

# **The Design of a Fringe Benefit Costing Program** **L'évaluation du coût d'un programme d'avantages sociaux**

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Article abstract

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# The Desing of a Fringe Benefit Costing Program

**Brock D. Macdonald**

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## INTRODUCTION

On May 31, 1972, the Employers' Council of British Columbia put on a one-day seminar in Vancouver on the subject of settlement reporting and costing. As part of his presentation, Mr. Felix Quinet then suggested a national costing seminar in the interests of standardizing terminology and sharing methodology. Indeed, as Mr. Quinet then pointed out, the phenomenon of « isolated competence », to use his own expression, has made it quite difficult to arrive at a standardized way of analyzing and communicating costs of collective agreements and settlements. This is the problem of variety in both method and language, where research practitioners, working in relative isolation from one and other, have each developed and refined their individual costing programs. The result is that there are many different approaches to the measurement of wages and fringe benefits and each approach has its own peculiar nomenclature and definitions.

Yet, as Mr. Quinet emphasized, the thoroughness and precision of each of these isolated systems is not to be questioned ; each is useful and accurate in its own right. Rather it is the lack of a common language and uniform methodology that makes communication of social and economic data between industries and from one part of the country to another so very difficult.

This variety in terminology, analytical method, and level of complexity was evident among a small group of large companies and employers' associations whose researchers have met together over the past four years in Research Subcommittee at the Employer's Council of British Columbia. We set out in 1969 to reach agreement on a standardized settlement reporting program from which we could all share information about wage and fringe benefit costs arising out of settlements.

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Although we made several bold attempts to gain the necessary acceptance of the majority of member companies, we met with frustration each time. There were major differences in company payroll system, there were problems of information security, and even among our small committee there were differences in terminology requiring complicated definitions. As a result we were unable to create a settlement cost reporting system that was of value to all member companies and associations, many of whom already had established research programs of their own.

The big problem was with semantics. The copious definitions that accompanied our trial survey forms just never seemed sufficient and I am sure they turned off other members completely about the values of the reporting system. There was also the problem that comparatively few members were able to provide the information in the standardized form that we required — many just didn't have payroll information readily available in the form we wanted.

We also discovered that many of the smaller members had not developed a labour relations research capability. It is most difficult for these smaller companies, which lack comprehensive labour relations resources, to run off the required statistics from their payroll systems. Only a minority of member companies have the advantage of computerized payroll and even some of these must contend with limitations on information availability due to the design of their payroll system.

When the Mediation Commission and B.C. Department of Labour began to meet our information needs with useful and timely settlement reports and fringe benefit surveys, the Research Subcommittee decided to defer the standardized settlement reporting project. However, it must be pointed out that much was gained from that experience: our various methods were shared, use of fringe benefit costing among smaller companies was promoted, and a degree of standardization of terminology was attained, as reflected by the reporting of settlements in the *Industrial Relations Bulletin*, a weekly publication of the Employers' Council of British Columbia.

Although our Research Advisory Subcommittee continues to meet today on matters other than standardized fringe benefit costing, at least we now know how we differ. We know that the terms «burden», «creep», «impact» and «secondary loading» generally have the same meaning in our respective costing systems, even though the effects of «isolated competence» are perpetuated.

When one thinks about a number of fringe benefit costing systems in use today in British Columbia, it seems that they have evolved over a period of time, almost on the basis of trial and error, until working definitions become familiar to everyone and until the form of the output data is tailored to the needs of the users (or the users learn how to best

apply the information available). Now again, this is not to find fault with these systems, most of which are highly sophisticated and innovative in their own settings. However, it is the evolutionary process that is often awkward and time consuming — working out the bugs until the fringe benefit costing data is eventually accurate, timely and understandable to users. After going through such growing pains, there is an understandable resistance to making major changes in terminology and format for the sole purpose of standardization of industry or national statistics. Such reluctance to change is thought to have been one further reason why we at the Employers' Council were unable to sell a uniform settlement reporting and costing system to all members.

Even when a company adopts a program used elsewhere, there will be problems of integration with other internal accounting programs, and after that, earning the confidence of those who eventually must use the output information.

One notable example of an uphill struggle to gain confidence comes to mind. When the B.C. Mediation Commission was first set up in 1968 they employed as Research Director, Gordon Cooper, a very capable operations researcher who was formerly with the C.N.R. He was asked by the Commissioners to create a comprehensive settlement costing program, including fringe benefit costing. After many months of deep thought, painful programming and consultation with eventual users including the Employers' Council, Cooper evolved an elaborate and flexible wage and fringe benefit costing system. But even after these development pains there was the enormous task of selling his product to mediators, industry and labour. Labour's outspoken rejection of the whole Mediation Commission concept made his task almost impossible. When the Commission was dissolved by the NDP Government last fall, this valuable program was accepted and used by only a minority of larger companies and employers' associations. Only a few labour unions had put aside their prejudices long enough to realize the great value of Cooper's work. Unfortunately there was not a large enough following to support continuation of the program and most regrettably it died with the Mediation Commission.

However, it is believed here that the problems of variety, growth and acceptance can be greatly eased if we can only stop for a moment to form a practical philosophy about fringe benefit costing. Are there some guiding principles for determining the design of a fringe benefit costing program? What are the limitations on the level of complexity? Let us examine the practical utility of several types of fringe benefit costing and attempt to draw out some useful criteria for design.

#### THE PRACTICAL UTILITY OF SEVERAL TYPES OF FRINGE BENEFIT COSTING

The concern here is with more than the mere selection of an appropriate costing method. Indeed reference is made to « design » of a

fringe benefit costing system, in the broader sense that good design will justify the performance of research in whatever form it must take to meet a specific requirement for information. Thus, design criteria should answer such basic questions as :

Why do the research in the first place ?

Why cost benefits ?

Why spend all that money on sophistication ?

What form should the output take ?

How will the output be used, at what level, and for what purpose ?

Answers to these questions should be helpful to those who want to start up a program of fringe benefit costing, and, as well, might be useful to evaluate programs already in effect.

Fringe benefit costing are seen here as a specialized information system. By this it is meant that it is a communications tool — involving collection, storage, retrieval, analysis and dissemination of information about labour cost. As an information system, fringe benefit costing will be most effective if it is used to retrieve specific and pertinent information quickly and put it into a simple, clear form which gets the message across with impact ! The general and practical utility of a fringe benefit costing program is its capacity to meet a specific information need.

There are at least three levels of information demand on a fringe benefit costing program and review is made of what is thought unique about the first two of these three levels which have been of the greatest concern to this writer over the past few years in his work with B.C. Hydro. For purposes of illustration, some examples of fringe benefit costing programs presently in use in British Columbia are described. The three levels of information need are :

1. Requirements for information within the organization — for planning and control and for formulating labour relations strategies.
2. Requirements for information for use in collective bargaining at the bargaining table.
3. Requirements for information which arise outside the organization — in the industry, among unions and companies and in government.

(I merely mention this need to distinguish it from the other two areas. It has many interesting technical considerations of its own which must be dealt with by others far more qualified than I.)

#### **Inside Information Requirements**

Information needs within the organization represent the greatest demands on the fringe benefit program ; in fact its scope and complexity

will be determined by the diversity of internal information needs. These requirements can generally be divided into three main classes :

1. *Comparative measurement* : — « How do our fringe benefits compare with those offered by the remainder of the industry or in the overall employment community ? »
2. *Performance information* : — In negotiations, « What are the differences in our positions and how much have we given away up to this point ? » As cost control, « What is the actual cost experience under our income protection plans ? »
3. *Predictive costing* : — « What will the future cost of changes be ? What are the long range costs of bargaining alternatives ? »

It is likely that the central motive for developing fringe benefit costing in the first place arises out of the need to answer these internal questions. Thus inside information requirements rank high in priority as system design criteria.

The most important single demand for information internally comes from senior management. For example, the directors want some quantitative description of a settlement, a question that is characteristically asked immediately after the settlement has been made. Normally it calls for a fast answer in the simplest possible terms — they don't want the details — eg : « wages  $x\%$  + fringes  $y\%$  =  $z\%$  total cost increase each year of a two year agreement. » But even this kind of statement can only be made after careful analysis of fringe benefit changes. In its bare simplicity it is ambiguous and may even lead to dangerous conclusions of pronouncements by a senior manager who doesn't understand the method of computation. Add further definition — or example, a footnote stating, « Percentages are expressed as time-weighted annual compound averages » — then the statement is no longer simple. It is therefore essential to work out the necessary costing conventions beforehand so that senior management will understand the language used and will thereby be able to back up any « quickie » comments to the press with fullest confidence.

The speed with which the information is prepared accurately is another important design consideration. Not only the directors, but also the labour relations strategy planners, require cost data very quickly. For example, when the union submits its agenda at the opening of negotiations there is an immediate demand for a cost analysis. This means that basic costing data must have already been assembled ; in fact, some of the demands may have been pre-costed in anticipation. The forest industry in B.C. has developed this particular resource into a real art ; they are able to run out an accurate cost summary of the union's numerous requests within hours of receiving them.

During negotiations the internal information needs of the organization will increase both in number and complexity. Negotiators must assess

differences in positions and they will require predictive cost analysis of possible bargaining alternatives. Again there is a requirement for effective timing — getting the results to the users while the iron is hot !

The fringe benefit program must be designed to withstand these time pressures if it is to be useful to bargaining strategists, particularly in the peak pressure period that precedes settlement. It is then that the negotiators want running estimates of the « gap » between the parties' respective positions. Accurate assesment of package costs can only be based on predictive costing techniques that have been tried and tested for validity well in advance of this peak demand period. If the cost information produced is going to affect strategy decisions during the final stages of bargaining, then the costing methods must be understood and acceptable to the decision makers long before the eleventh hour !

Just to illustrate the time pressure demand, let us recall an instance where B.C. Hydro negotiators were meeting with the Amalgamated Transit Union bargaining committee in a Vancouver hotel room. It was the final hour in an attempt to reach agreement, short of compulsion, and city transit workers were entering their fifth week of a strike that had completely shut down the public transportation system. In a separate room across the hallway the research staff cranked out cost analyses of the changing positions as the negotiators tried desperately to juggle the terms for settlement into some acceptable package that the union committee could sell to its members. This rather dramatic example shows how important decisions can be based on cost data estimated on the spot. In that instance a deal was made within the cost limits that was later accepted by the striking operators only by a narrow vote.

Unfortunately most fringe benefit costing programs are preoccupied with the short-term cost effect of changes — « over the life of the agreement ». There is far too little work done in determining the long range cost implications of changes. However, with the increasing demand for non-wage improvements, particularly in the welfare and hours of work areas, the attention of costing research is now reaching out beyond the expiry date of the collective agreement to consider cost implications of changes over the longer term.

One example is the banking of overtime premiums to be taken as time off in the future :

- What if time is taken off at a higher wage rate ?
- What if it is banked towards early retirement, to be paid at future rates and conditions ?
- What are the benefits of retiring older workers early and replacing them with low seniority, productive younger men ?
- What effects will future reductions to the work week have on the future cost of banked overtime ?

Another example is the cost implications of adding a dental insurance scheme to the welfare package :

- What future costs might arise out of experience rating of premiums ? (Are you being « lowballed » into a potentially expensive plan by initial premium quotations ?)
- What are the future cost implications of premium sharing ?
- What are the long-range cost implications of joint control ?

These longer range cost analyses will require special resources and sophisticated techniques such as cost/benefit analyses and actuarial forecasting which are not normally employed by smaller organizations. Perhaps the requirement for this kind of research is better satisfied on a shared basis through industry and employers' associations and labour federations. Certainly the capability for this type of fringe benefit research is an important consideration in the design of a new program or in the evaluation of an established research facility.

Earlier innovative costing programs designed to meet internal information needs were mentioned. A notable example is a fringe benefit costing program that was developed by MacMillan Bloedel Limited, the largest company in British Columbia's forest industry. Using a computer they have developed the capability of listing component fringe benefit costs for any group of employees, and these costs are based on actual payroll experience over any selected sample period. These costs are represented in hourly terms as cents per hour of time worked and they therefore provide an extremely useful breakdown of productive labour costs that reflects actual performance. From this valuable information they can accurately predict costs that will likely result from negotiated changes — and then later test the validity of those predictions against actual costs performance.

There is one further innovation to the MacMillan Bloedel fringe benefit costing program. Because their forest products are marketed internationally, they are most concerned about the effects on their product prices of any negotiated changes. To meet this special information need they have developed a program for forecasting the increased labour cost of a fringe benefit or wage improvement for employees engaged in the production of any particular product line — for example, partial board, shingles, plywood, or raw pulp.

Often internal information needs will require special programs which test the ingenuity of those who design fringe benefit costing systems. It is interesting that the MacMillan Bloedel program was created shortly after they learned of a similar program developed by Cominco for the Mining Association of B.C. This is a good example of how the Employers' Council Research Subcommittee led to a significant sharing of methodology.



### Information Needs for Bargaining

The second level of information need that was referred to earlier is the requirement for fringe benefit costing information for specific use at the bargaining table

To demonstrate home thoughts about using fringe benefit costing information in actual negotiations, please allow the author to draw on his own experience at B.C. Hydro and to describe the recent negotiations with the Amalgamated Transit Workers.

Following the strike and eventual settlement referred to earlier, the Amalgamated Transit Workers in Vancouver elected a full slate of new officers. During the months prior to the next round of negotiations, there were a number of occasions when the new officers demonstrated a militant attitude towards B.C. Hydro management, both in domestic labour relations and in the press. When the negotiations began again in the fall of 1972 the business agent aggressively handed down the most farreaching set of demands ever received by Hydro, from any of its unions. He sternly emphasized at the same time that his committee represented the militant younger employees on the transit system who demanded action at any cost. This aggressive and suspicious attitude persisted throughout the initial meeting and the possibility of ever reaching agreement through direct bargaining seemed remote indeed.

Hydro had used fringe benefit costing extensively in the previous round of negotiations, as described earlier. Anticipating a continuation of this approach, the new union officers retained a very capable labour economist and most of their demands had been researched in some depth prior to negotiations. As the meetings proceeded, still in a difficult and untrusting climate, the union submitted several research briefs to back up their demands.

A decision was made by the Hydro negotiators to recognize this factual information submitted by the union, and to commend the union committee for their refreshing sophistication. At the same time, and without strictly refuting the union's submissions, the fringe benefit costing approach was once again introduced by Hydro.

The design was to cost the total positions of both sides, once an initial offer had been tabled by Hydro. This drew attention to the disparity of positions in an objective way that inhibited intrusion of negative attitudes and emotions. Before long the parties were engaged in meaningful bargaining, on the basis of package costs, and with a much more hopeful and constructive attitude. An agreement was reached across the table on this basis. It was costly to Hydro yet it was generally agreed by management that the union had presented a well supported factual case for specific adjustments to wages, and more particularly, for improved working conditions including hours of work and shift provisions.

As factual information was introduced, Hydro was mindful of several communications requirements which affected the nature and complexity of the fringe benefit costing used. Perhaps these requirements are obvious from a communications point of view, but nevertheless they bear repeating :

1. First the union's research efforts were accepted and encouraged rather than attacked in the customary rebuttal form — the negotiators actually admitted to the merits of some of the evidence raised, particularly on the hours of work issue.
2. A fully costed position statement was presented quite early in negotiations, placing emphasis on methodology rather than on results — which obviously showed a gigantic gap at that point ! The purpose here was to gain acceptance and understanding of methodology and language. To this end all calculations and basic data were fully disclosed to the union committee and to their economist.
3. Although many of the initial costs were estimated, greater precision was used as negotiations progressed and differences closed. This played down the importance of the union's opening demands, but more important, the union was given the fullest opportunity to examine and attack Hydro methods. Hydro accepted these arguments objectively, as offered by the union as constructive criticism. As a result, there was considerable and open discussion about methods used, and in some cases, calculations were modified according to the union's suggestion.
4. Meetings were encouraged between the « costing experts ». At one point it was arranged that the union's economist should meet privately with a consultant retained by Hydro to discuss the issue of long-term disability insurance coverage.
5. The costing method used was as simple as possible, equating fringe benefit costs to the equivalent of a general wage increase. To gain acceptance, figures were weighted to the union's advantage (showing slightly lower costs) whenever value judgments were involved.
6. In the final stages of negotiations Hydro's whole approach was to bargain an acceptable cost package and consequently there was a heavy reliance upon full costing of package positions. By that point the parties were conversant with the language and methodology of the fringe benefit costing used.

The experience of those negotiations demonstrates clearly how the use of fringe benefit costing can encourage meaningful bargaining. It is noteworthy that the new union officers agreed with these observations after the contract was signed.

In particular, they agreed that the use of mutually acceptable factual information had helped the parties to develop a climate of trust — an essential ingredient for successful collective bargaining !

## L'évaluation du coût d'un programme d'avantages sociaux

L'évaluation du coût des revendications en matière d'avantages sociaux au cours de la négociation des conventions collectives est chose complexe. Elle l'est d'autant plus que l'on ne s'entend généralement pas sur la terminologie et la méthode d'analyse qui varient d'un employeur à l'autre. Aussi les chercheurs ont-ils beaucoup de difficultés à mettre au point un système qui soit valable pour les entreprises et les associations d'employeurs, principalement celles qui possèdent déjà leur propre système de calcul.

D'une part, les petites sociétés, qui ne possèdent pas un service de relations professionnelles aguerris, ne peuvent pas facilement extraire les statistiques utiles à cette fin de leur bordereau de paie.

C'est dans l'intention de pallier à cet état de choses qu'un sous-comité de recherche de l'*Employers' Council of British Columbia* a tenté de trouver une méthode permettant d'en arriver à une certaine standardisation dans ce domaine. L'expérience fut utile : on a pu en arriver à un certain degré d'uniformisation dans la terminologie, faire prendre conscience aux petites entreprises de l'importance de ce facteur dans l'évaluation des coûts, échanger des renseignements. Il y a eu une évolution certaine en Colombie Britannique, même si l'on doit encore recourir au pifomètre en attendant que les définitions proposées deviennent plus familières.

La Commission de médiation du ministère du Travail a fait, elle aussi, de grands efforts pour établir un service efficace afin d'aider au calcul du coût des avantages sociaux mais la grande difficulté ce fut de la vendre aux médiateurs, aux employeurs et aux dirigeants syndicaux. Cela n'a pas réussi et le service est disparu, l'automne dernier, en même temps que la Commission de médiation.

Néanmoins, il reste possible de faire accepter un tel service à condition de démontrer de façon concrète l'utilité, l'importance et la valeur pratique de tels calculs.

Un service du calcul du coût des avantages sociaux doit être un instrument de communication qui comporte à la fois la cueillette, l'emmagasinage, l'analyse et la diffusion des renseignements sur le coût de travail. Le service sera d'autant plus efficace qu'il sera en mesure de fournir rapidement des renseignements présentés avec clarté et avec simplicité.

Les renseignements sont requis à trois paliers : dans l'entreprise d'abord dans un but de planification, de vérification et de mise au point des méthodes à suivre dans l'évolution du régime des relations professionnelles, à la table de négociation, pour répondre enfin aux demandes des syndicats, des employeurs et du gouvernement.

C'est l'entreprise qui réclame le plus de tels renseignements afin de savoir comment les avantages sociaux qu'elle accorde se comparent avec ce qui existe ailleurs dans l'industrie et le milieu économique, afin d'établir les écarts, dans la négociation collective, entre ce qui est demandé et ce qu'elle est disposée à concéder, afin de connaître quel sera le coût pécuniaire des modifications à l'étude. Ce sont là des questions auxquelles les dirigeants d'entreprise veulent obtenir une réponse immé-