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FINANCIAL SECURITY

On contract? No pension? Read this

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I overheard two men talking over lunch the other day at a Toronto restaurant. The first man said he'd received an e-mail from his brother, who had just been laid off from his corporate job as a result of a company reorganization.

"Well, at least he'll get a severance package," the second man said.

"No package," the first man replied. "He's a contract consultant."

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Their exchange captured the changing nature of job security. Even the phrase, "job security" seems like an anachronism these days, more suited to a time when new episodes of *I Love Lucy* were still running on the tube and a degree meant certain employment. This rapidly changing career landscape requires an updated approach to financial decision-making.

If your financial planning hasn't stayed on top of employment trends, here are three major factors you need to consider:

ANNUAL BONUSES

Corporate Canada is becoming more focused on tying annual bonuses to specific performance goals for individual employees and companies as a whole. In other words, it's becoming harder to qualify for bonuses.

Financial implications – Treat the bonus as just that, a bonus. Fixed and necessary lifestyle expenses, including debt repayment, retirement savings, education savings and the like should be funded from regular cash flow. The bonus is best applied to the "extras," such as accelerated mortgage payments, catching up on unused RRSP contribution room, luxury vacations, and the like. That way, if the bonus doesn't arrive, it won't be a crisis.

CONTRACT POSITIONS

In a post-recession world, companies remain hesitant to hire more full-time staff. They have become used to hiring on a contract or temporary basis to deal with fluctuating business demands. This saves them money on benefits and allows them to increase and decrease labour costs in line with business needs and economic activity. In spite of the economic recovery, there is no evidence this trend is slowing.

Financial implications – Obtaining individual health and disability insurance coverage is essential for most contract employees, and professional liability insurance might be a consideration as well. Being self-employed has tax benefits, however. Many contract employees might be surprised to find out that the Canada Revenue Agency doesn't actually consider them self-employed for tax purposes.

PENSIONS

A recent report by ratings agency DBRS showed that, as of the end of 2012, the funding status of the 67 defined-benefit pension funds it examined stood at 84.4 per cent. That means that the vast majority of pensions do not have sufficient assets to fulfill the financial commitments they have made to current and past employees. Twelve pension funds fell below 70-per-cent funding. (Defined-benefit pension plans pay out a predetermined amount of money based on salary and years of service. The employer must make up funding shortfalls caused by weak investment returns. Payouts from defined-contribution plans, on the other hand, depend entirely on the returns achieved by plan members. The risk is borne by employees.)

Financial implications – Greater self-reliance on retirement funding is a permanent, long-term trend. Employees should find out the funding level of their DB pension plan to determine whether additional saving outside the plan is prudent. Employees should also prepare themselves for the possibility that their DB pension contributions may increase in the future, which means a reduced paycheque. Those with defined-contribution (DC) pension plans should ensure their money is being invested prudently to optimize their retirement nest egg. Too many employees pay too little attention to how their DC funds are invested.

Employment uncertainty does not have to equal financial uncertainty. It just means planning a little differently, in case you find yourself in the same shoes as the brother of the man in the restaurant.

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