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FLEXIBLE BENEFITS AS A STRATEGIC TOOL: SUPPORTING THE USE OF HUMAN RESOURCES AS A DISTINCTIVE COMPETENCY

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ABSTRACT

Changes in marketplace competitiveness have forced the small business owner to recognize the benefits of implementing sound management principles. Two areas of management that have gained increasing attention in the small business research are business strategy and human resource management. This paper suggests that smaller firms can gain a competitive edge through developing a distinctive competency in the human resource area. One human resource tool, flexible benefits plans, is described and a strategic model is suggested that outlines how they can be used to help develop a firm's human resources as a distinctive competency.

INTRODUCTION

Fundamental changes in the marketplace, such as changing consumer preferences, population shifts, the evolution toward a service economy, and record numbers of new business start-ups, have given increased importance to the use of progressive management techniques by small firm owners. Managers of large firms have long placed a priority on the use of strategic management techniques as a key competitive tool. However, the use of strategic management principles may also enhance the competitive position of many smaller firms. Early studies on the use of strategic management by smaller firms indicated a lack of widespread adoption (Sexton & Van Auken, 1982; Robinson & Pearce, 1984); however, Naffziger and Kuratko (1991) found that small firm owners do, indeed, spend a great deal of time with planning activities.

BENEFITS OF STRATEGIC PLANNING

Several benefits accrue to smaller firms engaging in strategic planning (Stoner & Fry 1987). Among them are: (1) strategic planning helps focus on the competitive nature of the firm, both externally and internally; (2) strategic planning helps set a formal direction for the firm; and (3) strategic planning allows employees to see the direction of the firm more clearly. In addition, numerous studies verify the influence of strategic planning on small firm performance (Miller & Toulouse, 1986; Orpen, 1985; Sexton & Van Auken, 1985; Robinson, Logan, & Salem, 1986). Porter (1980) suggested three generic strategies are available to firms: differentiation, cost leadership, and focus. A differentiation strategy seeks to establish a distinctive competency within a firm that clearly distinguishes that firm from its competitors, thus creating a reason for patronizing the firm rather than others (Miller & Toulouse, 1986). Stoner and Fry (1987, p. 89) defined a distinctive competency as "any area, factor, or consideration that provides a business a meaningful, competitive edge over its business rivals. Distinctive competencies represent those sets of factors that positively distinguish a firm from its competitors." Distinctive competencies can be developed and utilized as the foundation of a firm's competitive strategy. Opportunities for distinctive competencies within small businesses may include product or service quality, location, filling a special niche, flexibility and adaptability, strong consumer orientation, reputation and image, price, and human resources (Stoner & Fry, 1987). A distinctive competency has value to the firm only if customers perceive and place a value on it. The strategic use of one or more distinctive competencies for a firm depend upon key factors in the marketplace such as customer demands and the competition.

HUMAN RESOURCES AS A DISTINCTIVE COMPETENCY

A human resource focus can serve as a distinctive competency that will allow a firm to differentiate itself from the competition and serve as a cornerstone of the firm's competitive strategy in the marketplace. In support of human resources as a distinctive competency and a strategic tool, McEvoy (1983, p. 32) commented "There is little doubt that the effective management of human resources is a key element in the success of smaller businesses." According to Stoner and Fry (1987, p. 93) personnel, or human resources, can be a distinctive competency for a firm if "management and employees have extensive experience or knowledge, and know how to help the customer. When customers recognize these strengths and believe it is superior to the strengths of other businesses, a distinctive competency exists".

Hornsby and Kuratko (1990) provide evidence of the importance of human resources in small firms. Their research examined the critical issues in human resource management confronting small business owners. Wages and benefits, as well as the availability of quality workers, were consistently cited as the most critical issues by the small business owners. This suggests that human resource management is an area that should be given great attention by organizations in the 1990s.

Owners of businesses that are highly dependent on quality personnel, such as retailers and service providers, would do well to focus on the development and use of their human resources as a distinctive competency. Small manufacturers needing specially trained, highly skilled workers will benefit if they can retain their better employees, especially if they compete for employees against larger firms with higher wage scales. In order to achieve and maintain their competitive advantage, firm owners must pursue human resource policies that attract and sustain an exceptional workforce; however, the attraction and retention of competent workers has long been a recurring problem for small firms.

Schuler and Jackson (1987) cited a link between Porter's competive strategies of innovation, quality enhancement and cost-reduction, and role behaviors. Specifically, they cited12 role behaviors that are important to the implementation of these strategies. These role behaviors include: creative, innovative behavior; long-term versus short-term behavior; independent, autonomous behavior; concern for quality; concern for quantity; risk taking; concern for results; preference for responsibility; flexibility; tolerance of ambiguity and unpredictability; skill application; and job involvement.

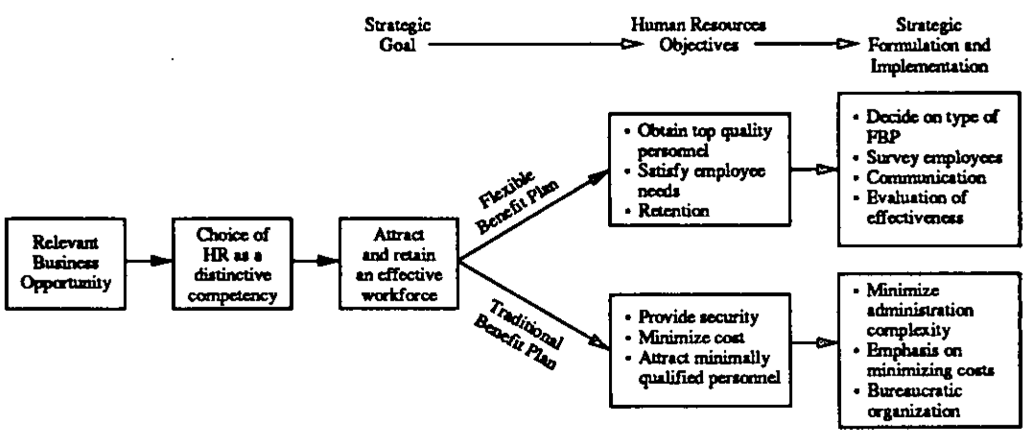
According to Schuler and Jackson (1987), six human resource "menus" can be chosen to reinforce desired role behaviors that lead to the implementation of competitive strategies. These menus include choices in planning, staffing, appraising, compensating and training and development.

In the area of compensation, the importance of the choices that can be made when designing a competitive compensation package is emphasized. One important decision is the choice between a "standard fixed package" of benefits versus a "flexible package" of benefits. While this is not the only compensation choice, the identification of the link between type of benefit package and desired role behaviors seems to be pertinent to the implementation of human resources as a distinctive competency.

This paper focuses on a specific human resource management tool, flexible benefit plans (FBPs), which may help smaller firms attract and especially retain qualified workers. Owners seeking to establish human resources as a distinctive competency may find flexible benefits to be a viable tool.

Figure 1 presents a model, based on Stoner and Fry's (1987) model, designed to illustrate the important considerations in using flexible benefit plans as a distinctive competency. It contrasts flexible benefit plans with traditional benefit plans as well as the strategic formulation and implementation of each method. These benefit alternatives will impact the employees, the organization, and the firm's strategy differently.

Figure 1. *Implementing Flexible Benefit Plans as a Distinctive Competency: An Illustrative Model.*



The model has significance for firms pursuing a business opportunity where the firm's owner has chosen to pursue human resources as a distinctive competency and the accompanying strategic goals are to attract and retain a high quality effective workforce. In order to achieve success in certain business situations, human resources can serve as an important part of business strategy. It is proposed that benefit packages are among the tools available to accomplish the strategic goal of attracting and retaining a quality workforce. The model contrasts the human resource objectives under both benefit systems and the outcomes that result from pursuing human resources as a distinctive competency through the use of a traditional benefit system and a flexible benefit system.

Finally, the model compares the strategic implementation of each type of benefit plan. In the use of FBPs the important steps revolve around surveying employee needs and preferences, deciding on the type of FBP to initiate, maintaining effective communication with the employees and, finally, evaluating the effectiveness of the plan. In contrast, the primary concerns of a traditional benefit plan revolve around minimizing administrative complexity, minimizing costs of the plan, and developing the bureaucratic mechanism to administer the plan. While those are concerns of the FBP as well, an FBP will look beyond administrative concerns to higher-order strategic performance goals and concerns of the organization.

This paper, as illustrated by the model, proposes that FBPs will lead to the more effective accomplishment of the goal of human resources as a distinctive competency by improving the likelihood that the firm will be able to attract and retain top quality employees. To more fully understand the use of FBPs as a distinctive competency, the following sections discuss the general role of employee benefits and the types of FBPs available.

ROLE OF BENEFITS

Schuler, Beutell, and Youngblood (1989) identified seven outcomes organizations seek through the use of benefits or indirect compensation. These are to: (1) attract employees, (2) increase morale, (3) reduce turnover, (4) increase job satisfaction, (5) motivate employees, (6) enhance the firm's image, and (7) remain cost effective. When an organization considers the package of benefits to offer, it must remember that there are mandatory benefits which are required by law such as workman's compensation, and voluntary benefits that an employer may elect to offer or not. Exhibit 1 indicates many of the benefits offered by employers.

Exhibit 1

Commonly Offered Benefits

MANDATORY BENEFITS
Social Security
Workman's Compensation
Disability
Unemployment

VOLUNTARY BENEFITS	
Pension/Retirement Plans	Health Maintenance Organization (HMO) Fees
Vacation Time	Psychiatric Services
Salary Continuation Plans	Profit Sharing
Group Life Insurance	Deferred Compensation/ Stock Plans
Group Hospital, Surgical and Medical Insurance	Executive Dining Rooms
Dental Insurance	Holidays
Accidental Death and Dismemberment Insurance	Recreation Facilities

Traditionally, organizations have allocated benefits to all employees in the same fashion; that is, each employee receives the same benefits. The quantity of some benefits, such as vacation, may be related to factors like seniority or tenure within the organization (Swanson, 1984); however, companies have recently begun trying a flexible approach to benefit packages. A flexible approach to the administration of benefits means the firm is allowing the employee more control over those benefits he/she receives and their quantity, recognizing that not all employees are in the same position in life nor do they place the same priority on all benefits. Flexible packages, by virtue of their design, should facilitate a firm's ability to achieve the goals mentioned by Schuler, et. al. (1989).

FLEXIBLE BENEFIT PLANS

A Flexible Benefit Plan is any plan that allows participants to choose some or all of their benefits, whether the choice be among different levels of one type of benefit or among different types of benefits. According to Foster (1986, p. 155) an essential element of a flexible benefit plan is that it offers "an individual combination of benefits to each employee, rather than a standard program that covers all employees in the same way."

During the 1980s, a great number of large firms switched to FBPs. By 1986, 28 of the Fortune 100 companies and 70 percent of the Fortune 500 companies offered flexible benefit plans (Finlayson, 1986). In 1983, the Conference Board identified three important reasons that motivated employers to adopt a flexible benefit plan: (1) to accommodate varying employee needs, (2) to help control benefit costs, and (3) to help control rising costs of health insurance (McCaffery, 1988).

The Hewitt Associates' 1986 survey of flexible compensation programs and practices found that meeting diverse employee needs and containing costs were still the number one and two reasons, at 90 and 80 percent respectively, for implementing flexible benefit plans ("Cost Management Works...", 1987, p. 66). Other commonly stated reasons are to increase the number of satisfied workers in an attempt to improve employee relations and worker morale and to increase worker retention and productivity. By using FBPs, employers are trying to make employees more aware of the value-to-cost ratio of the benefit plan and provide greater individualized attention.

Smaller firms that have implemented FBPs have tended to select one of five main types: (1) the reimbursement account, (2) the additional allowance or add-on approach, (3) the mix and match option, (4) the core carve out plan, or (5) the modular plan ("Flexible Benefits...For You?", 1985, p. 21; Foster, 1986; "Fundamentals of ... Programs", 1987, p. 188; Johnson, 1986; Kamerman & Kahn, 1987; McCaffery, 1988, p. 174). Exhibit 2 summarizes these FBP variations.

Exhibit 2

Characteristics of Principle Flexible Benefit Plan Types

TYPE OF PLAN	CHIEF CHARACTERISTICS
REIMBURSEMENT ACCOUNT (Flexible Spending Account)	Simplest, plan pays certain expenses not covered by basic plan with pre-taxed dollars.
ADDITIONAL ALLOWANCE (Add-on Approach)	Supplements core benefits with options based on length of service; employee receives "flexible credits"; excess may be invested in 401(k) plan.
MIX AND MATCH PLAN	Also supplements basic plan but allows for different coverage levels on various options; employee may buy additional coverage at own expense.
CORE CARVE OUT PLAN	Similar to additional allowance plan; current package is reduced to create two part plan with a core and flexible portions; core provides basic floor coverage; credits are used to by additional coverage.
MODULAR PLAN	Pre-designed, pre-packaged modules; each module is designed with particular type of employee in mind; modules have same range of benefits but with varying levels of coverage.

It is important to recognize that there are some important issues which confront companies when considering the selection of a flexible benefit plan. It is true that several potential barriers to successful implementation of FBPs do exist. There will usually be an initial expenditure for the development of the plan, such as the retention of a human resource consultant or legal advisor. Along with the cost will be concern for additional time devoted to the development and administration of the plan. Tax and other legal considerations must be dealt with and unions may not whole-heartedly endorse the use of an FBP. Finally, employees may need benefit counseling in order to fully understand their options and appropriate choices.

RESEARCH ON FLEXIBLE BENEFIT PLANS

There is a growing amount of research that has investigated the use of FBPs by smaller firms. Hornsby, Kuratko, and Wallingford (1991) surveyed 67 smaller firms (e.g., companies that employ 500 employees or less) concerning their benefits administration procedures. Companies were asked 14 questions concerning type of plan offered (e.g., flexible or traditional plans), types of benefits to be included in their plans, the impact of their plans, and their satisfaction with the plans.

While only 17 percent of the responding companies currently utilized FBP's, their responses were supportive. Companies that use FBP's cited the need to accommodate diverse employee needs, the need to improve employee appreciation of and satisfaction with benefits, and the need to control benefit costs as reasons for plan implementation. On the other hand, the majority of smaller firms that did not use FBP's cited profit maximization, lack of priority, and lack of expertise as reasons for not using this method of benefits administration.

Regarding the impact of FBP's, 40 percent of the companies using them actually reported a reduction in overall benefits cost and 40 percent reported no change in costs. The remaining 20 percent reported that they did not keep track of the costs. In addition, the companies that utilize FBP's were slightly more satisfied with their plans than those who used traditional plans.

The entire sample was asked to suggest changes in their current plans. One of the most frequently reported comments was the need to offer different levels of coverage to employees based on their needs and their willingness to pay for increased benefits coverage.

Additional support for FBPs is found in a recent survey conducted by Grant Thornton Accountants (October, 1991). In a survey of 1,825 smaller firms (i.e. less than 500 employees), 31 percent utilized some form of FBP. Furthermore, the study indicated that the firms offering flexible benefit plans were more inclined to provide the extra health care benefits such as dental coverage, HMOs, PPOs, and wellness programs.

The Grant Thornton study also found that health care costs in the firms studied have escalated an average 18.3 percent per year. However, the firms offering FBPs spent only 7.5 percent of payroll costs while other firms spent 7.9 percent of payroll costs on benefits. Therefore, in addition to being able to offer a larger variety of health care benefits, FBPs allow them to be delivered at lower cost to the company. This finding is consistent with the findings of Hornsby, et. al. (1991).

A 1990 study conducted by Life Insurance Marketing Research Association also supports the use of FBPs in smaller firms. A survey of 770 small business owners found that companies who did not choose an FBP did so because of administrative complexity. However, of the respondents who utilize an FBP, only 10 per cent stated that the plan was difficult to administer.

In summary, while only a few studies have been conducted which investigate the utilization of FBPs in smaller firms, these studies suggest that smaller firms are beginning to recognize the importance of addressing employee benefits needs. Furthermore, FBPs may serve as a mechanism to reduce the cost of benefits.

CONCLUSION

Most of the reasons cited for not adopting FBP's are based on the firms' lack of understanding of the benefits that could result from their implementation. Firms surveyed cited the need for developing procedures for varying benefit levels based on need and willingness to pay. The choice of a FBP may be the solution to this need. Furthermore, if attracting and retaining competent employees is a critical issue for the 1990s (Hornsby & Kuratko, 1990), smaller firms may need to select compensation options that may improve their ability to attract and retain good employees (Schuler, Beutell & Youngblood, 1989).

This paper does not attempt to suggest that FBPs are the only mechanism capable of maintaining human resources as a distinctive competency. Higher wages, training programs, job enrichment, and better overall benefit plans may also contribute to better retention of key employees. However, it is hypothesized that the use of a flexible benefit plan will lead to more effective accomplishment of the goal of making human resources a distinctive competency than will traditional benefit plans because of the more positive approach they take toward dealing with workers in today's environment. For firms that find themselves depending on high quality employees for competitive success, those techniques that enable them to retain top workers should be given every consideration. Evidence indicates that FBPs can be successfully implemented in smaller firms.

In summary, FBP's may be an important tool for developing human resources as a distinctive competency. More empirical research is needed to ascertain the impact of these plans on management and employees. However, small firm owners and managers must first recognize the need to emphasize their human resources and develop a strategy that will help them reach their desired competitive level. Too often this aspect of operations is overlooked or given little attention in smaller firms. Researchers and consultants in this area can help companies prosper by increasing the emphasis on human resources as a distinctive competency.

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