Retirement plan awareness

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In addition to wages, many employees receive benefits such as dental, life or supplemental medical insurance plans. Employer-sponsored retirement plans—registered pension plans (RPPs), group RRSPs and deferred profit-sharing plans—are another key component of total compensation.

During the mid-1990s, firms were thought to be moving from defined-benefit registered pension plans toward defined-contribution arrangements—particularly group RRSPs—because RPPs were more costly to administer and subject to substantial regulation. While subsequent examination showed the death of defined-benefit plans to be greatly exaggerated (Frenken 1996), the growing popularity of group RRSPs presents employees with a greater variety of employer-sponsored retirement plans than in the past.

But, can all employees make the distinction between RPPs and group RRSPs? How many think they have a RPP even though their employer does not provide one? How many mistakenly think they have a group RRSP? Most important, how many think they have at least one of the two but, in fact, have neither?

Accurate information about one's employer-sponsored retirement plan is crucial in deciding the timing of retirement, the role personal savings will play, and the allocation of one's portfolio between safe and risky investments. Such information is especially important since, contrary to many RPPs, group RRSPs require workers to decide whether to participate and if so, how much to contribute.

Using the Workplace and Employee Survey (WES), this article first reviews trends in RPP coverage over the last decade and provides estimates of workers with group RRSPs (see *Data source*). It then examines how well full-time permanent employees in the private sector understood their coverage in an employer-sponsored retirement plan in 2001.[1]

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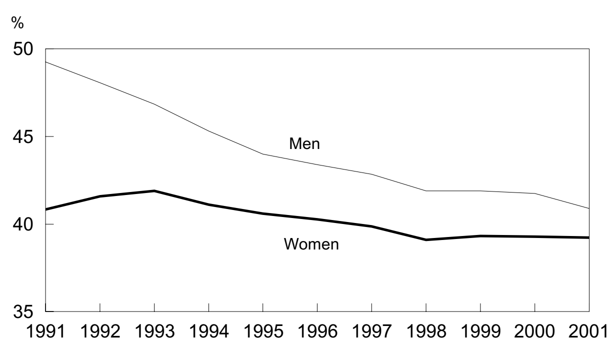
Trends in RPP coverage

In Canada, the retirement plans most commonly offered by employers are registered pension plans (RPPs), group registered retirement savings plans (group RRSPs), and deferred profit-sharing plans (DPSPs). Registered pension plans are by far the most popular. While information on DPSPs is limited, the available evidence suggests participation in them is fairly low—only 350,000 workers in 1993 compared with 5.2 million who had RPPs (Frenken 1995).[2]

According to the Pension Plans in Canada Survey, at the end of 2001 about 5.5 million employees—representing 40% of all employees, including those in the public sector—had an RPP in their job (Chart A). This percentage was down from 45% in 1991.[3] Among men, coverage fell 8 percentage points to 41%; for women the drop was much less—from 41% to 39%.

Chart A: After declining through most of the 1990s, RPP coverage stabilized.



Source: Pension Plans in Canada Survey

These numbers hide diverging trends between younger women (aged 25 to 34) and prime-aged women (aged 35 to 54). Between the mid-1980s and the late 1990s, RPP coverage increased among prime-aged women but fell among young women (Morissette and Drolet 2001). In contrast, both younger men and prime-aged men saw their percentage fall.

Group RRSPs

While anecdotal evidence suggests that group RRSPs are becoming more popular, information on employee participation is difficult to obtain from survey data since many workers do not appear to have a clear understanding of what constitutes a group RRSP.

In 2001, 2.1 million private-sector employees reported having a group RRSP in their job (Table 1). However, fully half a million were employed by firms having *no* group RRSPs. Only 1.6 million employees, representing 14% of the private-sector workforce, reported having a group RRSP *and* were in firms offering group RRSPs to at least some employees.[4]

Among workers who reported having a group RRSP but were in firms that did not have one, fully two-thirds had an employer that offered an RPP to at least part of the workforce. This suggests that many workers confuse group RRSPs with RPPs.[5] It is unlikely that the discrepancy originates from employers not reporting a group RRSP even though they have one in the workplace—for several reasons. First, employers must negotiate administration fees and investment returns with financial institutions when they sponsor group RRSPs. Second, they must make automatic payroll deductions for employee contributions. Third, employer contributions to group RRSPs are treated as earnings and hence are subject to all payroll deductions. Taken together, these factors strongly suggest that employers who offer group RRSPs are fully aware that they do so.[6]

Furthermore, employers are likely to have a clear understanding of the distinction between RPPs and group RRSPs. First, unlike group RRSPs, RPPs are subject to federal or provincial regulatory legislation. Second, employers must pay for actuarial services for defined-benefit RPPs. Third, employer contributions to RPPs are not considered part of an employee's earnings and so are not subject to payroll taxes (see *Features of RPPs and group RRSPs*).

Workers' knowledge of retirement plans

Be it RPP or group RRSP, as long as workers have some type of retirement plan, they will probably not suffer serious consequences as long as they have a clear understanding of its generosity. More serious concerns could eventuate if workers think they have an RPP or group RRSP but their employer provides neither.

In 2001, about half of full-time permanent employees in the private sector reported having an RPP or a group RRSP (Table 2). However, 8% of them were working for firms having neither type of plan. This means that 4% of full-time permanent employees in the private sector (390,000) thought they had a retirement plan but didn't.

Workers who have been in a company for only a short time and are not familiar with the fringe benefits may have a poorer knowledge of their retirement plans than those with more seniority. This likely explains why almost 20% of employees with less than two years of seniority who reported at least one retirement plan worked for firms reporting no retirement plans. The corresponding proportion is at most 7% among employees with 10 or more years of

Table 1: Employees reporting a retirement plan in their job

	'000	%
Employees in private sector	**11,605**	**...**
Report participating in a group RRSP	**2,079**	**100.0**
In firms offering group RRSPs to some employees	1,570	75.5
In firms offering no group RRSPs	509	24.5
Offering RPPs to all full-time permanent employees	327	15.7
Offering RPPs to some employees	20	1.0
Offering no RPPs	162	7.8
Report participating in a RPP	**4,440**	**100.0**
In firms offering group RPPs to some employees	3,707	83.5
In firms offering no RPPs	732	16.5
Offering group RRSPs to all full-time permanent employees	364	8.2
Offering group RRSPs to some employees	45	1.0
Offering no group RRSPs	323	7.3

Source: Workplace and Employee Survey, 2001

Data source

The sample of 17,061 permanent full-time, private-sector employees used in this study was drawn from the 2001 **Workplace and Employee Survey** (WES). WES consists of both employer and employee components. Employers are sampled by physical location—the statistical unit that comes closest to the concept of a workplace in which employer and employee activities can be linked. Employees are then sampled within each location using employer-provided lists. WES covers all industries except farming, fishing, hunting, trapping and public administration.

Employees were asked if their employer offered any non-wage benefits, such as a pension, life insurance, or dental plan. Those answering yes were then asked if they participated in an employer-sponsored pension plan. The question stated that this did not include C/QPP or group RRSPs. The next question specifically asked if they participated in a group RRSP.

Employers were asked if they offered any non-wage benefits—health-related, pay-related, or pension-related. The examples given for pension-related benefits were pension plans and group RRSPs. They were then presented with a list of non-wage benefits and asked to indicate which were not available, available to all, available to non-management non-union employees, or available to non-management union employees.

seniority. In fact, low seniority explains why young workers appear less informed about their retirement plans than their older counterparts.[7]

University graduates, unionized workers, workers in large establishments, and those employed in finance and insurance, and communication and other utilities appear to be better informed than other workers. Among those who reported having a retirement plan, at most 3% were in firms providing neither RPPs nor group RRSPs.

Recent immigrants

Of the one-third of recent immigrants (those who arrived in 1991 or later) who reported having an RPP or a group RRSP in their job, 27% worked for employers who did not provide a plan. This means that 9% of all recent immigrants reported, contrary to their employer, that they had at least one retirement plan—a proportion twice as high as observed among Canadian-born workers.

Table 2: Workers reporting at least one retirement plan

	Total	No plan in firm
	%	
Both sexes	**51.1**	**8.2**
Men	52.0	9.0
Women	50.0	7.2
Age		
Less than 25	22.3	17.5
25 to 34	46.0	11.1
35 to 44	50.4	9.1
45 to 54	63.3	5.5
55 and over	55.6	5.0
Seniority		
Less than 2 years	26.8	19.0
2 to 5	42.2	11.8
5 to 10	53.2	7.5
10 to 20	64.8	6.5
20 or more	76.6	2.2
Education		
High school or less	39.4	10.7
Some postsecondary	49.6	12.1
Postsecondary certificate/diploma	55.1	7.8
University degree	64.7	2.8
Immigration status		
Canadian-born	51.6	7.2
Arrived 1991 or later	32.9	26.7
Arrived before 1991	54.2	9.2
Union status		
Non-member	40.8	12.3
Member	77.6	2.7
Region		
Atlantic provinces	54.4	4.0
Quebec	46.9	7.7
Ontario	53.9	8.7
Manitoba	60.6	5.9
Saskatchewan	56.9	3.9
Alberta	44.3	7.0
British Columbia	47.9	11.7
Employer characteristics		
Single location	38.1	15.2
Multiple locations	70.5	2.4
1 to 19 employees	21.2	29.2
20 to 99	44.7	14.5
100 to 499	64.7	3.6
500 or more	85.4	0.4
Manufacturing	52.3	8.2
Other goods	44.4	12.4
Finance and insurance, and communication and other utilities	72.8	0.7
Transportation, warehousing, wholesale and retail trade, and consumer services	35.6	17.4
Other services*	60.5	4.8

Source: Workplace and Employee Survey, 2001
** Real estate, rental and leasing operations, business services, education and health, information and cultural industries.*

Features of RPPs and group RRSPs

Employer contributions are mandatory for RPPs, optional for group RRSPs.

Employers offering an RPP are required by law to contribute to it. In contrast, those offering a group RRSP may choose not to contribute—although the concept of employer contributions to group RRSPs is not well defined.

A group RRSP is simply a collection of individual accounts set up through the employer. The employer may put a certain amount of money into the plan for each contributor, or may contribute nothing and simply collect the employee contributions through payroll deductions. In either case, the employer will contract a financial institution (for example, a mutual-fund company) to invest the funds.

Because the federal Income Tax Act recognizes only contributions made by employees, employers contribute indirectly by increasing an employee's pay and then contributing the increase to the group RRSP through payroll deduction. The amount contributed by the employer is recorded on the employee's T4 slip as employment income. The employee can then claim the contribution as a tax deduction.

For instance, suppose Employee A is paid $40,000 per year and offered the chance to contribute 5% of her salary to a group RRSP to which the employer also contributes 5%. If she agrees, her pay will be increased from $40,000 to $42,000, and then $4,000 deducted (the employee contribution of $2,000 and the pay increase of $2,000) for investment with a financial institution. Employee A will report employment income of $42,000 and claim a deduction of $4,000 when filing her tax return.

Workers with the same employment income will have the same opportunity to prepare for retirement.

As long as the employment income shown on the T4 is the same, workers in firms offering a group RRSP but not contributing to it will have the same opportunity to prepare for retirement as their counterparts in contributing firms.

Compare the situation of Employee A to that of Employee B, paid $42,000 but employed in a firm offering a group RRSP but not contributing to it. If Employee B decides to put $4,000 into this group RRSP (the amount invested in the account of employee A), he can claim the amount as a tax deduction while also reporting $42,000 of employment income.

The same reasoning can be applied to Employee C, also paid $42,000 but employed in a firm offering no retirement plan. Employee C saves $4,000 per year in an *individual* RRSP and gets the same rate of return as employees A and B who have group plans. (This may not always be the case, since the employers can sometimes bargain with financial institutions for better rates of return.) Employee C would be as well off as A and B.

Contrary to defined-benefit RPPs, group RRSPs do not guarantee workers a certain level of income at retirement.

At the beginning of 2000, about 85% of workers with an RPP had a defined-benefit plan. In the absence of business failure, most of these RPPs guarantee workers a certain retirement income, which usually increases with years of service and pay. In contrast, group RRSPs, like defined-contribution RPPs, provide a retirement income that depends on the rate of return in the financial markets—which is subject to fluctuation.

Consequently, *if* they enjoyed high rates of return on their savings while they were in the labour market, workers in group RRSPs—like those in defined-contribution RPPs—could (but would not necessarily) end up with a higher retirement income than those in defined-benefit RPPs.[8] They could also end up with a lower retirement income if the financial markets performed poorly.

Employees in defined-benefit RPPs also face some uncertainty regarding their retirement income.

While not subject to the investment risk faced by workers with group RRSPs, employees in defined-benefit RPPs who are laid off face some uncertainty regarding the level of income they will receive at retirement. Employees who spend their career with the same employer and have defined-benefit RPPs know in advance what their retirement income will be. However, if they are laid off they could end up with a lower retirement income than anticipated, if their benefits cannot be transferred from one plan to another.

To illustrate, suppose Mr. X works for the same employer for 35 years, earning $40,000 a year for the first 15 years and $80,000 for the last 20 years. If he belongs to a defined-benefit RPP that pays a benefit equal to 2% per year of service, based on average earnings during his last five years, Mr. X will have a retirement income of $56,000 a year.

However, if Mr. X is laid off after 15 years and immediately finds a new job paying $80,000 that he keeps for the next 20 years, he will end up with a retirement income of only $44,000 if the benefits of his first plan are not portable. He will receive $12,000 from his first RPP (.02 x 15 x $40,000) and $32,000 from his second RPP (.02 x 20 x $80,000).[9]

In a group RRSP, the employee never loses employer contributions after leaving the firm.

Before the mid-1980s, workers with RPPs who were contemplating leaving a company had to think twice. If they quit, they would possibly not be entitled to their employer's contributions until age 45 and after 10 years of service. If they left before this period (the vesting period), they would receive only their own contributions, albeit usually with interest. Some firms did, however, offer better vesting rules.

During the mid-1980s and early 1990s, pension legislation was modified so that employees changing jobs were generally entitled to their employer's contributions after two years of service.[10]

In a group RRSP, an employee never loses employer contributions. The money (from both employer and employee contributions plus return on investment) can be transferred to an individual RRSP. The ability to collect employer contributions even after a short stay in a company (less than two years) may be attractive for highly mobile workers.

This discussion draws heavily on Cohen and Fitzgerald (2002), who provide an excellent survey of the various retirement programs in Canada.

Why are recent immigrants less informed about their retirement plans? Differences in educational attainment can be ruled out since recent immigrants are more educated than their Canadian-born counterparts (Table 3). Lower seniority and under-representation in large establishments (500 or more employees) and in unionized jobs, where the incidence of misinformation appears to be minimal, may explain part of the difference. However, even after controlling for these differences and other factors, at least 70% of the difference between recent immigrants and Canadian-born workers remains.[11]

What explains the remaining difference? Despite their fairly high educational attainment, recent immigrants may have an imperfect knowledge of the labour market institutions in Canada. For instance, since they contribute through payroll deductions to the Canada or Quebec Pension Plan (C/QPP), some may think that these retirement plans are employer-sponsored. The data support this view. Among recent immigrants who reported having an RPP in their job, a solid 53% were in firms with no RPPs (Chart B). The corresponding numbers for Canadian-born workers and older immigrants were 15% and 20% respectively.

A key issue then is whether recent immigrants have realistic expectations about the fraction of employment income that C/QPP will replace at retirement. Whatever the underlying factors, the consequence is that almost 1 recent immigrant in 10 appears to be seriously misinformed about their coverage in an employer-sponsored retirement plan.[12]

Conclusion

Given the increasing popularity of alternative retirement plans such as group RRSPs, assessing employee awareness of their coverage by some type of retirement plan in their job becomes more important. This is particularly true since group RRSPs, contrary to many RPPs, require workers to decide whether to participate and, if so, how much to contribute.

Unlike their employers, many workers do not have a clear understanding of the distinction between RPPs and group RRSPs.[13]

While only 4% of all full-time permanent employees in the private sector reported an RPP or group RRSP while being in a firm reporting neither, the corresponding proportion was twice as high among immigrants who arrived in Canada in 1991 or later. In fact, one in four recent immigrants who reported at least one type of employer-sponsored retirement plan in their job was actually working for a firm providing neither an RPP nor group RRSP.

In 1999, about one-third of families with a major income recipient aged 45 to 64 and still working had not saved enough to replace two-thirds of their income at retirement (Statistics Canada 2001). While savings insufficient to provide adequate income at retirement may result from income constraints, the misconception of having a private retirement plan may also be a contributing factor. To address this issue, it is important to emphasize differences between RPPs, group RRSPs and C/QPP and to provide workers with accurate information about the coverage and characteristics of their retirement plans. In this way, chances are increased that employees will make sound decisions about savings, consumption and retirement.

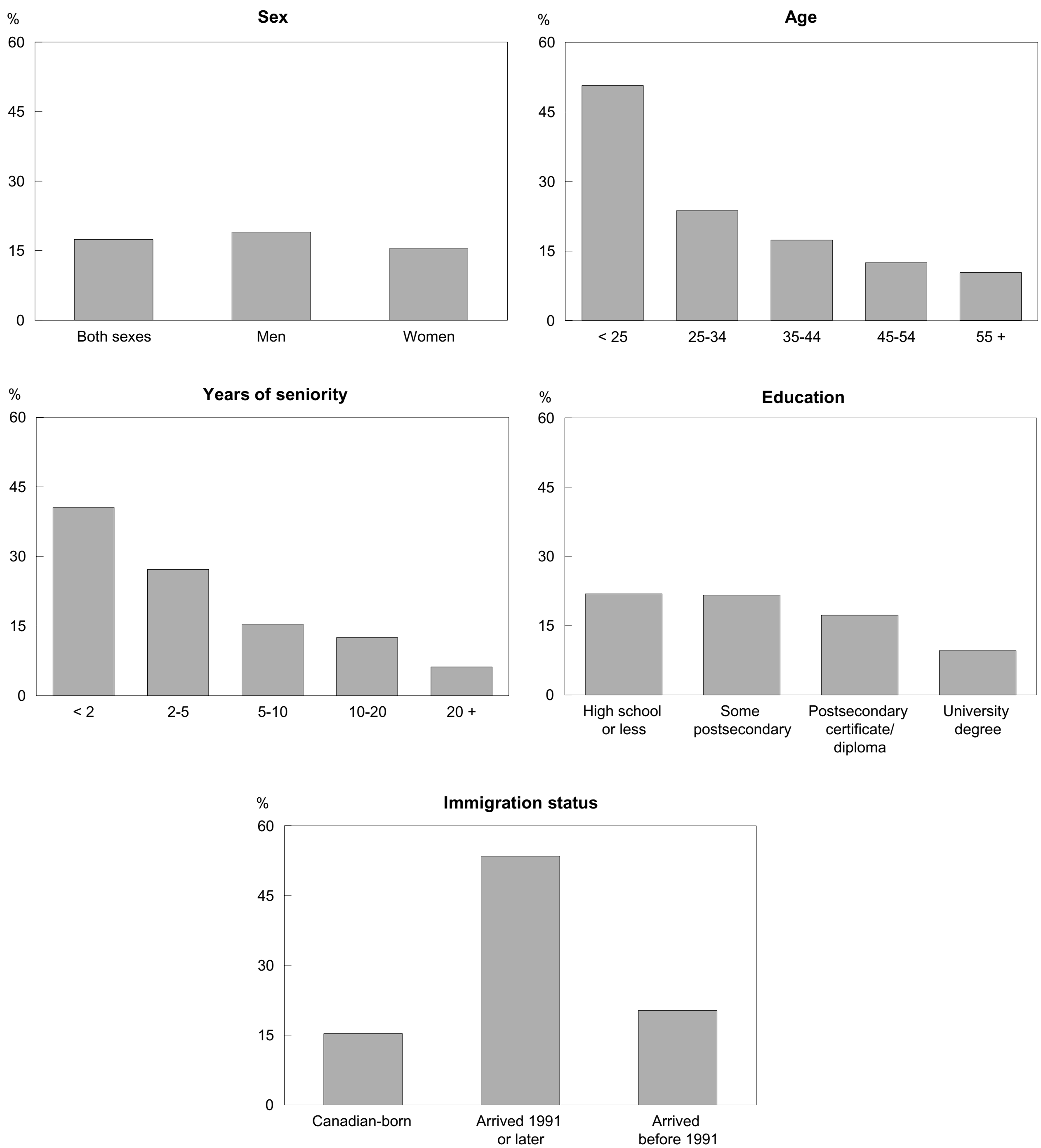
Perspectives

Table 3: Selected characteristics of immigrant and Canadian-born workers*

	Canadian-born	Arrived 1991 or later	Arrived before 1991
		%	
Education			
High school or less	30.5	23.1	26.2
Some postsecondary	24.9	15.9	20.9
Postsecondary certificate/diploma	26.2	28.5	31.3
University degree	18.4	32.6	21.6
Establishment size			
1 to 19 employees	28.7	33.2	26.0
20 to 99	30.1	33.7	28.0
100 to 499	18.2	21.5	21.1
500 or more	23.1	11.5	24.9
Less than 2 years seniority	19.8	40.1	13.0
Unionized workers	29.1	9.7	28.2

Source: Workplace and Employee Survey, 2001
** Full-time permanent employees*

Chart B: Among full-time permanent employees, young workers and recent immigrants were the most likely to erroneously report having a registered retirement plan.



Source: Workplace and Employee Survey, 2001

Notes

1 See Mitchell (1987) and Starr-McCluer and Sundén (1999) for U.S. evidence on worker knowledge of pension provisions.

2 Deferred profit-sharing plans "permit employees to share in company profits. Employer contributions, either a percentage of profits or a fixed dollar amount, are set aside in a fund. A separate account is maintained for each member, credited with investment income and paid out at the employee's death, retirement or termination." (Frenken 1995, p. 10)

3 Throughout the decade, the vast majority of RPP members were in defined-benefit plans—89.8% in 1991 compared with 84.1% in 2000.

4 This compares favourably with the estimate derived from the 1999 Money Purchase Plan report by Benefits Canada, which found that 1.5 million people were enrolled in such plans. The report was based on a survey of the main financial institutions offering money purchase plans to employers.

5 Similarly, of the 732,000 workers who reported having a RPP but were in firms that did not offer one, 56% were in firms offering group RRSPs to at least part of their workforce (Table 1).

6 For the employer portion of WES, the primary respondent is the human resource manager in a large establishment or the business owner in a small establishment.

7 The differences across age groups observed in the second column of Table 2 vanish in a logit model where the probability of an individual working in a firm reporting no retirement plan—conditional on workers reporting at least one retirement plan—is modelled as a function of age, seniority, education, sex, union status, immigration status, industry, establishment size and an indicator of multi-establishment employer. However, workers with less than 2 years seniority remain more likely to be misinformed than those with 10 years or more in this model.

8 This is more likely to happen if workers in defined-benefit RPPs changed employers during their career and could not transfer their pension assets to their new employer's RPP.

9 It is assumed here that both RPPs have the same benefit formula, and that the benefits from the first RPP cannot be transferred to the second RPP—which is the case for many defined-benefit RPPs offered in the private sector.

10 Under the new rules, vesting takes place after two years of participation in the plan, but only applies to employer contributions made after the effective date of the amendments. For employees who became members of an RPP after these amendments, vesting applies to all employer contributions.

11 The differences between recent immigrants and Canadian-born workers, observed in Table 2, are examined using two separate logit models (where the set of covariates is defined above). For workers who reported having a retirement plan, an initial probability of misclassification of 7.2% is assumed (that observed for Canadian-born workers). Then, being a recent immigrant raises the probability of misclassification by 14 percentage points—that is, 72% of the difference found in the raw data. For all workers, an initial probability of misclassification of 3.7% is assumed (that observed for Canadian-born workers). Then, being a recent immigrant raises the probability of misclassification by 4.3 percentage points—that is 84% of the difference found in the raw data. The marginal effect of a discrete covariate k, ΔP_k, is evaluated around the mean P of the dependent variable using the following formula: $\Delta P_k = [1+\exp(-x'b - b_k)]^{-1} - P$, where $x'b = \ln[P/(1-P)]$. See Gunderson, Kervin and Reid (1986), p. 267.

12 Federal/provincial regulatory pension legislation has certain disclosure rules, requiring employers to provide each RPP member with an annual statement showing such items as length of plan membership; amount of employee contributions (if required); estimates of future retirement benefits; and current benefits on termination, death or possibly disability. In the case of group RRSPs, financial institutions likely also produce an annual report for each member showing current market value of investments and the member's equity. Even though these statements identify the plan, one can safely assume that few members would study them and make note of the type of plan referred to.

13 It is possible that some workers reported having no group RRSP or RPP while being in a firm offering one or both of these plans. Since participation in group RRSPs is generally optional while participation in RPPs is sometimes optional, sometimes compulsory, this study was not able to investigate whether such responses represent another form of misclassification.

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