Employee Benefits 7th edition Martocchio Test Bank

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CORRECT ANSWERS ARE LOCATED IN THE 2ND HALF OF THIS DOC.

TRUE/FALSE - Write 'T' if the statement is true and 'F' if the statement is false.

1) Employee benefits act as a tool for recruiting and retaining desired employees.
   - ⊙ true
   - ⊙ false

2) Social exchange is one where the nature of exchange has been specified at the time of employment.
   - ⊙ true
   - ⊙ false

3) Once the social exchange is set between employer and employee, it does not change over time.
   - ⊙ true
   - ⊙ false

4) Employee benefits need to be considered as economic exchange between employer and employee rather than social exchange relationship.
   - ⊙ true
   - ⊙ false

5) Despite an increasingly diverse workforce in the US workplace, traditional benefits practices assuming similarity among workers can still work well for today's organizations.
   - ⊙ true
   - ⊙ false

6) Psychological contracts explicitly establish terms of employment, which stands in contrast to exchange agreements, such as wage and salary levels.
   - ⊙ true
   - ⊙ false

7) Long-term relationship between employer and employee pertains to transactional psychological contracts.
   - ⊙ true
   - ⊙ false

8) Job security, recognition, and support in exchange for commitment and loyalty to the employer more pertain to relational psychological contracts.
   - ⊙ true
   - ⊙ false

9) Employee benefits practices can fulfill either transactional or relational psychological contracts.
   - ⊙ true
   - ⊙ false

10) Legally required benefits would form a part of employees' transactional expectation.
   - ⊙ true
   - ⊙ false

11) Retirement plans is a good example of benefits that fulfill both transactional and relational expectations.
   - ⊙ true
   - ⊙ false

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12) Psychological contracts do not develop and change over time.
   - ⊙ true
   - ⊙ false

13) Violations of psychological contracts are basically the same as unmet expectations.
   - ⊙ true
   - ⊙ false

14) Violations of psychological contracts are likely to be more intense than unmet expectations because of feelings of betrayal and the onset of mistrust.
   - ⊙ true
   - ⊙ false

15) Employer's expectation of the employee is not as important as employee's expectation about the employer.
   - ⊙ true
   - ⊙ false

16) Tax incentives are the only reason employers offer benefits to employees.
   - ⊙ true
   - ⊙ false

17) One reason for employer-provided health insurance is to avoid adverse selection.
   - ⊙ true
   - ⊙ false

18) As the size of the insured group increases, so does the difficulty for the insurance companies to predict the total medical expenses of the group.
   - ⊙ true
   - ⊙ false

19) Economies of scale refers to the lower amount of co-pay required of employees in a large company as opposed to those in a small company.
   - ⊙ true
   - ⊙ false

20) Medical expenses tend to be higher for men than for women, and higher for minority groups than for whites.
   - ⊙ true
   - ⊙ false

21) The degree to which employers will decrease their hiring, if the market compensation level increases, can affect how much of a benefit's increase cost will be passed on to the employees.
   - ⊙ true
   - ⊙ false

22) Offering some benefits in a compensation package can attract qualified, but undesirable job applicants.
   - ⊙ true
   - ⊙ false

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23) When health benefit costs rise for a single employer in a market, the employer will likely be able to pass along the benefit costs to workers, even if the workers valuation of the benefit has NOT changed.
- ⊙ true
- ⊙ false

24) The IRS offers tax benefits to companies that offer retirement plans.
- ⊙ true
- ⊙ false

25) The concept of justice in the work setting concerns the distribution of rewards, information, and other resources.
- ⊙ true
- ⊙ false

26) If health insurance premiums rise because of advances in medical care technology, employees would probably perceive that the increase added value to their insurance.
- ⊙ true
- ⊙ false

27) Employees in a large company are less likely to be subject to medical underwriting than those in a small company.
- ⊙ true
- ⊙ false

28) Most small group health insurance policies are based on experience ratings.
- ⊙ true
- ⊙ false

29) Even if increased health insurance costs are NOT accompanied by an increase in employees' valuation of the insurance, cash wages will probably be adjusted downward anyway.
- ⊙ true
- ⊙ false

30) One of the drawbacks of Medicare and Social Security insurance, is that neither program can avoid adverse selection.
- ⊙ true
- ⊙ false

31) Offering benefits to employees can be cost effective for employees, but NOT for employers.
- ⊙ true
- ⊙ false

32) Perceived organizational support is an employee's perception of the fairness of the accounts given for certain procedures.
- ⊙ true
- ⊙ false

33) Distributive justice is employees' perceptions of fairness of the process by which decisions are made and the extent to which employees can participate in the process.
- ⊙ true
- ⊙ false

34) Medical expenses are higher for people with new medical histories.
- ⊙ true
- ⊙ false

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35) Experience rating is the process of gathering information about employees' risk profiles.
   - ⊙ true
   - ⊙ false

36) Organizational citizenship behavior is enforceable by management.
   - ⊙ true
   - ⊙ false

37) Offering certain types of benefits in combination with reduced compensation is one way of recruiting desirable workers.
   - ⊙ true
   - ⊙ false

38) An insurance pool refers to all employees who fall into an insured category.
   - ⊙ true
   - ⊙ false

39) Behaviors such as helping other employees, looking out for the employer's interests, and going beyond job requirements to help achieve company goals, are all examples of perceived organizational support.
   - ⊙ true
   - ⊙ false

40) Employee-benefits practices that lead to perceptions of injustice or feelings of contract violations might also lead to poor performance, reduced commitment, and increased likelihood of turnover.
   - ⊙ true
   - ⊙ false

41) In most cases employees do not give up anything to get benefits because they are "free-add-ons" in a compensation package.
   - ⊙ true
   - ⊙ false

42) The greater value employees place on a benefit, the larger reduction in cash wages they will accept if the benefit is introduced into a compensation package.
   - ⊙ true
   - ⊙ false

43) Employers are unable to cut wages when a new benefit is introduced or the cost of providing an existing benefit increases.
   - ⊙ true
   - ⊙ false

MULTIPLE CHOICE - Choose the one alternative that best completes the statement or answers the question.

44) What are the two basic causes for psychological contract violations?
   - A) Distributive and procedural justice
   - B) Reneging and incongruence
   - C) Changing composition of the workforce and the economic challenges
   - D) Legal and industrial environments

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45) Which of the following is not closely associated with the nature of transactional psychological contracts?
   A) Economic and extrinsic focus
   B) Close-ended, specific
   C) Narrow scope
   D) Long-term relationship

46) Which of the following employee benefits is more relevant for relational psychological contracts?
   A) Legally required benefits
   B) Promotions
   C) Life insurance
   D) Accommodation and enhancement benefits

47) Being able to spread the administrative costs to larger groups of employees, to reduce the health insurance cost per employee, is referred to as what?
   A) Insurance pooling
   B) Economies of scale
   C) Economies of scope
   D) Administrative underwriting

48) Which of the following employee benefit might fulfill both transactional and relational expectations of employees?
   A) Life insurance
   B) Retirement
   C) Legally required benefits
   D) Accommodation and enhancement benefits

49) When a company gathers as much information as possible about each participant's risk profile and then offers health insurance at a lower price to healthier people and at a higher price to less healthy people, this is called:
   A) –distributive justice.
   B) –adverse selection.
   C) –an experience rating.
   D) –medical underwriting.

50) Which of the following can be avoided by using experience ratings?
   A) Adverse selection
   B) Medical underwriting
   C) Economies of sales
   D) Insurance pooling

51) What is medical underwriting?
   A) A process where employers have to verify the medical history of their employees
   B) A process where the employer has to pay the difference for insuring high-risk employees
   C) A process where employees provide their past medical history to insurers
   D) A process where one insurance company combines with another to insure a company

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52) In insurance terms, what does adverse selection refer to?
   A) When employees choose an insurance plan they don't like but are stuck with it for a year
   B) When insurance companies use medical underwriting to choose who to insure
   C) When employees are forced to choose between what they think are two inferior insurance programs
   D) The tendency of an insurance pool to disproportionately attract "bad risk" employees and discourage "good risk" employees

53) The degree to which an increase in benefit costs is passed along to employees in the form of lower cash wages generally does NOT depend on which of the following factors?
   A) The cash value employees place on the benefits
   B) The degree to which employers will increase or decrease their hiring when the market compensation level decreases or increases
   C) Whether the benefit cost increases for all employers in a market or for a particular employer
   D) Whether or not the employee is a manager

54) What are the three main reasons that employers offer discretionary benefits?
   A) Employers have a cost advantage, the benefits help in recruiting and retaining workers and the company gets tax incentives to offer them
   B) It's required to by law, the company gets tax incentives to offer them, employers have a cost advantage
   C) The company gets tax incentives to offer them, the benefits help in recruiting and retaining workers, it's required to by law
   D) The benefits help in recruiting and retaining workers, employers have a cost advantage, it's required to by law

55) What is an insurance pool?
   A) Insurance companies that join together to underwrite a self-funded insurance policy
   B) Employers who join together to insurance all their employees under one policy
   C) People who join together to by a group insurance policy
   D) Insurance companies that join together to issue one large-group insurance policy

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56) Employee benefits such as mental health benefits, wellness programs, smoking cessation programs, stress management, and recognition and rewards are all examples of:
   A) Perceived organizational support.
   B) Procedural justice.
   C) Organizational citizenship behavior.
   D) Distributive justice.

57) Why does health insurance become less expensive when the size of the insurance group increases?
   A) Administrative costs are lower, more employees are contributing co-payments, the threat of high-risk individuals driving out low-risk ones is less
   B) Insurance is less risky to provide, the threat of high-risk individuals driving out low-risk ones is less, administrative costs are lower
   C) More employees are contributing co-payments, insurance is less risky to provide, administrative costs are lower
   D) Insurance is less risky to provide, more employees are contributing co-payments, the threat of high-risk individuals driving out low-risk ones is less

58) Which of the following is not a reason why insurance rates decrease as group size increases?
   A) The administrative cost is reduced
   B) There is lesser risk in providing insurance
   C) It is easier to predict cost of insurance
   D) High-risk policy holders are driven away

59) Which of the following statements about employee attitudes and employee benefits is correct?
   A) Employment can be implicit, such as a documented job offer.
   B) Employment can be explicit, such as psychological contracts.
   C) Employee benefits can be both implicit and explicit.
   D) All benefits must be explicit.

60) Which of the following are the four types of justice perceptions outlined in the text?
   A) Distributive, procedural, informational, and interpersonal.
   B) Procedural, interpersonal, organizational, and distributive.
   C) Informational, unequal, distributive, and interpersonal.
   D) Interpersonal, distributive, procedural, and organizational.

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61) Which of the following statements is the definition for perceived organizational support?
   A) The perceived fairness of the accounts given for certain procedures.
   B) The perceived fairness about how rewards are distributed.
   C) The perceived fairness of processes.
   D) The perceived degree to which the employer values the employee's contributions and well-being.

62) When discussing organizational citizenship behavior, which of the following statements is NOT true?
   A) Satisfied employees engage in good citizenship behavior.
   B) A company's employee benefits practices do not influence employees' satisfaction.
   C) Organizational citizenship behavior is discretionary.
   D) Citizenship behaviors tend to go beyond the formal job requirements.

63) If a company eliminates a benefit then intentionally or unintentionally fails to educate their employees about the elimination, employees may judge the employer's decision as unfair. This example is a type of:
   A) Interpersonal justice
   B) Informational justice
   C) Procedural justice
   D) Distributive justice

ESSAY. Write your answer in the space provided or on a separate sheet of paper.

64) Compare and contrast social exchange and economic exchange in the employment relationship.

65) Discuss what psychological contracts mean in employee benefit practices and how psychological contract develop.

66) Briefly discuss how employee benefits aid in recruiting certain types of workers.

67) Explain the concept of justice in a work setting and briefly describe the four types of justice perceptions.

68) Discuss the issue of who pays for employee benefits.

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Answer Key

Test name: Chapter 02

1) TRUE
2) FALSE
3) FALSE
4) FALSE
5) FALSE
6) FALSE
7) FALSE
8) TRUE
9) TRUE
10) TRUE
11) TRUE
12) FALSE
13) FALSE
14) TRUE
15) FALSE
16) FALSE
17) TRUE
18) FALSE
19) FALSE
20) FALSE
21) TRUE
22) TRUE
23) FALSE
24) TRUE
25) TRUE
26) TRUE
27) TRUE
28) TRUE
29) FALSE
30) FALSE
31) FALSE
32) FALSE
33) FALSE
34) FALSE
35) TRUE
36) FALSE
37) TRUE
38) TRUE
39) FALSE
40) TRUE
41) FALSE
42) TRUE
43) FALSE
44) B
45) B
46) D
47) B
48) B
49) C
50) A
51) C
52) D
53) D
54) A
55) C
56) A
57) B
58) D
59) C
60) A
61) D
62) B
63) B
64) Essay

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- The basis for understanding the employment relationship lies in the concept of social exchange—the most basic concept explaining social behavior. Social exchange in the employer–employee relationship is one in which the employer offers inducements (wages and employee benefits) in return for employee contributions (performance and commitment).
- Economic exchange, as with wages and salary, is one in which the nature of the exchange has been specified at the time of employment. Of course, economic exchange can be renegotiated at any time during employment, as with yearly pay raises.
- The employment relations can be said to constitute both economic exchange and social exchange. In exchange for continued employment and wages, employees are obligated to work for the employer.
- A psychological contract has been defined as an employee's subjective perceptions of the relationship of mutual obligations with the employer/company.● Employee benefits can be a part of the psychological contract employees hold about the employer's obligations to them in exchange for their work efforts.
- Psychological contracts result in employees holding a range or continuum of expectations from the employer, ranging from pay and promotions to career development and family welfare.

65) Essay

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- The continuum of expectations that employees hold from an employer can be seen as having two poles: transactional psychological contracts and relational psychological contracts Toward the transactional end of the continuum, employees' expectations from the employer are more economic and extrinsic in nature. Thus, employees' expectations of high pay and promotions or career advancement in exchange for hard work would represent transactional types of expectations in the psychological contract. On the other hand, toward the relational end of employees' expectations from the employer that might be either economic or noneconomic, but are also emotional, subjective, and intrinsic in nature. Thus, employees' expectations of job security in exchange for loyalty to the employer would represent relational types of expectations in the psychological contract.
- Toward the transactional end of the continuum, employees' expectations from the employer are more economic and extrinsic in nature. Thus, employees' expectations of high pay and promotions or career advancement in exchange for hard work would represent transactional types of expectations in the psychological contract.
- On the other hand, toward the relational end of employees' expectations from the employer that might be either economic or noneconomic, but are also emotional, subjective, and intrinsic in nature. Thus, employees' expectations of job security in exchange for loyalty to the employer would represent relational types of expectations in the psychological contract.
- Toward the transactional end of the continuum, employees' expectations from the employer are more economic and extrinsic in nature. Thus, employees' expectations of high pay and promotions or career advancement in exchange for hard work would represent transactional types of expectations in the psychological contract.
- On the other hand, toward the relational end of employees' expectations from the employer that might be either economic or noneconomic, but are also emotional, subjective, and intrinsic in nature. Thus, employees' expectations of job security in exchange for loyalty to the employer would represent relational types of expectations in the psychological contract.
- Legally required benefits would form a part of employees' transactional expectations from the employer.

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- Employee benefits such as the paid time off and accommodation and enhancement benefits examined in the previous chapter might help fulfill employees' relational expectations.
- Retirement plans would be a good example of employee benefits that fulfill both transactional and relational expectations; similarly, educational assistance benefits aimed at rewarding continued employment as well as career development would help fulfill both transactional and relational expectations.
- Most psychological contracts take shape in the preemployment phase phase, when people seek information during recruitment and after receiving a job offer. Employees might seek information about both transactional and relational expectations from their potential employer.
- Ultimately, what the employee learns about employer's benefits practices will form a part of the employee's expectations from this exchange relationship along this transactional–relational continuum.
- Employees can form expectations that comprise their psychological contracts from two sources: their interactions with other members of the company and their perceptions of the company's culture.
- Psychological contracts are flexible in nature, undergoing constant change based on the interactions employees have with the company and with other employees. This flexibility allows employees to adapt to changes in the company's practices. If employees hold relatively stable expectations from employers, any changes in the policies and practices of the company will lead to the employee feeling betrayed unless changes entail offering more rather less. However, if the employees have flexible expectations, they are more likely to change their psychological contracts to adjust for the changes the employer is compelled to make.
- If employees hold relatively stable expectations from employers, any changes in the policies and practices of the company will lead to the employee feeling betrayed unless changes entail offering more rather less.
- However, if the employees have flexible expectations, they are more likely to change their psychological contracts to adjust for the changes the employer is compelled to make.
- If employees hold relatively stable expectations from employers, any changes in the policies and practices of the company will lead to the employee feeling betrayed unless changes entail offering more rather less.

- However, if the employees have flexible expectations, they are more likely to change their psychological contracts to adjust for the changes the employer is compelled to make.

66) Essay
Main Points
- Tailor the benefits package with certain benefits to attract a certain type of workers
- Recent undergraduates might be attracted to a tuition reimbursement benefit
- Women 20-40 might be interested in company-paid health insurance
- Older workers might be attracted to stronger retirement plans
- Tailoring packages might have unintended consequences, like
- Offering strong mental health or substance abuse benefits might attract substance abusers
- Attracting older workers with strong retirement benefits, might increase health insurance costs
- Attracting younger women might increase the need for replacement workers due to maternity leaves and FMLA time off

67) Essay
Main Points
- The concept of justice is concerned with the distribution of conditions and goods that affect individual well-being. In a work setting, the distribution of rewards (such as pay and benefits), information, and other resources will all lead to perceptions of justice.
- Perceptions of justice may be based on the rules by which distributions are made, the way rules are implemented, or the way decisions are made. The basis on which employees are eligible for benefits, the value of those benefits, how the benefits are administered, and employer decisions about which benefits to offer to employees would all influence employees' justice perceptions.
- There are four types of justice perceptions. Distributive justice is perceived fairness about how rewards are distributed; procedural justice is the perceived fairness of processes; informational justice is the fairness of the accounts given for certain procedures; and interpersonal justice is perceived fairness of the interpersonal treatment people receive from others.
- Distributive justice is employees' perceptions of fairness of the outcomes they receive. Where employee benefits are concerned, employees will form perceptions of fairness based on the benefits they are eligible for.

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- Procedural justice deals with employees' perceptions of fairness of the process by which decisions are made and includes the extent to which employees can participate in the process as well as the rules followed.
- Interpersonal justice is the perception of the degree to which the employer demonstrates concern and social sensitivity toward employees.
- Informational justice deals with perceptions about the quality of information used to explain organizational decision making.

68) Essay

Main Points

- Most workers with employer-sponsored health insurance pay a token monthly contribution toward their insurance premium
- The typical monthly contribution ranged between $41.00 to $245.00 for people with single coverage and $198.00 to $1096.00 for people with family coverage
- The monthly contributions allow employers to charge employees different rates, depending on insurance needs, like family size and different levels of coverage
- Monthly contributions make it easier for employers to pass along benefit cost increases to employees
- Instead of lowering income employers may also
- Scale back a scheduled bonus
- Reduce the yearly income increase
- Hire new workers at a lower income level

Part One: Introduction to Employee Benefits

Chapter Two: The Psychology and Economics of Employee Benefits[1]

I. Learning Objectives

In chapter two, you will gain an understanding of:

1. The employment relationship as an exchange relationship and the psychology behind why firms provide employee benefits.
2. Employee benefits as part of the psychological contract and how some employee expectations about benefits might be formed.
3. How employee perceptions of justice or fairness are important to understanding how pay and benefits practices influence employee attitudes.
4. The economic rationales for why companies offer employee benefits.
5. Who pays for employee benefits?

The purpose of this chapter is twofold. First, it is important to learn about the *psychological* basis of employee benefits. Employers can use this knowledge to understand how employee benefits influence the attitudes and performance of their employees. Also, employers can then develop and maintain effective benefits programs aimed at promoting worker satisfaction, commitment, and productivity.

Second, it is important to understand the *economic* basis of employee benefits. Employee benefits are a costly proposition. Even though employee benefits are expensive, most employers continue to offer them. Still, it begs the question pertaining to whether companies should have workers pay for life or disability insurance. After considering the psychology of employee benefits, we will take up topics about the economics of employee benefits.

II. THE PSYCHOLOGY OF EMPLOYEE BENEFITS

1. This discussion is organized into three sections
2. First, the employment relationship as social exchange is considered
3. Second, psychological contracts are discussed
4. Third, we look at the relationship between having a benefits program and employee attitudes

A. Employment Relationship as Social Exchange

1. In the most general terms, the employment relationship consists of clusters of human resource practices offered to a group of employees along with the resulting employee contributions to the employer

[1] The material in this chapter pertaining to the psychology of employee benefits was prepared by Professor Niti Pandey, Department of Business Administration, Eastern Connecticut State University, and edited for this edition by Joseph Martocchio. The material in this chapter pertaining to the economics of employee benefits was prepared by Professor Darren Lubotsky, Department of Economics and the Institute for Government and Public Affairs, University of Illinois at Chicago, and edited for this edition by Joseph Martocchio.

2. The basis for understanding the employment relationship lies in the concept of **social exchange** – the most basic concept of explaining social behavior
   i. All social behavior can be seen as "an exchange of activity (*work effort*), tangible (*visible performance*) or intangible (*motivation and commitment*), and more or less rewarding or costly (*pay and benefits*), between at least two persons (*employee and employer*)"
   ii. Thus, social exchange in the employer-employee relationship is one in which the employer offers inducements (e.g. wages, employee benefits) in return for employee contributions (e.g. performance, commitment)

B. How Employee Benefits Constitute Social Exchange

1. For companies, employee benefits not only offer cost advantages and tax incentives, but also act as a recruitment tool for attracting and retaining desired employees
   i. Employee benefits provide employees with economic and income security, and also with personal and family welfare
   ii. While wages or salary act as a basic remuneration, employee benefits elicit increased motivation and commitment from employees toward company goals
2. The employment relationship can be said to constitute both economic exchange and social exchange
   i. **Economic exchange**, as with wages and salary, is one in which the nature of the exchange has been specified at the time of employment
   ii. Explicit company policies and procedures help ensure that each party fulfills the obligations in the exchange relationship
   iii. Certain employee benefits can fall under the category of economic exchange
      a. For example, health insurance can be viewed in monetary terms, since it costs employers to pay for employees to have health insurance and is usually a part of the explicit agreement at the time of employment
3. Social exchange tends to evolve over the employment period and is not necessarily established at the time of employment
   i. If an employer can provide an employee with benefits suitable to an employee's evolving needs, the employee is likely to reciprocate with increased work effort and commitment
   ii. Hence, employee benefits are an especially relevant component of the social exchange between the employer and employee

C. Workforce Changes and the Employment Relationship

1. Jobs are no longer characterized by traditional job security, strong loyalty to the organization, or the patriarchal role of the organization in the life of the employee
   i. Instead, work arrangements and careers have become more flexible
   ii. There has been an increase in part-time and contingent workers
   iii. Regular layoffs have been taking place, especially in certain industries, such as manufacturing
2. From economic and market challenges, the workforce in the U.S. and other developed economies is becoming increasingly diverse
   i. Several trends have led to this increased diversity

   ii. Exhibit 2.1 illustrates the expected changes in workforce demographics through 2029
3. Traditionally, the design of compensation and benefits packages had assumed a similarity among employees of attitudes, needs, and expectations
   i. Particularly on a white, married, male workforce
   ii. Through the decades, employees developed a strong entitlement mentality, while employers did little to manage these expectations
   iii. Nowadays, companies are shifting some of the costs of benefits to employees
      a. These dynamics can be better understood by becoming familiar with the role of economic challenges facing companies and changing workforce demographics
      b. Both of these will determine the emerging role of employee-benefits practices in the social exchange relationship between employers and employees
4. The cost of benefits is noteworthy, with companies often spending about 30 percent of the total compensation budget on employee benefits
   i. Companies stand to miss opportunities to promote employee satisfaction, commitment, and productivity unless the set of employee benefits is placed in the context of the psychological contract

III. PSYCHOLOGICAL CONTRACTS

1. **Psychological contracts** are an articulation of the exchange relationship between the employer and the employee
   i. A psychological contract has been defined as an employee's subjective perceptions of the relationship of mutual obligations with the employer/company
   ii. Employee benefits can be a part of the psychological contract that employees hold about the employer's obligations to them in exchange for their work efforts
2. Psychological contracts *implicitly* establish terms of employment, which stands in contrast to exchange agreements, such as wage and salary levels
   i. Psychological contracts are not an either-or proposition
   ii. Expectations from the employer fall on a continuum ranging from pay and promotions to career development and family welfare
3. Exhibit 2.2 shows the continuum of expectations encompassed between **transactional psychological contracts** and **relational psychological contracts**
   i. Toward the transactional end of the continuum, employees' expectations from the employer are more economic and extrinsic in nature which translates to expectations of high pay and promotions or career advancement in exchange for hard work
   ii. Toward the relational end, employees' expectations might focus on either economic or non-economic, and these expectations are emotional, subjective, and intrinsic in nature
      a. Employees' expectations of job security in exchange for loyalty to the employer represent relational types of expectations in the psychological contract

b. The main features of the continuum of expectations in psychological contracts can be summarized in Exhibit 2.3

4. Employee benefits practices could fulfill both transactional and relational expectations
   i. Legally required benefits are a part of employees' transactional expectations from the employer
   ii. Employee benefits such as paid time off and accommodation and enhancement benefits examined in the previous chapter might help fulfill employees' relational expectations
5. Some benefits might fulfill both transactional and relational employee expectations
   i. Such as retirement plans, educational assistance or career development
6. Psychological contracts usually change over time
   i. Communication and education about the employee-benefits practices of the company is critical in establishing reasonable employee-expectations, discussed further in Chapter 11

A. Psychological Contract Development

1. Most psychological contracts take shape in the pre-employment phase, when people seek information during recruitment and after receiving a job
   i. Employees might seek information about both transactional and relational expectations from their potential employer
   ii. Ultimately, the knowledge learned will shape expectations along this transactional-relational continuum

2. Employees can form expectations from two sources: interactions with other members of the company and their perceptions of the company's culture
   i. If either source in inaccurate, employees might form unrealistic expectations
3. Psychological contracts are flexible in nature, undergoing constant change based on interactions with the company and with other employees
   i. This flexibility allows employees to adapt to changes in the company's practices
   ii. If employees hold relatively stable expectations, any changes in the policies and practices will lead to the employee feeling betrayed unless changes entail offering more rather less

B. Psychological Contract Violation

1. A violation of the psychological contract occurs when an employee perceives a discrepancy between the promises made by the employer and the actual fulfillment of the promises
   i. If a company withdraws or changes certain benefits, and those practices constituted an employee's psychological expectations from the company, then the employee will feel that the contract has been violated
2. Violations of psychological contracts differ from unmet expectations
   i. The responses to the violation of psychological contracts are likely to be more intense

   ii. Violation of employees' expectations can cause feelings of betrayal and the onset of mistrust
3. There may be two basic causes for violations of psychological contracts: reneging and incongruence
   i. When a company deliberately breaks a promise to employees, either willingly or because of circumstances, reneging is said to occur
   ii. Incongruence occurs when the employee and the employer have different conceptualizations of the employment relationship

C. Employee Benefits as Constituting Psychological Contracts

1. If employee benefits are a part of employees' psychological contract, then it is important for employers to ensure that employee expectations about benefits are clearly articulated and flexible
   i. Violations can be avoided by clear communication and education about the nature and scope of the employee benefits practices offered by the company
2. Just as employees have expectations from the employer, the employer is also likely to have expectations from the employee
   i. If the organization feels that employee performance is not what is expected, it can decide to withhold certain employee benefits, especially discretionary benefits
3. Employee benefits have, over the years, become a growing source of employees' psychological contract violations
   i. Expectations about employees' cost burden, needs, and benefits design will all affect employee satisfaction

IV. EMPLOYEE ATTITUDES AND EMPLOYEE BENEFITS

1. Congruence between employees' and the employer's expectations will lead to greater fit between the employee and the employer as well as a sense of fairness
2. Violations of contracts will lead to perceptions of injustice

A. Justice and Perceived Organizational Support

1. The concept of justice is concerned with the distribution of conditions and goods that affect individual well-being
   i. In a work setting, the distribution of rewards (such as pay and benefits), information, and other resources will all lead to perceptions of justice
   ii. Perceptions of justice may be based on the rules by which distributions are made, the way rules are implemented, or the way decisions are made
2. There are four types of justice perceptions
   i. **Distributive justice** is perceived fairness about how rewards are distributed
   ii. **Procedural justice** is the perceived fairness of processes
   iii. **Informational justice** is the fairness of the accounts given for certain procedures
   iv. **Interpersonal justice** is perceived fairness of the interpersonal treatment people receive from others

   v. Job satisfaction, organizational commitment, evaluation of authority, organizational citizenship behavior, withdrawal, and performance are all affected by employees' perceptions of justice along these dimensions
3. Where employee benefits are concerned:
   i. Distributive justice – employees will form perceptions of fairness based on the benefits they are eligible for
      a. if employees believe the employer should provide them with certain benefits and the employer fails to do so, employees will conclude the employer is being unfair
   ii. Procedural justice – deals with employees' perceptions of fairness of the process by which decisions are made and includes the extent to which employees can participate in the process as well as the rules followed
      a. By establishing rules for eligibility and contributions to retirement plans, employers can ensure procedural justice perceptions
      b. Allowing employees a voice in the use of such benefits can enhance their perceptions of procedural fairness
   iii. Interpersonal justice – is the perception of the degree to which the employer demonstrates concern and social sensitivity toward employees
      a. For example, a manager's awareness and concern for employee development and needs and encouraging employees to participate in the benefits program
      b. Is likely to lead to fairness perceptions about interpersonal justice
   iv. Informational justice – deals with perceptions about the quality of information used to explain organizational decision making
      a. the accuracy and timeliness of information will influence employees' perceptions of informational justice
4. Earlier human resource practices were standardized, today there is a shift toward non-standardized, idiosyncratic work arrangements
   i. Employee benefits can be a part of this new individualized employment relationship
5. **Perceived organizational support** is an employee's perception of the degree to which the employer values the employee's contributions and well-being
   i. Organizational support may implicitly incentivize higher job performance
   ii. Becoming a part of the social exchange relationship
6. Certain employee benefits practices can act to signal organizational support
   i. such as mental health benefits, wellness programs, smoking cessation programs, stress management, as well as those aimed at recognizing the employees' contributions such as recognitions and rewards
7. Certain rewards and job conditions are more likely to lead to perceived organizational support, such as recognition, pay, promotions, job security, autonomy, and training
8. From a social exchange perspective, employees will value the employer's discretionary efforts more highly than those that are beyond the employer's control
   i. Discretionary benefits are more likely to generate perceptions of organizational support than legally required benefits
   ii. The importance of flexible benefits practices, suited to the diverse necessities of the changing workforce, can hence be understood in terms of critical

employee attitudes such as perceptions of fairness and perceived organizational support

B. Organizational Citizenship Behavior

1. Employees' discretionary behavior, not explicitly or directly recognized by the formal reward system of the employer, but in aggregate promoting organizational effectiveness, is termed as **organizational citizenship behavior**
   i. Behaviors such as helping other employees, looking out for the employer's interests, going beyond job requirements to help achieve company goals, are all examples of organizational citizenship behavior
   ii. Satisfied employees engage in good citizenship behavior – a company's employee benefits practices can influence employees' satisfaction
2. Organizational citizenship behavior is discretionary, it is not enforceable but rather a matter of personal choice
   i. If employees perceive their employer as generous and fair, they will seek to reciprocate by showing good citizenship behavior
   ii. In addition to job performance and commitment
3. Employees' perceptions of both distributive and procedural justice are likely to affect citizenship behavior
   i. If employees perceive the employer is unfair, they will withhold good citizenship behavior
   ii. Employee-benefits practices that lead to perceptions of injustice or feelings of contract violations might also lead to
      a. Poor performance
      b. Reduced commitment
      c. Increased turnover
      d. Reduction in extra-role, prosocial behaviors
4. There are two reasons why job satisfaction would lead to organizational citizenship behaviors
   i. It could be because people tend to reciprocate those who benefit them
   ii. Also, employees who are satisfied and experience positive mood states tend to engage in good citizenship behaviors
5. The concept of organizational citizenship behavior is based in social exchange
   i. Employee benefits are an important part of the social exchange process and can be an important component of employees' psychological contract with the employer
6. Based on how companies design, communicate, and implement employee benefits they can lead to varying perceptions of fairness and organizational support
   i. Thus, employees will engage in related organizational outcomes such as job performance, commitment, and citizenship behavior
   ii. The role of employee benefits in eliciting organizational effectiveness is undeniable

V. THE ECONOMICS OF EMPLOYEE BENEFITS: WHY DO EMPLOYERS OFFER BENEFITS?

1. Most employers compensate employees with some combination of cash and benefits, representing the extrinsic component of total compensation
    i. It might seem that employees and employers would both prefer a cash-only compensation package rather than a mix of cash and benefits
    ii. What advantages are there to employers and employees having benefits?
2. An employer might choose to include benefits in its compensation package for three primary reasons:
    i. A cost advantage to the employer
    ii. Recruitment of certain types of workers
    iii. Tax incentives

A. Cost Advantage

1. Benefits, like health insurance are cheaper for the employer to purchase for a group than employees can purchase individually
    i. For example, health insurance costs $1000 per employee, if purchased by employer that employs 500
    ii. Individually, the same policy would cost each employee $2500
    iii. Employees are better off if pay is reduced less than $2500
    iv. The employer benefits if they deduct more than $1000 to provide insurance
    v. Together, this means that both the employer and the employees will be better off if the compensation package includes the health plan and salaries are decreased by an amount between $1,000 and $2,500
    vi. Other benefits that tend to be cheaper when purchased as part of a large group are retirement annuities, disability, and life insurance.
2. Reasons why group insurance rates decrease as group size increases
    i. As the group gets larger, insurance becomes less risky to provide
    ii. The fear of high-risk policyholders driving out the low-risk ones is reduced
    iii. The fixed administrative cost per employee is reduced
3. As the size of the insured group gets larger, it becomes easier for the insurance company to predict the total medical expenses for the group – that means it is less risky to provide insurance to a larger group than to a smaller group
    i. In very large groups, total medical expenses are likely to be close to those predicted by the age, gender, and past medical history of the group
    ii. The number of people with larger-than-expected medical expenses will likely offset those with smaller-than-expected medical expenses
    iii. Because the insurance company bears less risk, they are willing to provide coverage at a lower cost to larger groups
    iv. Individual policyholders and small groups of policyholders may have to undergo **medical underwriting**, a process by which employees provide information on their past medical history in a questionnaire or physical exam
4. The larger the group the less likelihood of **adverse selection**
    i. The condition where the insurance pool attracts only "bad risks" and discourage the participation of "good risks"
    ii. Adverse selection in insurance markets stems from the fact that individuals know more about their own health status than does the insurance company

iii. One solution is for the company to gather as much information as possible about each participant's risk profile and then offer the insurance at a lower price to healthier people and at a higher price to less-healthy people
   a. This is referred to as **experience rating** and is how most auto insurance policies work

iv. Another solution is for a large group of people who come together for some other purpose to buy group insurance together
   a. With the requirement that all group members must buy into the insurance pool
   b. The insurance company can set the premium accordingly without fear that relatively good risks will drop out

v. Avoiding adverse selection is one justification for government-provided insurance programs, like
   a. Social Security
   b. Medicare
   c. Workers' Compensation

5. Finally, administering an insurance policy involves a good deal of paperwork, claims processing, and other administrative functions
   i. Many of these functions are not much more time-consuming and expensive to perform for a large group than for a smaller group, a process referred to as **economies of scale**
   ii. As the group gets larger, the average cost per insured person is reduced

B. Recruiting Certain Types of Workers

1. A second reason employers may want to offer a compensation package that includes both cash and benefits is to aid in recruiting and retaining certain types of employees
   i. In reality, not all information that is important to managers is revealed in a job application, such as the applicant's
      a. Future productivity
      b. Work habits
      c. Career plans
      d. Commitment to the employer
      e. Commitment to undergoing future training
   ii. By offering both cash and benefits that are more highly valued by some applicants, an employer may be able to get applicants to reveal some of these characteristics themselves
2. For example, suppose the ideal candidate is a highly motivated recent college graduate who would like to work for a few years and then go back to school for their MBA
   i. Looking at the job applications, it is difficult to tell which potential employees actually fit the description
   ii. How would the employer go about selecting a candidate?
      a. One strategy is to simply ask each applicant whether they are highly motivated to earn an MBA
         (i) But all the applicants would likely say "yes" if they thought it would increase their chances of getting the job

(ii) Or the potential employee may not know for sure if they want to earn an MBA or may not correctly define "highly motivated"

b. A second strategy is the employer could offer a pay package that includes a slightly reduced salary along with the promise to pay tuition in an MBA program – a **tuition reimbursement benefit**

(i) This package would be valued relatively more by the exact employees whom the employer wants to recruit

3. Offering particular benefits could also have unintended consequences for the types of employees most attracted to the employer
   i. For example, an employer touting its generous benefits for mental health services or substance abuse treatments may be attracting employees suffering from conditions that require such services or treatments
   ii. In some cases, this may not be the outcome the employer intended

C. Tax Incentives

1. A third reason employers may want to offer benefits is that the Internal Revenue Code (IRC) provides financial incentives to do so
   i. Most importantly, many benefits are not taxed as income to employees
      a. For example, an employee is at a 25% tax rate
         (i) If the company raises the employee's salary by $1000, the IRC would get $250
         (ii) If the company gives the employee a health insurance plan that costs $1000, employee receives total benefit without being taxed
         (iii) To buy a $1000 policy, employee would have to earn $1333.33 pretax to pay for it
      b. Retirement plans are also driven by generous tax treatments
2. All three of the preceding motivations presuppose that employees value a particular benefit and are willing to give up something to receive it – there are two important consequences of this
   i. First, employers need to figure out the cash value that employees place on a particular benefit and which types of employees value the benefit more than others
   ii. Second, if employees are willing to give up something to receive a particular benefit, then the cash component of wages and the types and amounts of benefits an employer offers will be inexorably linked

VI. WHO PAYS FOR BENEFITS?

1. One of the biggest misconceptions about employee benefits is that employers give them as "free add-ons" in compensation packages and the employees do not give up anything to receive these benefits
   i. Employees pay for all of their benefits in the form of lower cash wages or salaries then they would otherwise receive
   ii. When the cost of a benefit increases, it is employees who pay for the increase; employers' profits are generally not affected

2. The degree to which an increase in benefits costs is passed along to employees depends on four factors:
    i. The cash value that employees place on the benefit
    ii. The degree to which employers will increase or decrease their hiring when the market compensation level decreases or increases
        a. And the degree to which employees will change their desire to work when the market compensation package changes
    iii. Whether the benefits cost increases for all employers in a market or only for a particular employer
    iv. Whether the hiring decisions of a particular employer affect the market compensation level
3. First, let's define the concept of the "value that employees place on a benefit"
    i. For example, suppose you've accepted a new job and you now have 2 options; a $90,000 salary with no health insurance or $75,000 and a comprehensive educational assistance plan
    ii. Those who want to earn a graduate-level degree will place a relatively higher value on educational assistance programs and willing to forgo the extra $15,000 in salary
    iii. People with a graduate degree are more likely to choose the extra salary in lieu of the educational assistance
4. The lesson is that the greater the value employees place on a benefit, the larger the reduction in cash wages they will accept if the benefit is offered in a compensation package
    i. Suppose an employer wants to add a $10,000 (per employee per year) benefit to employee's salary of $100,000
    ii. Employers could assume the cost, which would reduce profits of $10,000 per employee per year, or reduce pay by $10,000
    iii. Could the company assume the cut in profits and still afford to keep their employees or hire new ones?
    iv. Would the $90,000 salary attract the right workforce?
    v. That depends on the value the employee places on the benefit
        a. There are bound to be some employees who value the plan at less than $10,000 per year and some who value it at more
5. When benefit costs rise for a single employer, the employer will likely not be able to pass along the benefits costs to workers if the workers' valuation hasn't changed
    i. For example, a company offers a competitive total compensation package worth $100,000 ($80,000 in salary and benefits valued at $20,000)
    ii. If benefits costs increase, this is not balanced by an increase in valuation from employees
    iii. The employer must pay the increase in costs
6. What if all employers could agree to pass along the higher benefits cost to employees?
    i. Workers in this scenario have the option of leaving the workforce altogether
    ii. The smaller workforce would force employers to raise their wage offers to fill their staffing needs
    iii. Employers will tend to pay for benefits cost increases

7. Exhibit 2.4 summarizes whether employers or employees will tend to pay for a benefits cost increase in various scenarios
8. Most workers with employer-sponsored health insurance pay a token monthly contribution towards their insurance premium
    i. According to data from the 2020 National Compensation Survey
    ii. Most employees were required to make a contribution toward their health insurance cost
    iii. The typical monthly contribution was ranged between $41 to $245 for single coverage and between $198 and $1,096 for family coverage
9. It may seem peculiar that employers charge employees these monthly contributions but there are advantages
    i. They easily allow employers to charge different prices to people with different family sizes, or to people who choose different plans
    ii. Employers can more easily raise these contributions when benefits costs increase
10. Instead of lowering income employers may also
    i. Scale back a scheduled bonus
    ii. Reduce the yearly income increase
    iii. Hire new workers at a lower income level

VII. Summary

This chapter discusses the psychological basis of employee-benefits practices from the point of view of employees, as well as the economics of employee benefits from the perspective of employers. Taken together, these topics illuminate the importance of offering employee benefits. Psychologically, employee-benefits practices can fulfill employees' transactional and relational expectations of the employer and the employment exchange relationship. If employees view their employer's benefits program as fair and meeting their expectations, then those employees will be satisfied and productive. When employees are satisfied and happy with the way the employer is treating them, they will be committed to the employer and even engage in good citizenship behaviors. Hence, it is important for employers to understand employee perceptions and attitudes about employee benefits. This will allow employers to design and communicate benefits programs that can attract and retain productive and committed employees. The economics of employee benefits explore why employers offer a mixture of cash and benefits and whether workers tend to pay for benefits cost increases in the form of lower cash wages. The primary reasons why employers offer benefits are that they can purchase the benefits at a lower cost than could employees on their own, employers use benefits to attract particular types of employees, and the government gives employers a tax incentive to provide some benefits. Whether workers or employers pay for benefits costs increases depends crucially on why costs increase, whether costs increase for all employers in the market, and how willing employees and employers are able to adjust their labor supply and demand when compensation costs change.

VIII. Discussion Questions

1. Discuss the concept of social exchange as it relates to the employment relationship. How does this concept apply to employee-benefits practices?

   Main Points

   - Employment relationship consists of clusters of human resource practices offered to a group of employees along with the resulting employee contributions to the employer
   - Social exchange in the employer-employee relationship is one where the employer offers inducements (e.g., wages and employee benefits) in return for employee contributions (e.g., performance and commitment)
   - If an employer can provide an employee with benefits suitable to the employee's evolving needs, the employee is likely to reciprocate with increased work effort and commitment
   - Therefore, employee benefits are an especially relevant component of the social exchange between the employer and employee

2. What are psychological contracts? Discuss the main features of psychological contracts and how they develop. Discuss how employees' psychological contracts might be violated and the consequences of these violations for employers.

   Main Points

   - A psychological contract has been defined as an employee's subjective perception of the relationship of mutual obligations with the employer and company
   - Psychological contracts result in employees holding a range or continuum of expectations from the employer, ranging from pay and promotions to career development and family welfare
   - The continuum of expectations have two ends: transactional psychological contracts and relational psychological contracts
   - Toward the transactional end, employees' expectations are more economic and extrinsic in nature
   - On the other hand, toward the relational end, employees' expectations might be either economic or non-economic, but are also emotional, subjective, and intrinsic in nature
   - Most psychological contracts take shape in the pre-employment phase, when people seek information during recruitment and selection
   - Employees can form expectations that comprise their psychological contracts from two sources: their interactions with other members and their perceptions of the company's culture
   - Psychological contracts are flexible, undergoing constant change based on the interactions
   - A violation of the psychological contract occurs when an employee perceives a discrepancy between the promises made by the employer and the actual fulfillment of the promises

- Violation of employees' expectations can cause feelings of betrayal and the onset of mistrust
- There are two basic causes for violations of psychological contracts: reneging and incongruence
- When a company deliberately breaks a promise to employees, reneging is said to occur
- Incongruence violations occur when the employee and the employer have different conceptualizations of the employment relationship

3. How do perceptions of employee-benefits plans influence organizational justice and organizational citizenship behavior?

   Main Point

- There are four types of justice perceptions: distributive, procedural, informational, and interpersonal
- Distributive justice is employees' perceptions of fairness of the outcomes they receive
  - If an employee perceives an employer as being unfair, they might withhold effort and lower their commitment to the employer
- Procedural justice deals with employees' perceptions of fairness of the process by which decisions are made and includes the extent to which employees can participate in the process as well as the rules followed
  - Establishing rules for eligibility and contributions to retirement plans, employers can ensure procedural justice perceptions
  - Allowing employees to have voice in the use of benefits can also enhance their perceptions of procedural fairness
- Interpersonal justice is the perception of the degree to which the employer demonstrates concern and social sensitivity toward employees
  - A manager's awareness and concern for employee development and needs is likely to lead to fairness perceptions about interpersonal justice
- Informational justice deals with perceptions about the quality of information used to explain organizational decision making
  - If a company intentionally or unintentionally fails to inform employees about a benefit's elimination or change, employees may judge the decision as unfair
- Organizational citizenship behavior is discretionary
  - Employees' perceptions of both distributive and procedural justice likely affect citizenship behavior
  - Perceptions of injustice or feelings of contract violations might lead to poor performance, reduced commitment, increased turnover, extra-role reduction, and reduction of prosocial behaviors
  - Employee benefits are an important part of the social exchange process and an important component of employees' psychological contract with the employer

4. One reason employers offer benefits is that the benefits may be cheaper for the employers to provide than it would be for the employees to purchase on their own.

Even if a particular benefit is cheaper for an employer to provide, would that employer always want to provide it? Why or why not?

Main Points

- Even if a particular benefit is cheaper for an employer to provide, employers would not always want to provide it as part of a compensation package for variety or reasons
- For instance, offering mental health services or substance abuse treatment might be cheaper for the employer to purchase similar to health insurance plans
- However, the employer might also find that the types of employees who are most likely to accept a position, or most likely to stay at the employer, are those suffering from these conditions
- Employers would like to attract and retain certain types of employees and therefore, they would want to design their benefit packages based the needs and preferences of their current and potential employees
- It does not make sense for the employer to provide benefits just because they can purchase it cheaper

5. A major theme of this chapter is that employers need to know the dollar value that employees place on benefits. Explain concisely why this type of information is important for employers to have. What methods do employers actually use to gauge their employees' valuation of benefit packages?

Main Points

- The greater value employees place on a benefit, the larger reduction in cash wages they will accept if the benefit is introduced into a compensation package
- For instance, an employer can understand their employees' valuation of benefit packages by offering two choices for a newly hired employee
- In the first choice, let's say the employer provides $75,000 annual salary plus a comprehensive health care plan, and as a second choice the employer offers a $90,000 annual salary without a health care plan
- Those who tend to use health services more frequently and more risk averse will tend to place a relatively higher value on the health insurance plan, and are therefore, more likely to forgo the extra $15,000 in salary
- On the other hand, healthier people and those willing to bear more financial risk are more likely to choose the extra salary
- Similarly, if the choice was between a $75,000 salary plus the health plan vs $100,000 salary and no health plan some employees who would have opted for the health insurance in the first situation would now choose the higher salary instead
- Here, employees prefer $25,000 in cash to health insurance provided by the employer
- This type of decisions of employees helps employers to understand their employees' valuation of benefit packages

IX. Cases

Cutting Costs at Builders Manufacturing

1. Do you think the company should reduce the contributions to the retirement plan?
2. How do you think the employees will react to such a reduction in their benefits?

Instructor Notes

Employers offer benefits to employees for many reasons. An employer is able to offer benefits such as health insurance or retirement plans at a lower cost than if the employee would purchase the benefit on their own, and thus the benefit becomes of more value in the compensation package. Employee benefits can also attract certain kinds of workers and offer tax incentives for employers. As most employers now offer benefits such as a retirement savings plan, an employer will also consider competitor offerings when establishing a benefit plan. For these reasons, benefits can offer a different value in the total compensation offered to an employee.

Student Responses

1. Do you think the company should reduce the contributions to the retirement plan?

   The retirement plan is a discretionary benefit and, due to the generous nature of this particular benefit, the one carrying the most cost for the company and therefore the benefit most likely to be the target of necessary cuts. Some students may feel the cuts should be made in order to keep the company operating. There will be no retirement at all if the company cannot survive until the industry rebounds. Other students may feel the cuts will lead to employee mistrust and the company cannot afford to have an unhappy workforce. Students may suggest making the cuts temporary and educating the workforce about the financial needs for the cuts.

2. How do you think the employees will react to such a reduction in their benefits?

   The employee's reaction to the reduction will depend on how the company communicates the need for the reduction. Employee benefits are an especially relevant component of the social exchange between the employer and employee. Retirement plans fall in the middle of the continuum of employee expectations, carrying both extrinsic and intrinsic expectations. Though psychological contracts are flexible in nature, this reduction in company contributions can lead to employees' feeling betrayed and perceiving the company as reneging on their promise. The reduction may trigger perceptions of distributive justice throughout the workforce and lessen their perceived organizational support. The company's best line of defense is to offer clear communication and education about the reduction and the necessity of the reduction to keep the business afloat. If the cuts are temporary until the industry rebounds and the employees understand the reason behind the cuts, the company and the employees may weather the crisis together.

Cutting Benefits at Generals Construction

1. Does Jane have a valid concern?
2. What kind of changes could the company make to benefits to address Jane's concerns?

Instructor Notes

When designing benefit plans, organizations are challenged to balance economic needs with the expectations of employees. In this case, based on the psychological contract that the employees have with the company, these cuts could make the employees feel that their expectations were violated. Such cuts are particularly challenging when the company is doing well financially. It will be difficult for workers to understand the need of such cuts. Newer companies often make decisions about benefit offerings without taking a long-term outlook. Creating a generous benefit package can attract needed workers, but employers should be cautious and only offer benefits they can sustain.

Student Responses

1. Does Jane have a valid concern?

   Yes, Jane does have a valid concern. Generals Construction has a psychological contract with its employees regarding their benefits. During the hiring process, and over the first ten years, the employer offered a generous benefit package to attract and retain employees. In turn, the employees expected those benefits to be a continuing part of the employment relationship. A violation of the psychological contract occurs when there is a discrepancy between what was promised and the actual fulfillment of those expectations. While the employer likely did not have a written contract promising the continuation of the benefits, the fact that they were offered for ten years suggests to the employees that they will continue. This is particularly true as the company is continuing to succeed and grow. Now that the company is stable, the employees will react negatively to such a cut in benefits. They are likely to feel betrayed and distrustful. They might be willing to accept the changes if the company was in a downturn. Further, cutting the benefits of the construction workers and not the others is likely to have an even more problematic effect on company morale.

2. What kind of changes could the company make to benefits to address Jane's concerns?

   The employees in this case may have an unrealistic expectation of what the company should provide them, but that expectation was established based on the company providing them the benefits consistently over an extended period of time. If the company wants to shift employee expectations, it needs to do so gradually as well. Shifting some of the burden of the cost of health care insurance to employees would not be entirely unacceptable. However, those changes should be more gradually. It would be wise to begin with giving a smaller portion of the premium to the employees. While they might charge a little more for employees who have coverage for their full family, they should not cut their support entirely. Further, cutting a vacation benefit that the employees have grown accustom to having is not something that the employees will accept readily. The company could change the new hire vacation allowance, however, the negative impact of cutting only the construction worker vacation would likely result in the loss of workers. Jane should take some time to review all benefits offered by the company to understand utilization rates. For example, if the company offers vision insurance and only a few employees use it, they could consider cutting the vision insurance. They could also examine expenses in other areas of employee management that they could cut.