Retirement plans in the voluntary sector

Background
Access to retirement or pension benefits for employees of voluntary sector organizations (VSOs) is a major issue that needs to be addressed. In a sector already finding itself less competitive against other labour market sectors, VSOs have to rely on personal values as incentives to recruit and retain employees. This “in it for the work” thinking is fast losing its lustre as the workforce ages and employees find themselves having to consider their income needs in later life.

And this issue becomes more critical as the sector begins to recruit the next generation of younger workers. The “popular culture” notion that there will not be a public pension fund to take care of their income needs when they age has, by all indications, made them far more aware about the need for retirement income, and has set access to this kind of benefit in their workplace as a very high priority.

According to a survey of non-wage benefits in Canada by sector (Workplace and Employee Survey 1999), 17.5% of employers in the non-profit sector provided an employer-sponsored pension plan while 10.4% provided a Group RRSP. This is significantly fewer, by a margin of as much as 50 percent, than the number of participating private sector and broader public sector employers. The figure varies further depending on whether the agency is unionized or not. This exacerbates already significant compensation shortfalls so prevalent in the sector.

It is important to understand the distinctions between the two major types of pension plans and the differentiation between pension plans and RRSPs. For clarification:

- Defined Benefits Pension Plans provide retirement income to employees based on some pre-determined calculation or formula, most typically involving some combination of years of service and contributory income. Employers who sponsor these plans are liable for adequately funding the plans to ensure that benefit recipients receive their payouts for the full duration. In times where the investment environment does not provide sufficient returns on the invested assets of the pension plan, the employer must still fund the payments to pensioners.

- Defined Contribution Pension Plans are based on the employer, often with employee participation, contributing an amount into a plan. The benefit from the plan is dependant on the plan’s investment performance. If the plan’s investment performance is poor, the employer has no obligation to make additional payments.

- Group RRSPs are not, technically speaking, pension plans. They are employer-sponsored vehicles for employees to invest in RRSPs, often with matching funds from the employer. Occasionally, an employer may fully fund contributions. Group RRSPs give the employee the advantage of pre-tax contributions directly from payroll deductions, lower commissions and administration fees paid by the employer. The last two items, which may be scaled down as the investment pool grows, or, as in the case of administration fees be paid wholly by the employer, ensure that a larger amount of the employee’s contributions are left for investment and growth, when compared to an individual RRSP.
Interestingly, where retirement plans exist in the Voluntary Sector, there are 68% more Defined Benefit plans than Defined Contribution plans and Group RRSPs. These are typically plans established many years ago. Any plans established in the past few years have tended to be Defined Contribution. In addition, fewer employers in the Voluntary Sector have been prepared or able to offer this option at all in the recent past.

It should be noted here that some VSOs have made a practice of providing funds directly to an employee for investment in the employee’s individual RRSP. We recommend against this option as we see this practice as not being tax efficient for the employee and as having a deleterious effect on their retirement fund. The funds are provided to the employee as income therefore immediately triggering taxes and payroll costs on the entire amount. The contribution by the employee to the RRSP is made in after-tax monies. While the tax position on these funds are reconciled when the individual files their tax return for the year, the lower net payment results in a significantly lower amount being available for investment. The compounding effect of this, over time, can have an enormous impact on the employee’s retirement fund.

Over the past several years, as the investment markets have turned downward, pension plan assets have followed suit. Data from Statistics Canada released in December 2002 indicate that two-thirds of all pension plans are in the red and pension plan assets in Canada have been reduced from $614 billion to $541 billion between the years 2000 and 2002. Regardless, organizations with Defined Benefit plans must come up with the cash to fund the pensions of their past employees.

Over the past years, this has made Defined Benefit plans very unattractive from an employer’s point of view and there has been a rush to Defined Contributions. From an employee's point of view, having access to a guaranteed benefits formula under Defined Benefits would appear far more attractive than betting on the vagaries of the stock market in order to fund retirement when the market is performing badly. There will always be this tension between employers’ and employees’ interests. There is, or rather there should be, one over-riding common interest however... providing a reasonable retirement benefit that secures the employee’s future and builds loyalty and motivation to stay.

Issues

Issues preventing employees in the non-profit/voluntary sector from accessing adequate pensions are similar to the impediments in other employee benefit areas.

- Affordability: Agencies are unable to budget for pension contributions.
- Employment: Temporary or contract employees are often not considered eligible by employers for participation in pension plans. Many agencies have “permanent” staff who fall into this category. It should be noted that the practice of issuing term contracts for employees based on project funding does not override the “permanent” status of an employee under labour law who may have had multiple contracts with the same VSO over a period of years, based on funding patterns.
- Funders: Funders do not fund pension (or Group RRSP) contributions, and project-based funding encourages the use on non-permanent staff.
- Employee Affordability: Employees are often unable to make payments to employer-sponsored RRSPs and, therefore, do not trigger employer contributions.
- Employer Knowledge: Employers are unaware of options or are unable to explore options fully because of lack of knowledge (e.g., the tax and
investment implications of providing RRSP contributions directly to employees in the example provided previously).

- **Employee Knowledge:** Employees with no or small RRSPs are unaware of the risk they may already face even twenty plus years away from retirement. While there is certainly flexibility in a Group RRSP, for example with respect to transferring RRSPs from one employer to another or into a private account, often employees may not have been appropriately informed so as to understand how their plan works and how to make the best of it.

- **Pension Industry:** Pension plan management and investment firms are not motivated to sell into the sector because of the lower proportion of individual wealth found there. While investment firms will certainly take on the business of a VSO’s Group RRSP (see the last paragraph under the section “Challenges”), it is important to keep in mind that the individuals who make up these plans are typically not high-income earners.

Investment advisors often see Group RRSPs as a way of capturing the business of the individual contributors and “high net worth” individuals are more likely to be found in private sector plans.

A significant risk factor with respect to employees’ retirement income is the fact that employers who sponsor Group RRSPs are not compelled to contribute. And, of course, neither are employees. VSOs may offer the Group RRSP approach but there is nothing compelling them to make their plans work.

Multi-employer pension plans (like OMERS1 in local government) are almost non-existent in the non-profit sector. One Defined Benefit plan we are aware of that has operated in the Toronto area for a number of years is now in peril and may shortly be dismantled due to liability issues. Members of an association of health organizations in Ontario have the option of joining a hospital sector plan. Other groups may have other options, but these would be in the minority.

**Challenges**

Of course the ever-present challenge is funder “buy-in” and participation. To properly fund a retirement plan, whether a full pension plan or an RRSP, even when the employee makes contributions, requires financial input and resource management on the part of the employer, and by default, the funder.

Having said all this, it should be acknowledged that where a VSO chooses to go down this road and has the financial wherewithal to do so, finding providers is less daunting than with respect to Employee Group Life, Disability and Health benefits. For the provider there is no risk associated with receiving these funds for investment.

One of the most significant challenges encountered by VSOs is that as not-for-profit entities they are significantly limited in the way they can approach and fund retirement for their employees. As non-profit corporations they are unable to use the tax laws optimally to fund

The Ontario Municipal Employees Retirement System is the pension plan for almost 327,000 current and former employees of municipal governments, school boards, libraries, police and fire departments, children’s aid societies and other local agencies throughout Ontario these plans. While private sector corporations have more alternatives, the only options available to VSOs are to provide traditional defined benefits or defined contribution pension plans, or RRSPs.
Sponsor accountability is another significant challenge. VSOs that have chosen to offer a retirement benefit in the past few years have almost universally offered Group RRSPs. Even where all the contributions emanate from the employees, this limited program does not relieve the VSOs of a number of obligations. The most significant of these are administration and communication.

Sponsors offering Group RRSPs must be aware that they have responsibilities for making payroll deductions and remitting them to the plan provider in a timely fashion. Administration also requires the completion and submission of appropriate documentation. Communication and education are crucial activities, and VSOs have the ongoing responsibility to raise their employees’ awareness and orient them to the Group RRSP.

There is a developing trend in the United States and current literature is beginning to indicate that fully transferring the onus for investing onto the employee in their version of Group RRSPs may not be acceptable, and that this may, in fact, represent a breach in the organization’s fiduciary responsibilities for which they may be held liable in the future. Employers (and VSOs, as may be the case) in this model must provide education and support and must promote participation when offering plans.

In addition to all of the above, monitoring the service levels of the provider against the Service Level Agreement is a responsibility of the plan sponsor, and VSOs must consider their capacity to follow through.

**Conclusions and observations**

Pensions represent a large compensation gap in the sector. Affordability may be one of the main issues but dealing with knowledge gaps as well as rigorous adherence to plan growth by employees and employers alike can maximize what is available. The simple principles of paying oneself first, making ongoing investments and dollar cost averaging can be applied to greatly impact retirement fund outcomes.

While funding does not often accommodate pensions or retirement benefits, joining existing plans or pooling for maximum effect, and to control management and administration fees can be an option for some agencies or groups of agencies.

For larger organizations, with sufficient funding to move forward on their own, there are no real obstacles, although their options to act are more limited than for organizations in the private sector. For very small VSOs there are some multi-employer Group RRSPs available in the nonprofit marketplace that may be an appropriate solution.

It is observed that even in the event that a small VSO is unable to provide employer-funded retirement benefits some options do exist. Providing access to a fully employee-funded Group RRSP is always an option, where regular deductions are made from payroll and where, through small contributions over time, in conservative vehicles with the effect of compounding, at least some future income can be set aside. Even this option would be a major step forward, and one that VSOs should consider acting on.