

Increasing the Coverage of Supplementary Pension Funds: the Italian Case

Ambrogio Rinaldi
COVIP
rinaldi@covip.it

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The Italian pension system in 1992

First-pillar public pensions: general coverage

- of all employed workers
- PAYG, earnings related
- contribution 32.7% of salary
- high replacement rate (up to 80% and above)
- lax age requirements
- indexation to wages
- many privileged categories (civil servants, etc.)
- special schemes for many self-employed

⇒ pension expenditure already high (13% of GDP), to reach 23% by 2030

Supplementary pensions: 3% of work force

- only for high-income employees (managers, banking & insurance sector)
- 600.000 members of PFs no specific regulation of PFs

Households' long-term savings in real estate, T-bonds, mutual funds

Pension Reforms of 1992-95

Public pensions:

•1992: parametric reform

- more stringent age requirements
- calculation refers to earnings over a longer time span
- indexation changed: from salaries to prices (partial over a threshold)

•1995: structural reform

- Introduction of NDC
- Long transition phase

⇒ **Public expenditure for pensions strongly reduced in the long term**

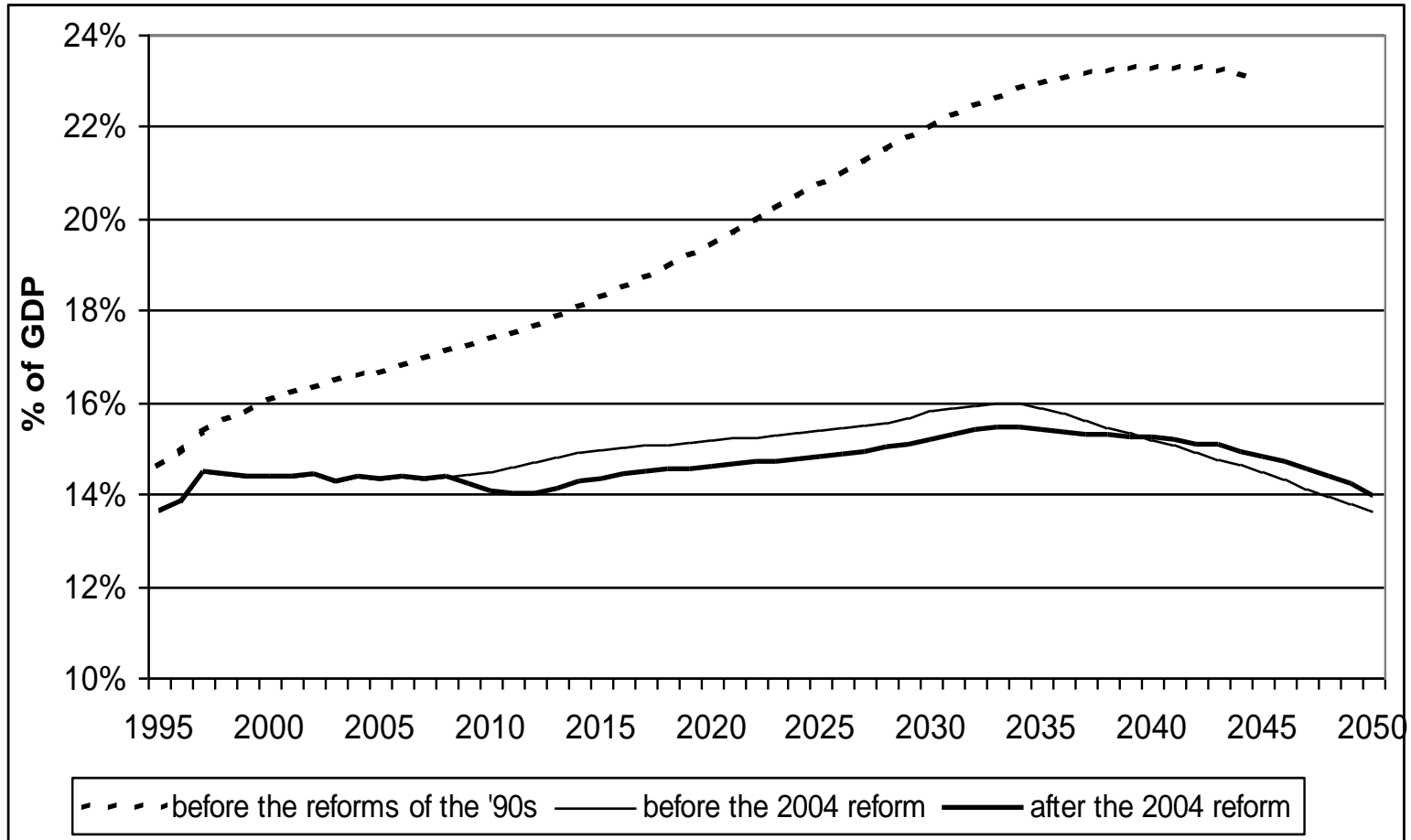
⇒ **Rate of substitution also reduced**

Supplementary pensions:

- Introduction of comprehensive legislation (completed in 1997)
- Specialized supervisor (COVIP)
- Fiscal incentives

⇒ **1997-98 first new pension funds instituted**

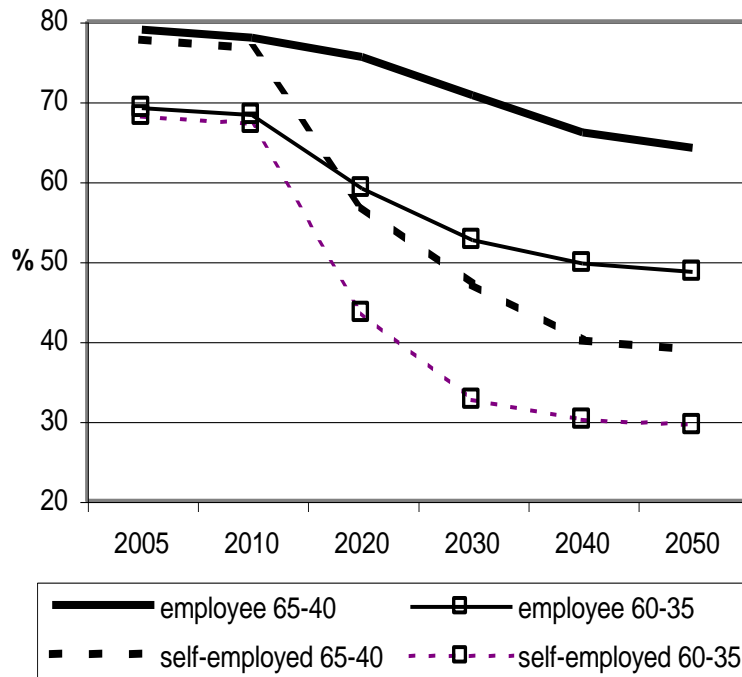
Public expenditure for pensions before and after the reforms (1995 – 2005)



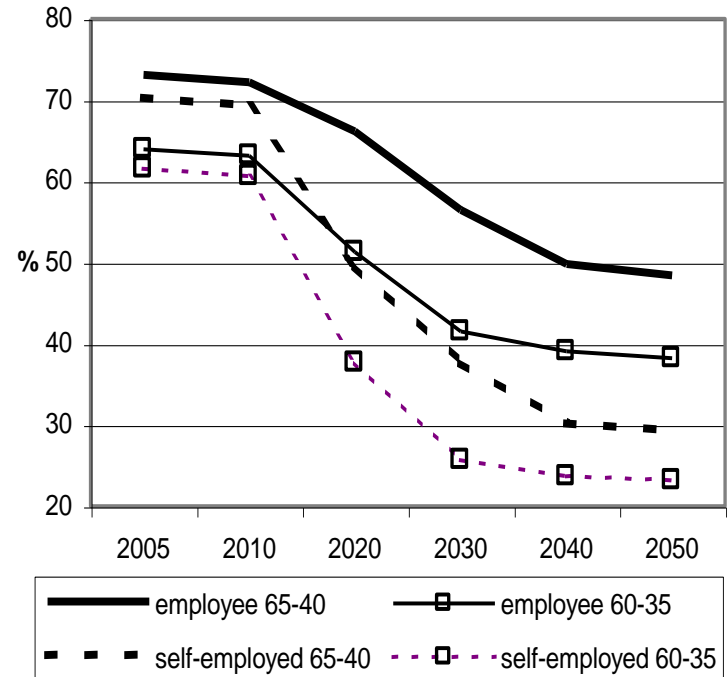
Slide gently provided by Angelo Marano (Prime Minister's Office)

Gross replacement rates of public pensions (2005-2050)

No individual career



Dynamic career: earnings risings from 100% to 200% of the average



...a few years after the reforms:

Public pensions

- pension expenditure put under control, but still some work to do...

Supplementary pensions

- **still very low membership rate: 13% of workforce**
 - **big differences between sectors**
 - many new funds instituted:
 - 35-40 industry funds, covering 80% of employed workers of private sector
 - 70-80 “open” funds, instituted by all financial and insurance groups
 - Many insurance-based pension products (PIP)
-**but competition is low**

Another round of pension reforms: 2004-07

Public pensions

- **No structural changes: NDC system confirmed, but with some inconsistency...**

Supplementary pensions

- **automatic enrolment for all employed workers in the private sector**
 - default contribution rate : about 6,91% (the annual accrual of severance pay: the “TFR” - Trattamento di Fine Rapporto”
 - Possibility to opt-out for individual workers and keep the TFR as it is
 - For “large” firms (over 50 employees), TFR is paid out anyway (to the Treasury if the individual worker wants to keep it as it is)
- **Increase in competition between pension schemes**
- **Fiscal incentives for pension funds strongly reinforced**

What is the TFR?

"Trattamento di Fine Rapporto"

- a sort of severance pay, or deferred salary, imposed by law and applied to all employed workers in the private sector
- **6.91% of current salary** kept by the employer as book reserves
- paid to the employee at termination of employment (average “length” at payment is 7 years)
- revaluation rate preserves its real value against inflation:

1,5% + 3/4 of inflation rate

Mixed Results of the TFR reform

- Limited increase in coverage
 - up to 26% of employed workers of private sector
 - or 20,7 % of the workforce
 - Large differences between sectors, etc., are still there
- What went wrong?
- Structural reasons (demand side)
 - Consistency of policy
 - Implementation

The TFR Reform: some critical issues

- Structural reasons (demand side)
 - TFR may be good (for employees and employers), perhaps better than pension funds
 - lack of trust in financial markets (financial crisis – unlucky timing!)
- Consistency of policy
 - Conflicting policy aims
 - development of private pensions vs. financing the public budget through the TFR
 - Failure to take the responsibility of choosing “what is best” for the worker
 - why automatic enrolment only with the TFR and not with contributions set in labour agreements?
 - role to play for the State and/or for social parts
- Implementation
 - Need to sign forms to certify “non-action”
 - Strongly wanted by the Treasury (disincentive to accept the default?)
 - Favoured also by trade-unions, in order to enhance awareness

What to do now to increase coverage?

Public debate is considering:

- Information campaigns
- A new round of automatic enrolment for all workers
- Increase in competition between sches (profit / non-profit)
- Targeted measures
 - by sector
 - for the young
 - for the self-employed
 - for the public sector workers

There is a need for:

- a consistent plan
- consensus of social parts
- efficient allocation of responsibilities/tasks btw.
 - Legislation /State)
 - Social parts (employers, trade unions)
 - Individuals
- “soft” paternalism is probably a good approach – default options, etc.