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Shifts in benefit allocations among U.S. employers 2000 – 2020

By Brendan McFarland and Steven Nyce

Over the past two decades, escalating healthcare costs, historically low interest rates and an aging workforce have made employee benefits much more expensive. As we have explored in other WTW research, this has created numerous challenges for employers in managing their total rewards budgets, often causing them to reduce merit increases to pay for the rising cost of benefits.[1]

Meanwhile, many American households are struggling to make ends meet. Whether it's the baby boomers behind on retirement savings or the millennials trying to keep up with student loan debts, wage increases that barely eclipse general inflation are making their burden that much greater.

Delivering a benefit package that employees value has never been more important. With all the uncertainties surrounding the economy, labor markets and geopolitical environment, employees are looking to their employers for greater security and specifically more financial assurances than ever before. Failing to address these concerns has become a top business issue. The risk of losing key employees and the drag on employee engagement and performance are big concerns for employers that are unable to get this right.

Estimating the cost of employer benefits

This analysis focuses on employer costs as a percentage of average pay for defined benefit (DB),[2] defined contribution (DC),[3] postretirement medical (PRM) and active healthcare plans from 2000 to 2020. These represent the largest components of benefits spend at most organizations. The cost of retirement benefits is based on the WTW Benefits Data Source database, a comprehensive source of information about employee benefits, including retirement, health and welfare, paid time off, lifestyle and flexible benefits. The analysis defines total retirement benefits as the combined value of DB, DC and PRM plans.

To determine how much employers spend as a percentage of average pay, the analysis applies key economic assumptions to a hypothetical rather than actual workforce so we can compare spending on the same basis across all employers. DB spend (which related to both pension and retiree medical) represents the normal cost (value of benefits accrued during the year), and

[1] See "**Healthcare USA: The big paycheck squeeze**," *Insider*, May 2023.

[2] In a DB retirement plan, the employer promises a specified payment in retirement typically based on the employee's earnings history, tenure and age. The plan can provide a predictable income stream in retirement, as an annuity must be offered even if the formula is lump sum-based.

[3] In a DC plan, such as a 401(k) or 403(b), employees elect to defer compensation into an account that they typically manage, including choosing investment options. Most employers contribute to the account as well. These plans generally allow employees to take their account balance with them when they leave the organization or to transfer it to another employer-sponsored plan or individual retirement account.

benefits are valued using the projected unit credit (service prorate) methodology. DC values reflect assumptions of participation and contribution rates (this study considers only employer contributions). To ensure that employer spend as a percentage of pay is comparable across all years, factors were used to normalize all values to 2020.

Active healthcare costs as a percentage of pay used data from WTW's Financial Benchmarks Survey from 2000 to 2020. This database annually collects detailed healthcare plan and cost information along with individual enrollment choices for over 1,000 employers. Healthcare costs include employer contributions to premiums for medical and pharmacy plans, plus any account contributions and rewards/surcharges paid by the plan. Healthcare costs are adjusted by age, family size and geography to normalize per-employee annual costs across the database. Costs do not include the employee's portion of premiums or any point-of-care costs.

All values in this analysis are based on benefit programs offered to newly hired salaried workers. To control for the changes in the sample composition over time, we weighted the observations by the size of the employer's workforce to arrive at weighted averages.

These costs may not reflect the real-world dollar amounts spent on benefits and compensation for any given year. For example, retirement and retiree medical benefits can vary widely across a workforce because of changes to benefit plans over time, so some older, grandfathered cohorts might receive a benefit package no longer offered to newly hired employees. Likewise, some sponsors of DB plans are paying more to make up for earlier funding shortfalls, and such legacy costs are not included here.

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Active healthcare costs more than tripled, well surpassing pay increases.

The value of this approach is that it provides a window into the direction employee benefits are heading, which for many organizations can be very different from where they were in the past and where they are today.

Employer trends in benefit costs

Between 2000 and 2020, two dominant trends in core benefits emerged:

1. Active healthcare costs more than tripled, well surpassing pay increases, driving up total benefit values over the past 20 years.
2. Retirement programs, including DB pensions and retiree medical plans, were significantly scaled back, replaced by less generous account-based programs.

Total benefit costs increased from 14.9% of pay in 2000 to 19.4% of pay in 2020. During this period, active healthcare costs jumped from 5.9% to 12.3% of pay (Figure 1, next page). While healthcare costs have increased significantly over the past 20 years, this trend has slowed over the past decade. Employers have taken many actions to bend the cost curve, most notably adopting account-based healthcare programs. While the gap between rising healthcare costs and pay increases closed considerably over much of the 2010s compared with the previous decade, healthcare costs as a percentage of pay continued to rise — up 1.6% of pay.

At the same time, retirement cost increases as a percentage of pay remained flat over the past decade. This is a stark contrast to the previous decade where the generosity of retirement programs declined by over 20% to offset the significant increases in healthcare costs over the 2000s — from 9.0% to 7.1% of pay. Since the beginning of this century, many employers have shifted away from DB plans as their primary retirement vehicle, typically replacing them with an enhancement to the existing DC plan. In fact, DC benefits increased by 2.4 percentage points between 2000 and 2020, although not enough to replace the 3.6 percentage point loss in DB benefits. Those replacement levels normalized to some extent from 2010 to 2020, with DC values increasing by 1.1 percentage points to offset a 1.0 percentage point decline in DB values.

The value of retirement benefits has also declined due to many companies eliminating PRM for new hires. In fact, employer subsidies declined by 0.7 percentage points over the past two decades and only represent 0.2 percentage points of pay in 2020.

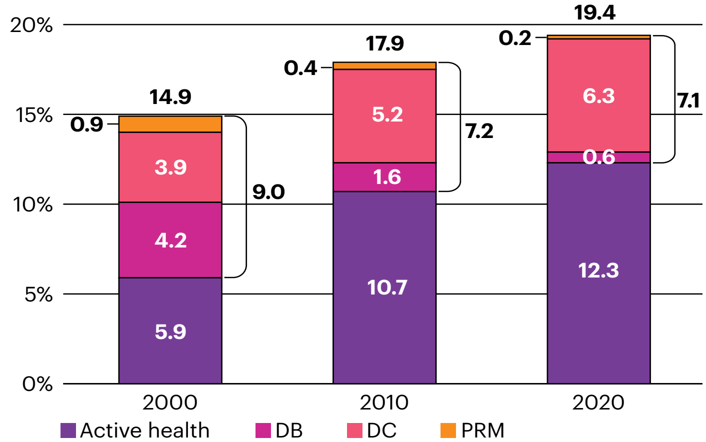
These trends reflect a seismic shift in the allocation of benefit dollars (Figure 2). In 2000, active healthcare costs comprised about two-fifths of benefits while retirement benefits made up the remaining three-fifths. By 2010, the ratio had flipped, with active healthcare benefits accounting for three-fifths of costs and the retirement share dropping to two-fifths. Over the past decade, the share of cost attributed to healthcare increased slightly compared with the previous decade, with active healthcare now comprising almost two-thirds of the total employer value.

As noted above, much of the reduction in retirement value can be attributed to the widespread shift from a traditional DB with supplemental DC to a DC only. The transition typically involved freezing or closing the DB plan.[4] Between 2000 and 2020, the percentage of organizations offering a traditional DB plan to new hires dropped from 48% to 5% (Figure 3). By 2020, 82% of employers sponsored only a DC plan for new hires compared with 37% in 2000. Employers typically contribute more to the DC plan after closing or freezing a DB pension, but the higher DC contributions generally do not offset the value of the lost pension.

Another notable trend in retirement plans is that many employers decided to continue providing a pension by converting their traditional DB plan to a hybrid DB plan.[5] Historically, traditional DB plans have often delivered richer benefits than hybrid plans, especially to longer-tenured workers. In a hybrid pension, the employer still bears the financial risk of managing a pension, whereas in a DC-only environment, all investment and longevity risks rest with the worker. Among companies that sponsored a DB pension for new hires in 2020, 72% offered a hybrid pension, up from 24% in 2000.

As noted above, retirement plan costs can vary widely among employers depending on the types of plans they offer. In 2020, among those that offer only a DC plan to new hires, the average retirement spend was 6.8% of pay (Figure 4, next page). Among employers that also offer pensions — hybrid or traditional — to new hires, the average retirement cost was 8.9% and 9.5% of pay, respectively. In

Figure 1. **Total employer benefit values as a percentage of pay, 2000 – 2020***

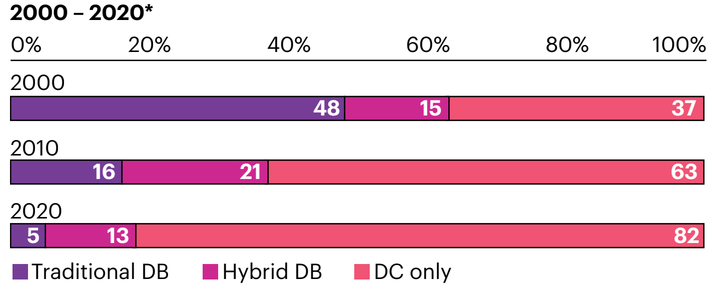


*All employers, weighted by employer size
Source: WTW Benefits Data Source

Figure 2. **Share of employer benefits as a percentage of pay — active health vs. retirement, 2000 – 2020***

*All employers, weighted by employer size
Source: WTW Benefits Data Source

Figure 3. **Prevalence of retirement plan types for new hires, 2000 – 2020***



*All employers
Source: WTW Benefits Data Source

[4] When a sponsor freezes a DB plan, some or all benefits stop accruing for some or all participants. For example, the plan might stop accruing benefits linked to service but continue those linked to pay, or benefits might stop for all participants younger than 50 with 15 or fewer years of service. After a sponsor closes a pension plan, benefits continue to accrue for participants while no one else can join the plan.

[5] Hybrid DB plans define the retirement benefit as an account balance rather than an annuity. Hybrid benefits typically accrue more evenly across a worker's career (although designs can increase benefit accruals by age, service or a combination of the two). When hybrid plan participants leave their employer, they usually take their account balance with them (either immediately or more typically some number of years later). As DB plans, hybrid plans must offer an annuity as the primary distribution option.

The biggest decline in retirement plan values occurred among companies retaining their traditional DB plans.

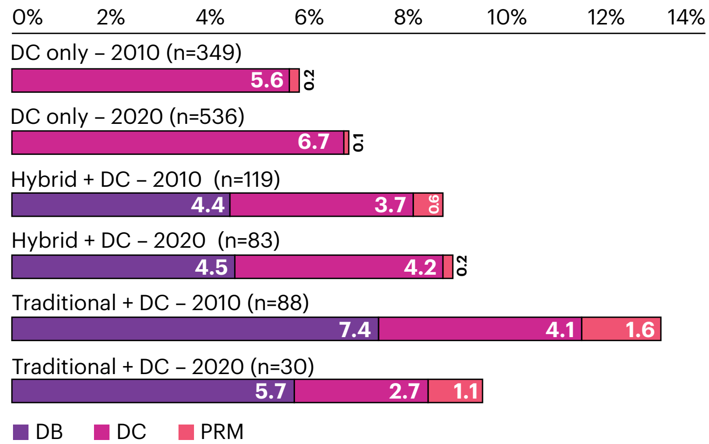
2020, the value of traditional DB plans averaged 5.7% of pay, while hybrid plans averaged 4.5% of pay. Additionally, hybrid sponsors offer richer DC benefits relative to their traditional DB sponsor counterparts, possibly to help offset the removal of the less generous traditional DB plan when replacing it with a hybrid pension. Moreover, employers that still offer traditional DB plans were more likely to also offer more generous PRM plans. In 2020, the average PRM value was 1.1% of pay for sponsors of traditional DB plans versus 0.2% among hybrid plan sponsors.

An important trend to examine more closely is the dynamics behind the flattening of retirement plan values over the past decade. From 2010 to 2020, average total retirement values as a percentage of pay offered to new hires were basically unchanged at 7.2% in 2010 and 7.1% in 2020.

Two main factors are driving this trend. First, DC-only sponsors became a much larger group (82% of the sample in 2020) and began offering more generous programs. As more DB sponsors closed their DB plans over the 2010s and became DC-only sponsors by 2020, a common trend for companies closing a DB plan was to simultaneously make enhancements to their DC plan. This ensured that the value of their retirement program remained competitive with their peers in which they compete for talent. As such, retirement values for DC-only sponsors increased from 5.8% to 6.8% of pay over the past decade.

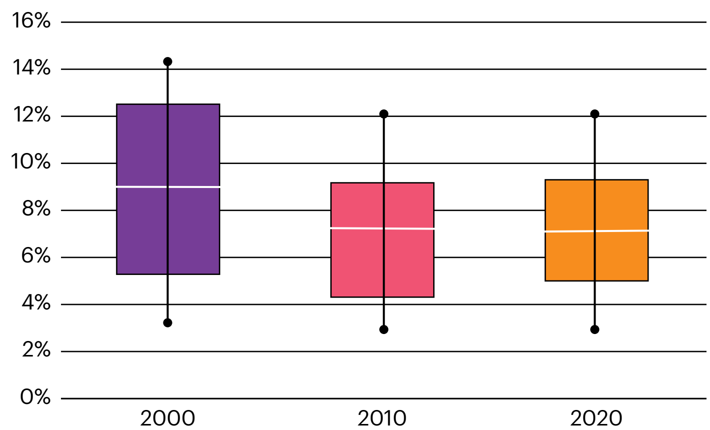
The second main factor behind the stabilization of retirement plan values is that companies offering DB plans to new hires in 2020 report lower plan values. The biggest decline in retirement plan values occurred among companies retaining their traditional DB plans. The main driver behind this trend is that many companies with the most generous DB plans in 2010 changed to hybrid plans by 2020, which tend to be less generous than traditional DB plans. Fewer employers who maintained their traditional DB programs made plan changes to decrease the value of their program. In total, the larger group of DC-only sponsors with more generous programs compared with a decade ago is offset by the reduction in retirement plan values among DB sponsors.

Figure 4. **Total employer retirement benefit values as a percentage of pay by retirement plan type — 2010 vs. 2020***



*All employers, weighted by employer size
Source: WTW Benefits Data Source

Figure 5. **Distribution of total employer retirement benefit values as a percentage of pay, 2000 – 2020**



	10th percentile	25th percentile	50th percentile	75th percentile	90th percentile
2000	**3.1%**	**5.3%**	**9.0%**	**12.4%**	**14.5%**
2010	**2.7%**	**4.3%**	**7.2%**	**9.1%**	**12.2%**
2020	**3.5%**	**5.0%**	**7.1%**	**9.2%**	**10.9%**

Source: WTW Benefits Data Source

Although retirement plan values remained largely unchanged over the past decade, the distribution of retirement values over the past two decades has narrowed quite significantly. Figure 5 illustrates how the lower and upper bounds have moved closer to the norm as richer DB benefits have become less prevalent and employers with less generous retirement benefits have made a move to close the gap with their peers. In fact, the range between the 90th and 10th percentiles has precipitously declined over the past two decades from 11.4% in 2000 to 9.5% in 2010 to 7.4% in 2020.

Benefit values still differ across industries

Overall benefit generosity also varies by industry (Figure 6). Active healthcare costs are substantial across all sectors, ranging from 11.3% of pay in the general services sector to 14% of pay in the oil and gas, utilities and chemicals sectors.

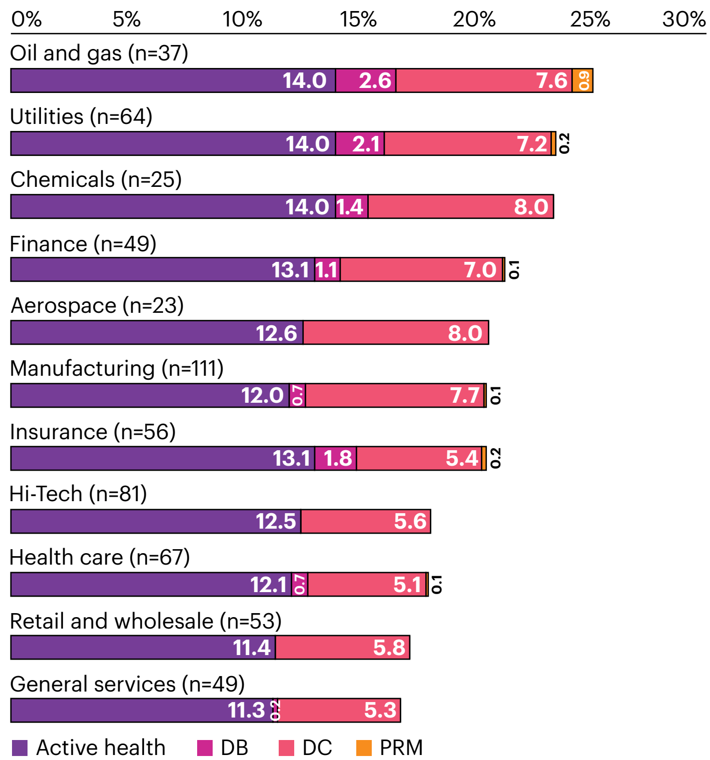
Disparities among industries are more pronounced for retirement benefits. For example, total retirement benefits averaged 11.1% of pay in the oil and gas sector compared with roughly 5.5% of pay in the general services sector. Utility, oil and gas, and chemical manufacturing companies have some of the highest DB sponsorship rates among sectors. Additionally, these sectors also provide very rich DC benefits. Utilities are typically heavily unionized and generally prefer to maintain a consistent retirement structure for both union and nonunion workers. Moreover, many oil and gas jobs are physically demanding, and DB plans help these companies facilitate an orderly retirement of their workforce.

Overall benefit costs as a percentage of pay were also higher than average in the aerospace, finance, insurance and manufacturing sectors. The finance and insurance sectors include insurance organizations, which have high DB sponsorship rates, although banks and other finance employers have been less likely to offer DB plans to new hires since the 2008 financial crisis.

While many manufacturers shifted from DB to DC plans over the past decade, most of them enhanced their DC contributions after closing or freezing the DB plan and thus provide DC benefits of relatively high value to newly hired workers today.

Disparities among industries are more pronounced for retirement benefits.

Figure 6. **Total employer benefit values as a percentage of pay by industry, 2020***



*Weighted by employer size
Source: WTW Benefits Data Source

Figure 7. **Change in total and retirement benefits by sector, 2010 – 2020**

	2010	2020	Change in total benefits	2010	2020	Change in retirement benefits
Retail and wholesale (n=53)	14.2%	17.2%	3.0%	4.9%	5.8%	0.9%
General services (n=26)	14.5%	16.8%	2.3%	4.6%	5.5%	0.9%
Health care (n=45)	16.8%	18.0%	1.2%	5.2%	5.9%	0.7%
Hi-Tech (n=81)	18.1%	18.1%	0.0%	6.6%	5.6%	–1.0%
Manufacturing (n=111)	18.9%	20.5%	1.6%	8.6%	8.5%	–0.1%
Aerospace (n=12)	19.2%	20.6%	1.4%	8.6%	8.0%	–0.6%
Finance (n=65)	19.5%	21.3%	1.8%	9.1%	8.2%	–0.9%
Insurance (n=56)	20.4%	20.5%	0.1%	10.0%	7.4%	–2.6%
Utilities (n=64)	23.6%	23.5%	–0.1%	12.1%	9.5%	–2.6%
Chemicals (n=25)	24.4%	23.4%	–1.0%	10.5%	9.4%	–1.1%
Oil and gas (n=37)	26.7%	25.1%	–1.6%	15.2%	11.1%	–4.1%

Source: WTW Benefits Data Source

On the other end of the spectrum, the high-tech, general services, and retail and wholesale sectors have had low DB sponsorship rates historically, as DC plans are probably a better fit for their more mobile workforces. DC values have remained comparatively low for this group, as there typically has not been a pension loss to prompt employers to enhance DC benefits.

In terms of industry trends over the past decade, we see supporting evidence for the narrowing of retirement benefit values across industries (Figure 7). In 2010, the average retirement value by sector ranged from 4.9% of pay (retail and wholesale) to 15.2% of pay (oil and gas). By 2020, this gap shrunk, ranging between 5.5% of pay (general services) to 11.1% of pay (oil and gas). Over the past decade, those industries with less generous retirement benefits in 2010 (retail and wholesale, general services and healthcare) increased the value of their retirement offerings. Conversely, those sectors with very rich retirement benefits in 2010 continued to scale back their retirement programs over the past decade. These patterns with retirement programs carry over to the overall value of benefits. Those sectors with the least generous benefits in 2010 (retail, general services) report the greatest enhancements, while those with the most generous benefits in 2010 (oil and gas, utilities) report the largest retrenchments in overall benefit values.

Conclusion

Significant changes in employer healthcare and retirement benefits have occurred over the past 20 years. Overall, benefits have become much more expensive for employers, driven mostly by the rapid increases in active healthcare costs, which have risen much faster than any other aspect of company rewards. Companies have responded by reducing other aspects of rewards, notably retirement benefits. While the value of retirement benefits declined markedly over the 2000s, the good news is that employers generally held the line on their retirement benefits over the past decade. Despite more moderate increases in employer healthcare costs over the past decade, benefits continued to become a larger share of companies' total rewards — increasing by over 30% over the past 20 years.

Looking ahead, what can we expect from employer benefits? As we have seen in the past few years, post-pandemic, many changes are in store for the current decade. Employers are likely to remain increasingly focused on adopting and delivering benefits that support the growing challenges facing employees. Projections for increasingly tight labor markets for most of the next decade suggest employers will continue to focus on using their benefits to attract and retain talent.

Managing the persistent rise in healthcare costs remains the biggest challenge for employers' benefit programs today.

What do employees want? While employee needs vary greatly by socio-demographic factors, our research shows workers have a universal desire for greater security in their benefit package.[6] Most want their employers to offer more generous retirement and healthcare benefits over any other benefits. There is a growing recognition that the rising cost of basic needs has employees struggling with their short-term finances. Increasingly, employers are looking at ways to broaden how they support employees' financial security through programs that better manage employee household spending and borrowing. This can include support for employees making big financial decisions and taking steps to free up retirement plan contributions for emergency purposes or to pay down debts such as student loans.

Employees also cite a need to make better use of their existing benefits. Employers are taking many steps to boost employee engagement in their benefit programs through integrated benefit platforms, targeted communication and navigation services to help steer employees when using benefits and by offering greater choice and flexibility in their offerings. Transparency in the benefits offered also helps to improve employee appreciation of their programs. In this regard, the shift from traditional DB pensions to hybrid pensions or DC plans helps to create greater line of sight for employees to the value of their retirement benefits and can be more favorable to employees who are more likely to change jobs, providing more equitable outcomes, especially to lower income employees.

But above all, managing the persistent rise in healthcare costs remains the biggest challenge for employers' benefit programs today. This includes adopting broad-based methods to control the drivers of price and utilization, especially the spend on prescription drugs — the fastest growing component of employer healthcare plans over the past five years.[7] With the adoption of the new slate of GLP-1 drugs marketed to the overweight and obese

[6] See **WTW's Global Benefits Attitudes Survey, 2022.**

[7] Health Care Cost Institute, **2021 Health Care Cost and Utilization Report.**

populations (which is upward of 40% of the workforce), this has the potential to put even more pressure on healthcare costs. Also, improving program efficiency, especially in selecting and coordinating with the vast number of vendor partners, is critical to ensure employees are getting ample value from these business investments. There are many other actions that employers have been taking to control their healthcare cost spend. [8]

But in the end, companies that are unable to effectively manage their healthcare cost increases face considerable pressure in other aspects of their total rewards budgets. It is those employers that can successfully manage the rising healthcare costs that stand to gain a significant advantage in the coming decade when the competition for talent is expected to be a top business issue.

[8] See **WTW's Best Practices in Healthcare Survey.**

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