both the employees and the company are met.”

Rod Ancrum – SVP Finance, HR & CFO, Credential Financial Inc.

CHART 12 – WHAT DO YOU BELIEVE YOUR ROLE SHOULD BE RELATIVE TO STRATEGIC HUMAN RESOURCE MANAGEMENT ISSUES?



Financial executives should be in the position of offering strategic advice, according to 46% of respondents, while 18% said financial executives should hold full strategic accountability for strategic human resource management issues. 15% said financial executives should have risk management accountability and 19% said the role should be limited to giving risk management advice. Only 2% said financial executives should have no role, either in the area of offering advice or being accountable.

Senior managers have a role to play in modeling health lifestyle choices, according to some respondents. Several agreed that managers need to lead by example, and should be role models for a health organization. "The challenge is making it enough of a priority. Other issues are more urgent," wrote one respondent.

CONCLUSION

> "The role of the CFO is to assess the risks that lie ahead for the organization. For an understanding of these risks, the CFO has to be very closely aligned with HR."
>
> **Roger Rees – CFO, SCI Group**

Given that four in ten (38%) financial executives surveyed said they were accountable for HR in the reporting structure of their organization, it is clear that financial executives have a role to play in working with HR to predict and control costs. HR is currently the third highest ranked responsibility of the executives, outranked only by finance and IT. In addition, most of respondents said they guide decisions related to strategic human resource management issues, about one in three said they monitor results of HR management issues and take action as needed, and one in five said they actually make the decisions. Financial managers can provide support by helping HR managers introduce and use measurement and tracking tools, to be used in conjunction with the finance department. These can track usage, predict trends, note unusual patterns (or potential abuse) and help the organization prepare for future cost demands.

> "We have done a number of things to bring focus to productivity. Each employee has personal objectives that are measurable and that directly align to our divisional and corporate strategies. We use a series of scorecards to manage and monitor our progress. We have implemented new systems in order to track information better, such as absenteeism and the reasons for it. The HR team is now embedded into our divisions and deal directly with front line management. They're in day-to-day conversations and getting the feel for what's happening in different parts of our organization."
>
> **Rod Ancrum – SVP Finance, HR & CFO, Credential Financial Inc.**

In order to address the perfect storm of factors, CFOs will have to pay closer attention to the following factors:

- The increasing availability of sophisticated and expensive medications. Employers can seek advice from external sources to ensure non-health related spending is kept to a minimum e.g. Ensuring generics are provided rather than brand name medications; that prescriptions are not filled before they are needed; encouraging the use of cheaper medications which are just as effective as expensive new ones.
- The demographic issues of an ageing workforce with expanding health needs. Employers can model healthy habits, offer incentives to help employees stay healthy with gym memberships, and ensure the workplace is both physically safe and fosters a nurturing environment for staff.
- The risk around prolonged absenteeism related to mental health. Employers can follow the new voluntary standard which promotes mental health in the workplace.

CONCLUSION

- To avoid liability, Employers should direct employee health concerns to a third party or consultant, to protect employee privacy and avoid concerns around discrimination. For instance, employees cannot be accused of discriminating against an employee for health reasons if they are not aware of the issue.
- Pension liability associated with the risk of moving from defined benefit to defined contribution plans, (which transfer the risk of asset allocation and investment choices to individual employees): Employers can choose alternative models such as target benefit plans. These are essentially defined contribution plans but the asset allocation evolves with the age of the employee, moving from high risk/higher return investments to lower risk/lower return investments as the employee ages.

It's clear everyone associated with an organization has a role to play in improving and maintaining employee health, and ultimately productivity:

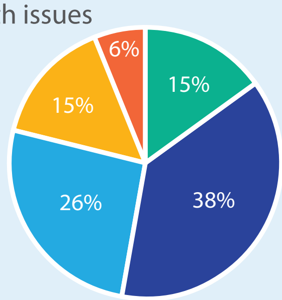
- It starts at the top, with leaders modelling healthy behavior, both physical and mental. It includes finance and HR, working cooperatively and as a team, to forecast, predict, model and manage costs while at the same time fostering and preserving employee engagement.
- It includes middle manager and supervisors who work on the front lines and can be the first to notice red flags in employee behaviour which may require intervention, both for employee health and safety but for other staff, as well as to reduce risk to the organization.
- And finally, responsibility rests with employees themselves, to maintain their own health and a healthy lifestyle, to not abuse benefit plans, to use medications responsibly and as directed, to work effectively and collaborate with others in a bully-free environment, to take an interest in their retirement, educate themselves and to ask for help when they need it.

This multi-faceted, multi-pronged approach, with all levels of a company working in tandem, fosters the health of not only employees but of the entire organization, which in turn benefits everyone.

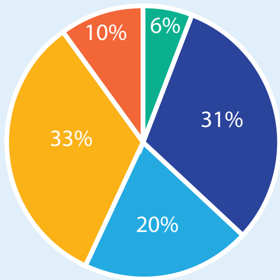
APPENDIX A: EMPLOYEE COST RISKS IN THE NEXT 5 YEARS

SMALL COMPANIES (REVENUES OF UNDER $99 MILLION)

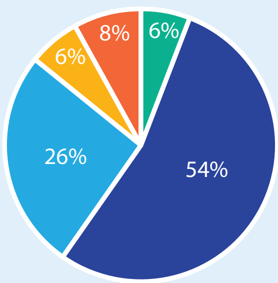
Stress and mental health issues



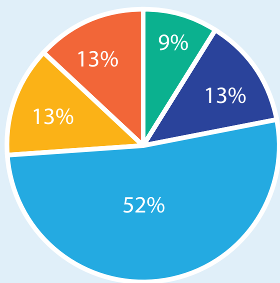
Chronic health issues



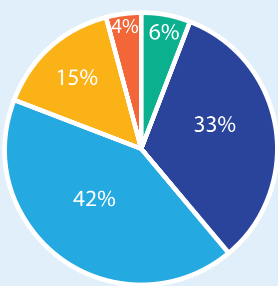
Drug plan costs



Pensions



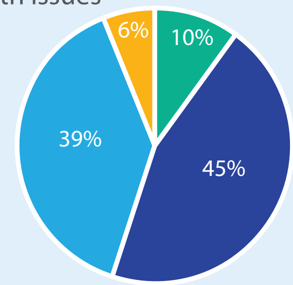
Absence and disability



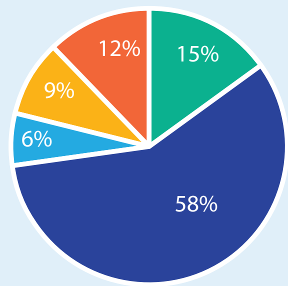
- Very significant risk
- Significant risk
- Neutral
- Not very significant risk
- Not significant risk

MEDIUM-SIZED COMPANIES (REVENUES OF $100-$999 MILLION)

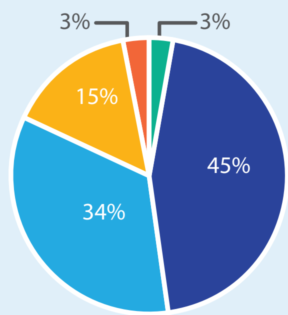
Stress and mental health issues



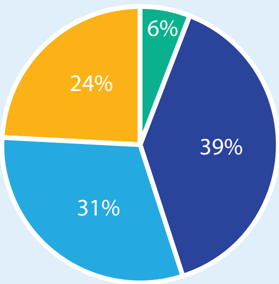
Drug plan costs



Absence and disability



Chronic health issues



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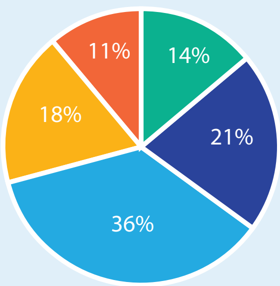
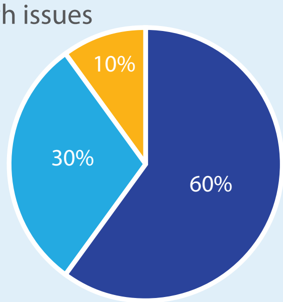
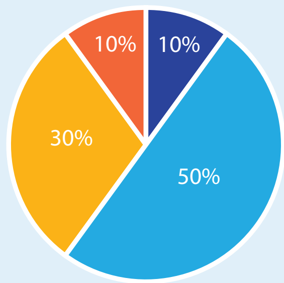


LARGE COMPANIES (REVENUES OF $1 BILLION OR MORE)

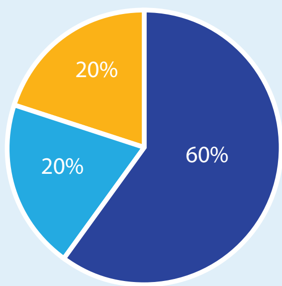
Stress and mental health issues



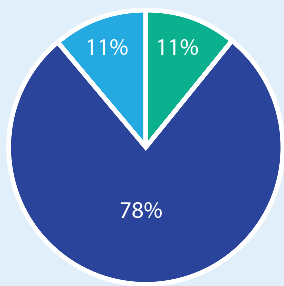
Chronic health issues



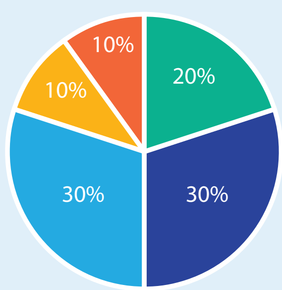
Drug plan costs



Pensions

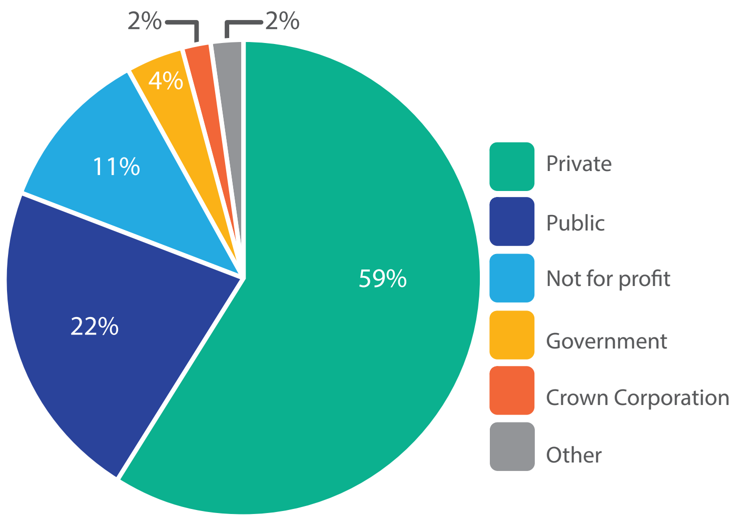


Absence and disability

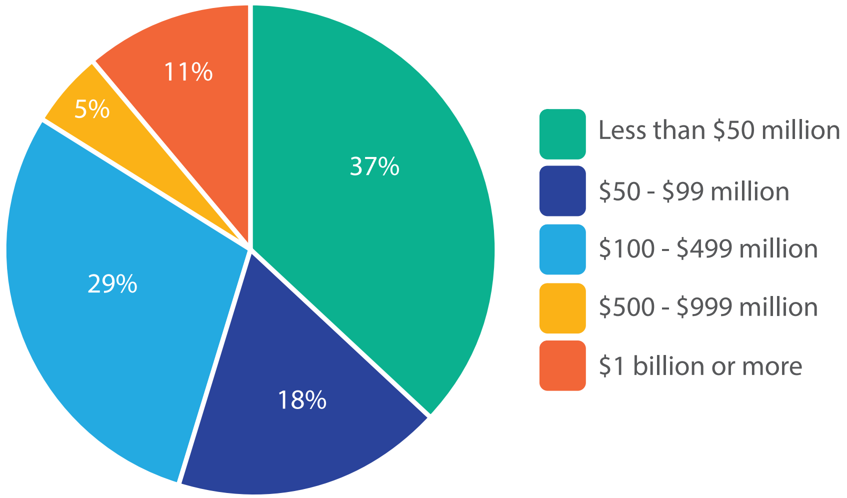


APPENDIX B: DEMOGRAPHICS

CORPORATE STRUCTURE

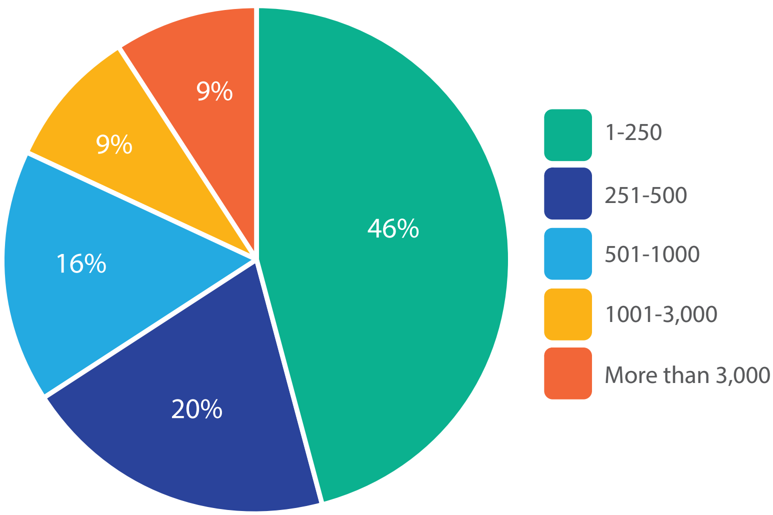


ANNUAL REVENUE

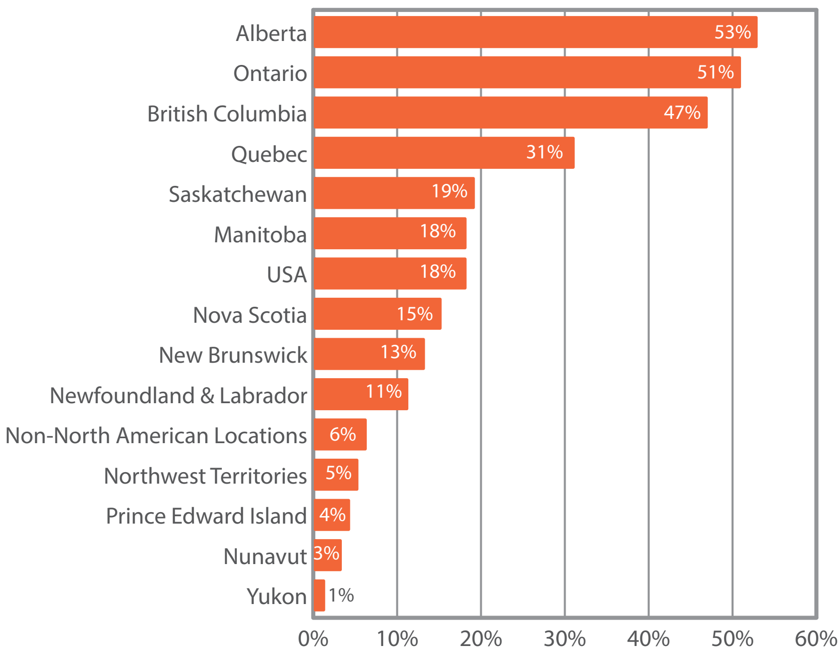


APPENDIX B: DEMOGRAPHICS

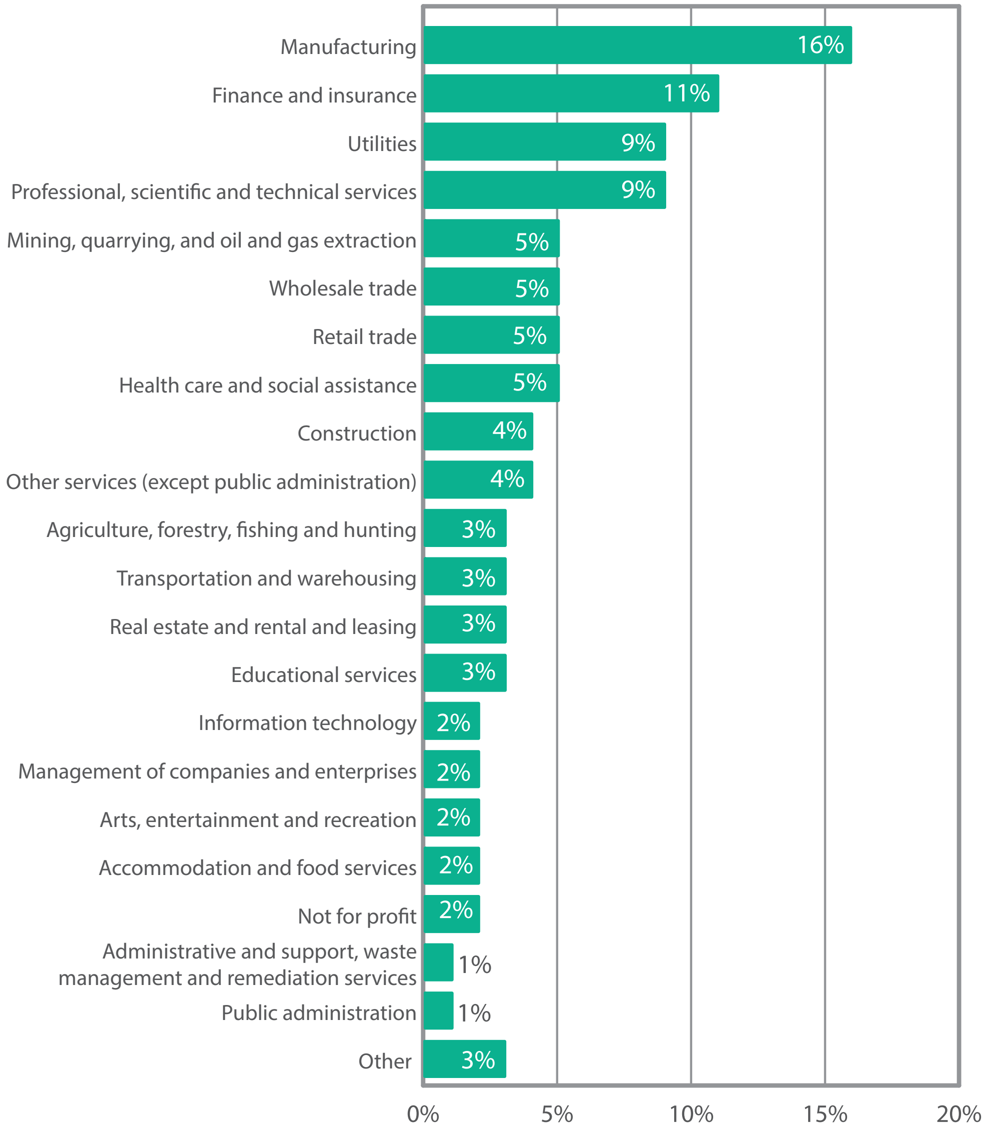
EMPLOYEES



LOCATION



INDUSTRY CLASSIFICATION



APPENDIX C: FORUM PARTICIPANTS

Forum Chair:	Michael Conway – Chief Executive & National President, FEI Canada
Moderators:	Christian Bellavance – VP, Research & Communications, FEI Canada Paula Allen – VP Research and Integrative Solutions, Morneau Shepell
Vancouver Participants:	Rod Ancrum – SVP Finance, HR & CFO, Credential Financial Inc. Suzanne Bedford – SVP, Finance & Operations, Colliers International Laurie Tugman – Executive Chairman, Nexterra Systems
Calgary Participants:	Wayne Braun – CFO & Corporate Secretary, Glenbow Museum Bill Cromb – VP Finance, Synchronicity Energy Trust Kirk Duffee – SVP, Lodging Services, Clean Harbors
Toronto Participants:	Alysia Carter – CFO, Ainsworth Stephen Massel – CFO, Hotspex Ajay Rao – CFO, Conros Corporation Roger Rees – CFO, SCI Group Jane Voll – Senior Representative, Bank of Canada Nigel Branker – Partner & Actuary, Pension consulting practice, Morneau Shepell
Montreal Participants:	Étienne Berlinguet – VP, Finances – Operations, Intact Financial Corporation Pierre Van Gheluwe – Treasurer, Yellow Media Inc.
Observers:	Laura Bobak – Senior Writer, FEI Canada Melissa Gibson – Communications & Research Manager, FEI Canada

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PotashCorp

FEI CANADA'S RESEARCH TEAM:

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Christian Bellavance – Vice President, Research & Communications

Laura Bobak – Senior Writer

Melissa Gibson – Communications & Research Manager

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