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COMMISSIONE DI VIGILANZA SUI FONDI PENSIONE

DC Pension Design: the experience in Italy

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Contents

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The National context in the 90's

- In the 70's and 80's, Italian public pensions became increasingly more generous and expensive for the public budget
  - PAYG
  - benefits linked to end-career salaries
  - low requirements for retirement age and years of contribution
- Demography and lower growth made clear that the Italian pension system was quickly becoming unsustainable
  - ➢ Since the early '90s, several rounds of reforms of public pensions
    - Still PAYG, pension expenditure as a % of GDP to be stabilized in the LT
    - benefits to be strictly linked to contributions (NDC), although with a long transition – and indexed to GDP growth
    - contribution rate at 33% of salaries for employed workers
  - ➢ In principle, <u>public pensions for future generations to be integrated by funded pensions for most workers</u>
  - ➢ In 1993 (and in practice from 1997) <u>a national framework for funded pension plans (occupational and personal) was put in place</u>

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Setting-up the system in the 90's

- 1993-97: new legislation established comprehensive framework for pension funds and plans (**PFs**)
  - Contractual Pension Funds (**CPFs**) – typically set up by agreement btw. social partners as non-profit, stand-alone entities; asset management to be outsourced to professional asset managers
  - Open Pension Funds (**OPFs**) – set up by financial institutions – mainly as personal plans, but open to host occupational plans
    - benefits regime: DC only for new plans;
    - adjustments required for «old» occupational plans : DB still allowed, but to be closed to new members
      - «old» occupational plans were typically set in some large companies and covered only 3% of work force
    - strict mark-to-market valuation required for new plans (UCITS-like accounting arrangements)
    - voluntary set-up for employers and voluntary membership for employees
    - main source of financing: new flows of severance pay (≈7% of salaries) - so-called **TFR**, «Trattamento di Fine Rapporto»
    - **ETT** as tax regime – contributions exempt from personal income tax (IRPEF) up euro 5,164 per year
    - **COVIP** established as the stand-alone specialized supervisor –ample powers to issue 2°level regulation and supervisory reporting
    - Standardized information to members introduced, to ease comparison and enhance competition
- from 1997: establishment of new plans; registration of old plans
  - Occupational PFs usually set up as CPFs at industry level – based on national agreements btw. social partners (trade unions/employers)
  - on the top of the TFR, contractually agreed contributions (≈2-3% , usually equally split btw. employer and employee)
  - offer of a range of 3-5 investment options quickly became the standard – both for CPFs and OPFs
  - in 2000-01: introduction of **PIPs** (Insurance-based Personal Plans)- to be set as with-profits or unit-linked policies (specifically designed as pension products), admitted to the same tax allowances as other pension plans

Main developments since early 2000's

- as of early 2000's, the Italian system of pension funds/plans is well established, with a comprehensive and up-to-date regulation
- however, membership level differs a lot across industries, firms of different size, geographical areas, age cohorts, genders – «weaker» workers are often unable to take part in the system.
- The main issue remains the financing of the system: small firms and weaker workers prefer to keep the TFR as it is; public pensions already require contributing 33% of salary, leaving limited room to additional savings for pensions

…..after long discussions at political level…..

- **2005-2007: nation-wide auto-enrolment set by law (with opt-out)**
  - In the the 1° half of 2007, almost all employed workers of the private sector were automatically enrolled in their industry pension fund, with the option to opt out, with the new flows of TFR to be paid in the pension funds
  - for employers with 50 or more employees, in case of opting-out employees, new TFR would have to be paid in a special account to the Treasury (to remove disincentive to foster membership among workers – at least for larger firms)
  - Tax incentives raised for the pay-out phase – «ETt model»

    ➢ in terms of increased membership, mixed results

- **from 2015: compulsory enrolment introduced in some industries by national labour agreements**
  - mandatory contribution usually set at mimimal levels (12-30 euros/month), rarely followed by additional voluntary contributions. Due to discontinuity of job tenures, discontinuity in contribution flows is often observed

➢ More recently, renewed proposals are put forward about a new round of nation-wide auto-enrolment…..

The supplementary pensions landscape at end-2022
(provisional data)

	Number of Plans	Individual accounts	Members	Assets (€ millions)	Contributions (€ millions)
Contractual Pension Funds	33	3,806,098	3,690,000	61,103	6,051
Pre-Existing Pension Funds	191	674,000	645,000	64,300	4,000
Open Pension Funds	40	1,841,707	1,790,000	28,047	2,846
PIPs (Insurance-based personal pension plans)	68	4,000,005	3,828,000	52,000	5,223
Total	**332**	**10,290,000**	**9,200,000**	**205,450**	**18,120**
As a % of labour force (15-64)			**36.3**		
As a % of working-age population (15-64)			**22.6**		
As a % of GDP				**10.8**	
As a % of HHs' financial assets				**4.3**	

The Italian system of DC pension funds/plans at year 2022: main strengths

- Stability of the DC framework since the 90's contributes to the overall resilience of the system
- By-partisan governance of occupational plans by employers and trade unions at industry level favours long-standing political support, adequate size and value-for-money solutions
- Constructive role played by the financial industry, operating on a competitive basis both as a service provider and as a direct supplier of pension products, contributes to good governance and risk management
- Overall resilience shown by the system across various crises (Great Financial Crisis of 2008, global pandemics, geo-political tensions, etc.)
- Wide, global diversification of asset allocation minimizes effects of defaults of specific borrowers
- Appropriate choice architecture offered to members allows matching individual preferences with actual risk exposure of chosen investment options
- Standardised, comprehensive information to members allows comparison across available pension plans regarding costs, returns, etc. – while individualized pension projections allow members to plan for retirement taking into account their own other sources of income (public pensions, etc.)
- Comprehensive supervisory reporting of quantitative data eases off-site regular and ad-hoc checks

The Italian system of DC pension funds/plans at year 2022: outstanding challenges

- to increase membership and contribution density in fragmented industries and for "weaker" workers
- to nudge members towards investment options that are more consistent with the long-term horizon and fit for producing higher returns and thus higher pension benefits (especially for the young); life-cycle, default investment options still to be spread across the system
- to review investment process and strategic asset allocation considering investment opportunities in alternative, innovative and illiquid assets, consistently with the long-term horizon of pension savings, possibly contributing more to national GDP growth
- to favour the diffusion of lower-cost, value-for-money solutions for personal pensions and the self-employed
- to develop more convenient and flexible solutions for the pay-out phase
- specific supervisory challenges: to ensure IORP II implementation, to facilitate ESG and digital transition

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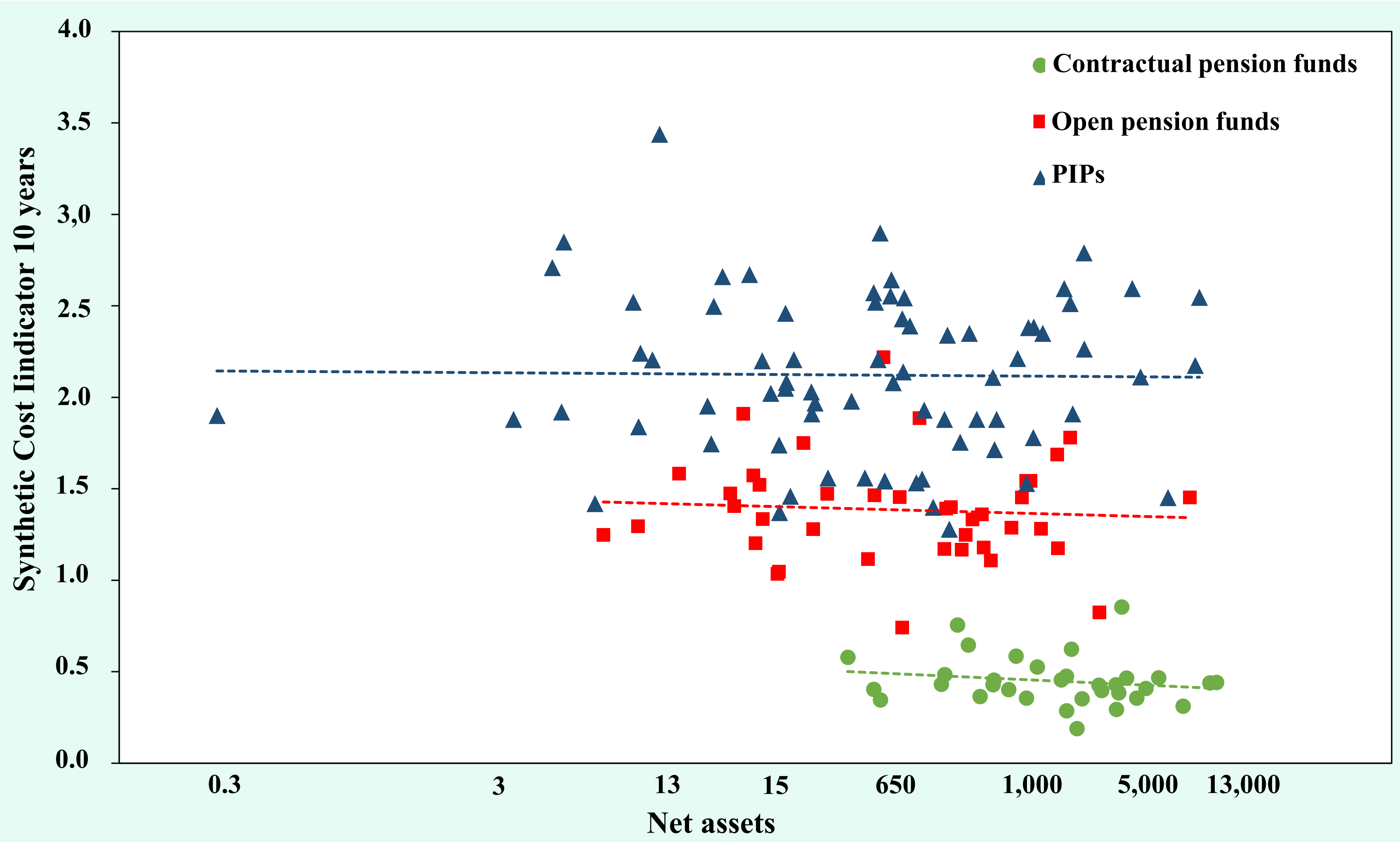
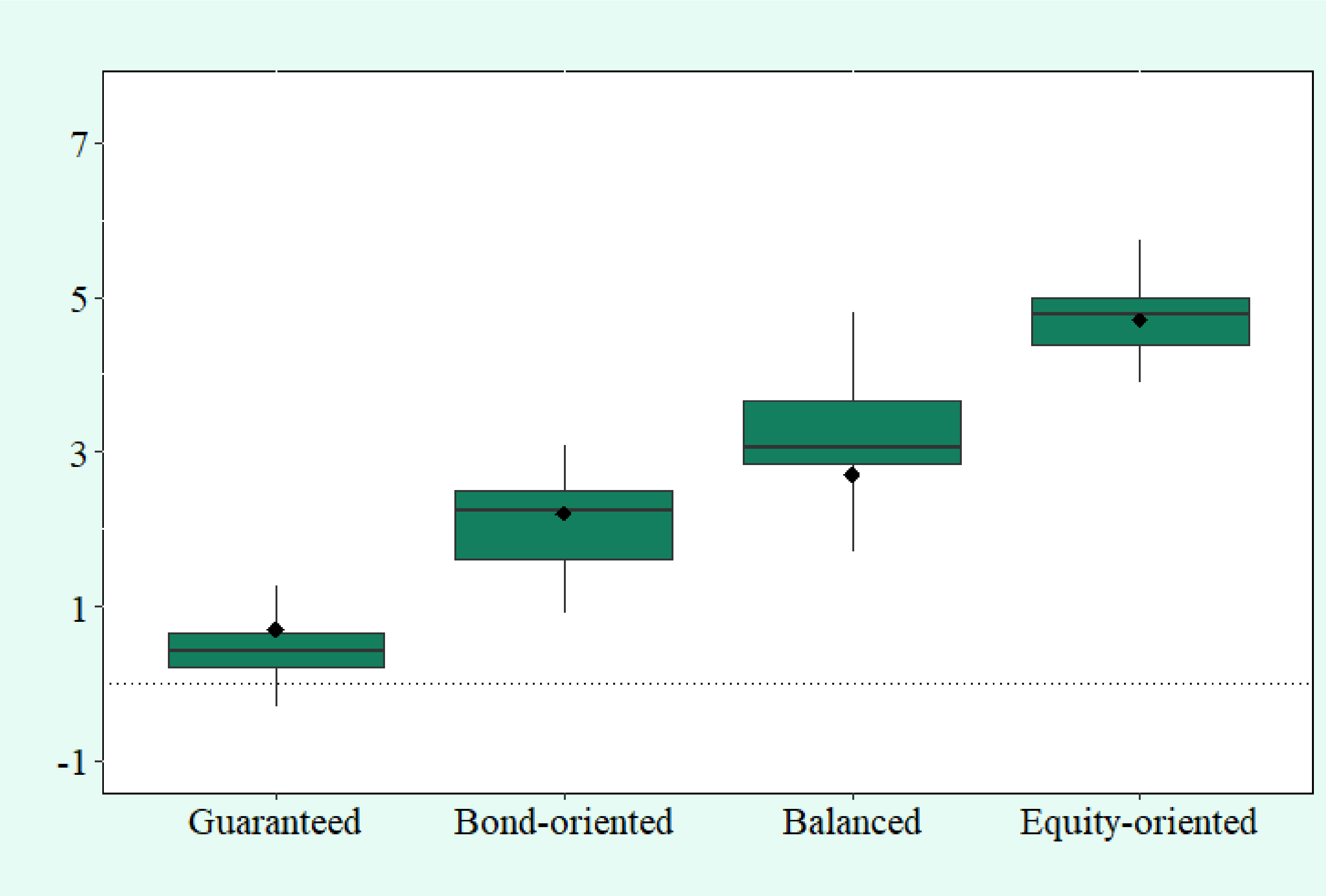
Costs and asset size

Year 2021



Contractual Pension Funds: distribution of 10-year returns by investment options

(Compounded net annual rates of return, end-2012 to end-2022)



The box plots show the distribution of the observed individual returns of the investment options. The green-filled areas show 50% of the returns (the 2° and 3° quartile), with the median shown by the bar in the middle. The wiskers show the remaining values (1° and 4° quartile), excluding extreme values. The asset-weighted mean of individual returns is shown by the diamond.

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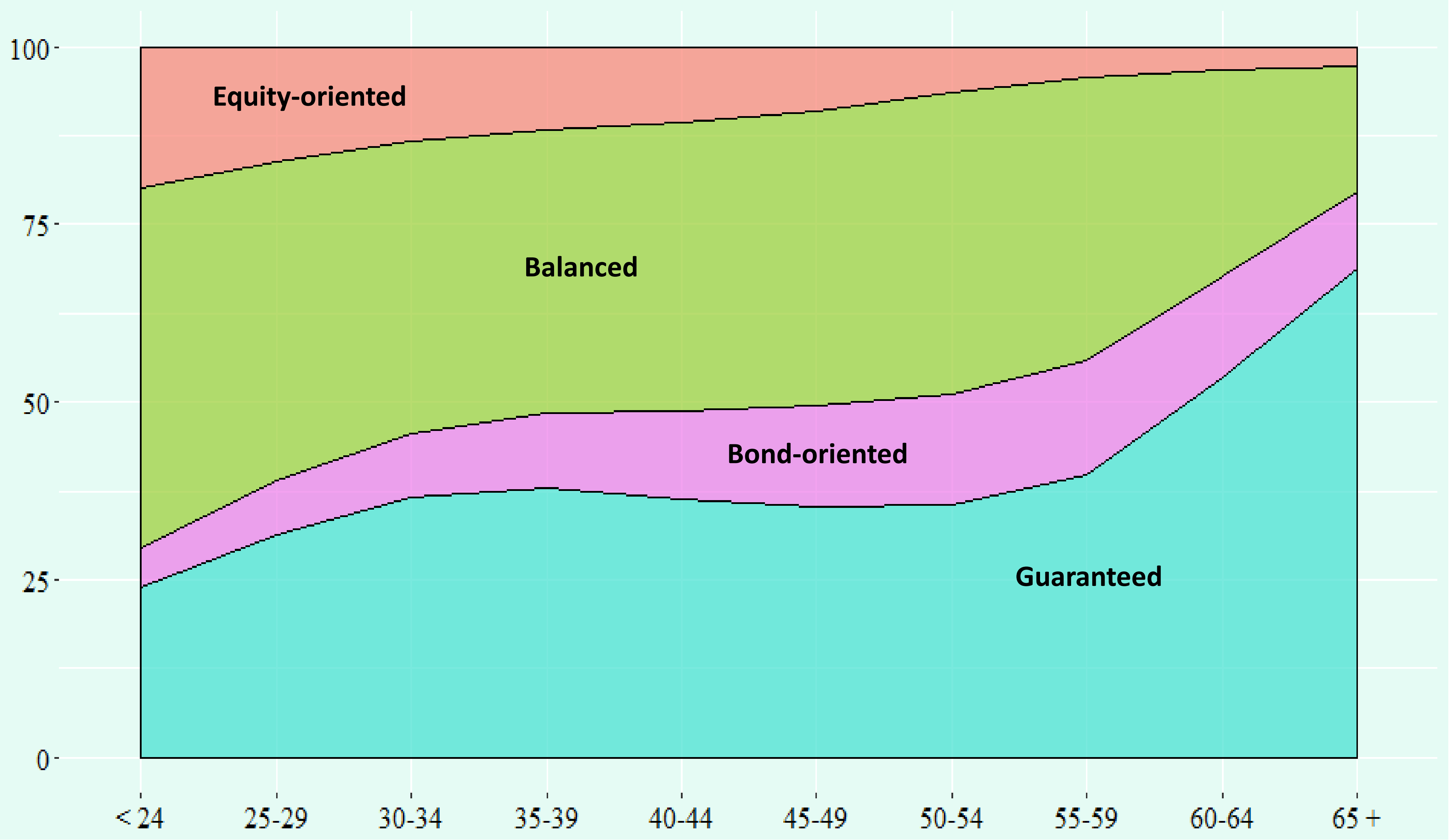
Investment options by age of members

all kinds of pension plans- year 2021



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DC Pension Design: the experience in Italy

ANNEX

- Structural features of different kinds of pension plans
- Additional selected tables

Structural features of different kinds of funds/plans

- Industry-wide Occupational Funds (non-profit) – so-called Contractual Pension Funds (CPFs)
  - linked to nation-wide labour agreements at industry level
  - governance by trade unions and employers (parity basis); mandatory outsourcing of asset management
  - regional and group/company pension funds also possible, but rarely put in place (no single company fund put in place)

- Open Pension Funds (OPFs)
  - established by financial and insurance firms
  - may host both occupational and personal plans

- Insurance-based Personal Plans (PIPs)

  ➢ for all the three kinds of new plans, choice btw. sub-funds offered to members

- Pre-existing Pension Funds (PPFs)
  - legacy from the past: many company pension funds, but covering only for 3% of workforce – higher-income employees
  - originally, wide diversity (stand-alone/book reserves, DB/DC, etc.) – over time, converging to the model of new CPFs
    - just a few pension funds still DB, closed to new members and often in course to be overcome
    - trend for consolidation, especially in banking groups

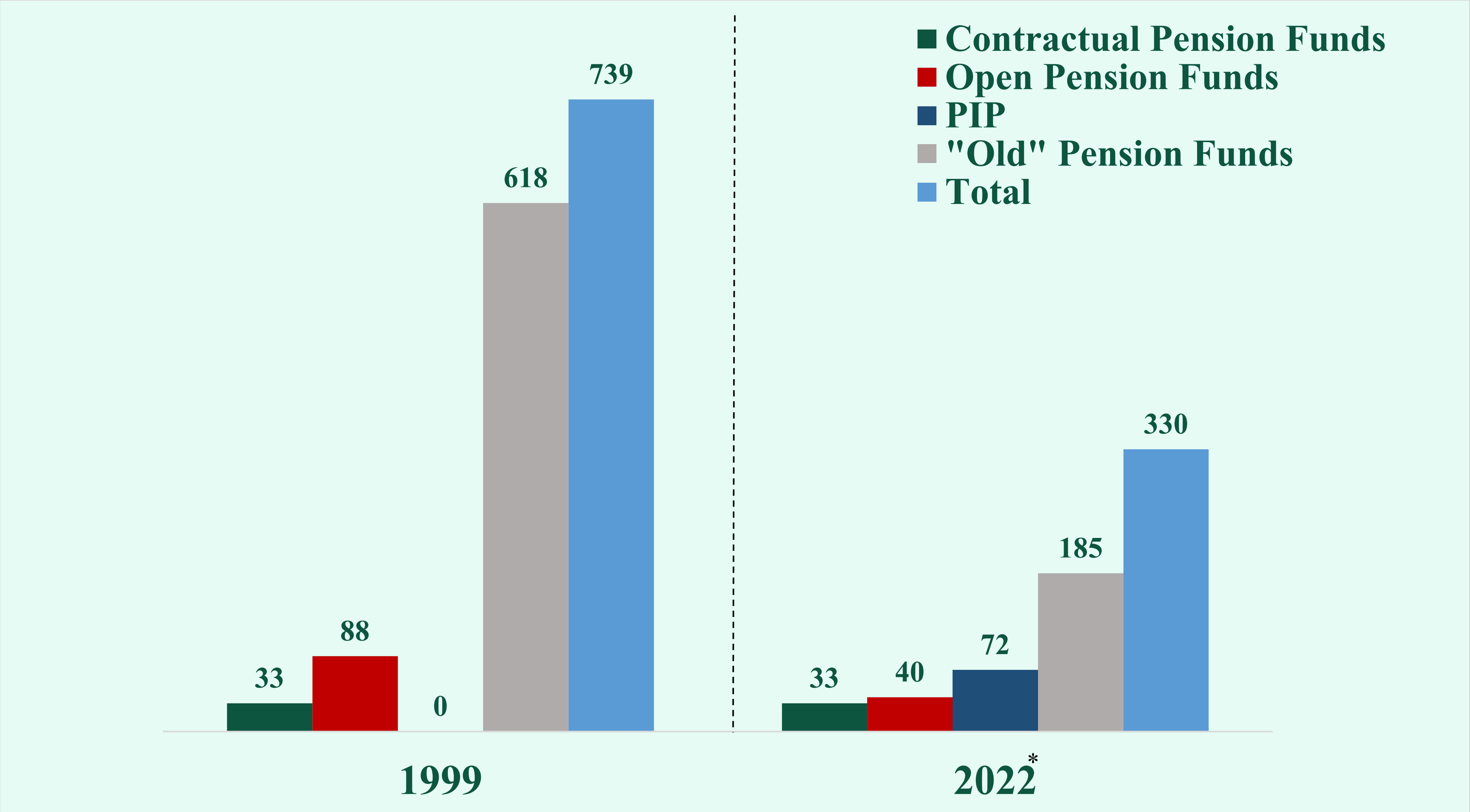
The supplementary pensions landscape at end-2022

(*preliminary, with more detailed data on PIPs*)

	Number of Plans	Individual accounts	Members	Assets (€ millions)	Contributions (€ millions)
Contractual Pension Funds	33	3,806,098	3,690,000	61,103	6,051
Pre-Existing Pension Funds	191	674,000	645,000	64,300	4,000
Open Pension Funds	40	1,841,707	1,790,000	28,047	2,846
New PIPs	68	3,697,215	3,520,000	45,400	4,963
Of which: With Profits		*2,335,777*		*33,870*	*3,616*
Of which: Unit Linked		*1,361,438*		*11,530*	*1,347*
Total	332	10,019,020	8,950,000	198,850	17,860
Old PIPs		308,000	308,000	6,600	260
Grand Total	**332**	**10,290,000**	**9,200,000**	**205,450**	**18,120**
As a % of labour force (15-64)			**36.3**		
As a % of working-age population (15-64)			**22.6**		
As a % of GDP				**10.8**	
As a % of HHs' financial assets				**4.3**	

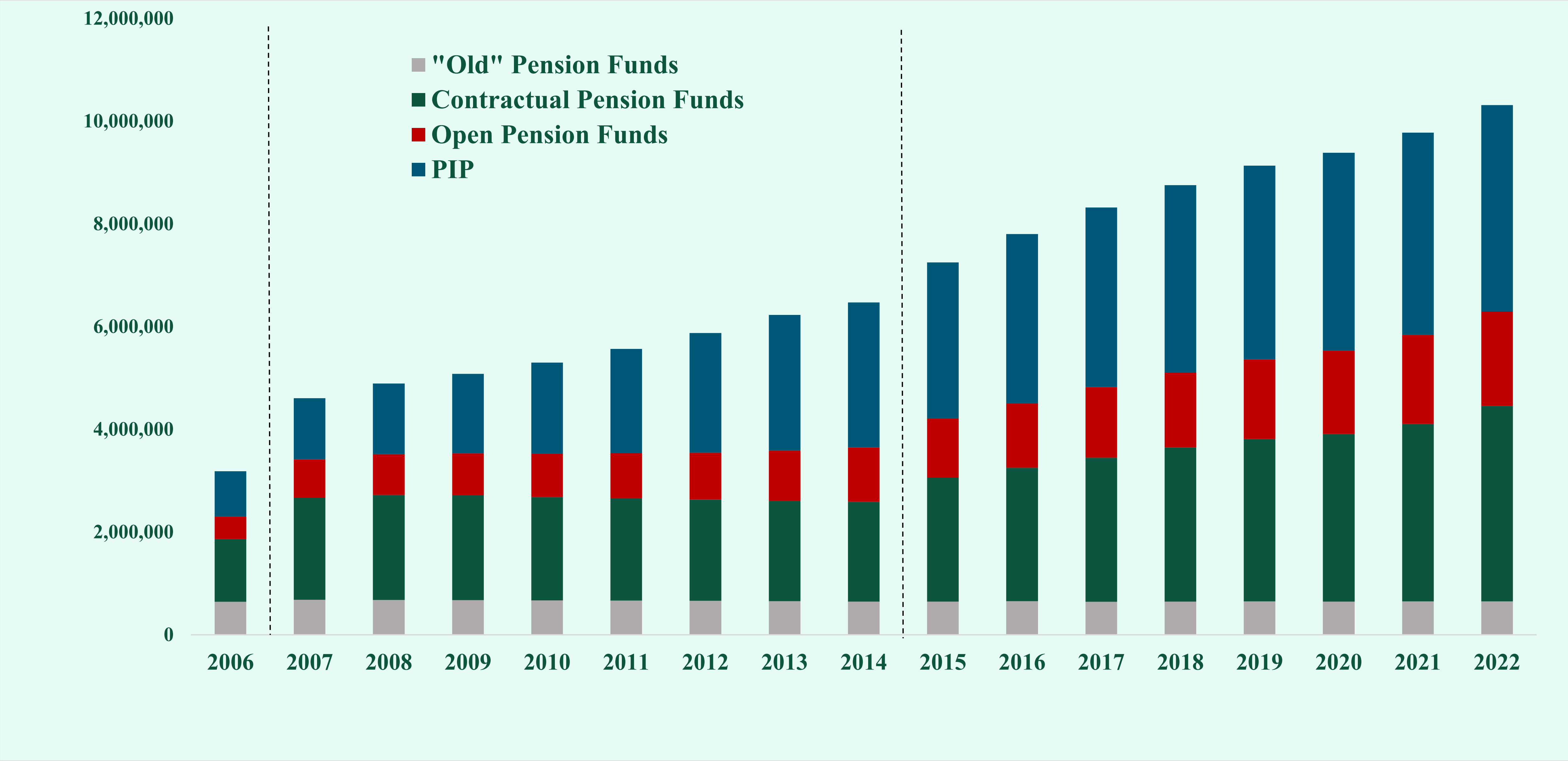
Members are net of multiple individual accounts for the same person

Number of pension funds/plans



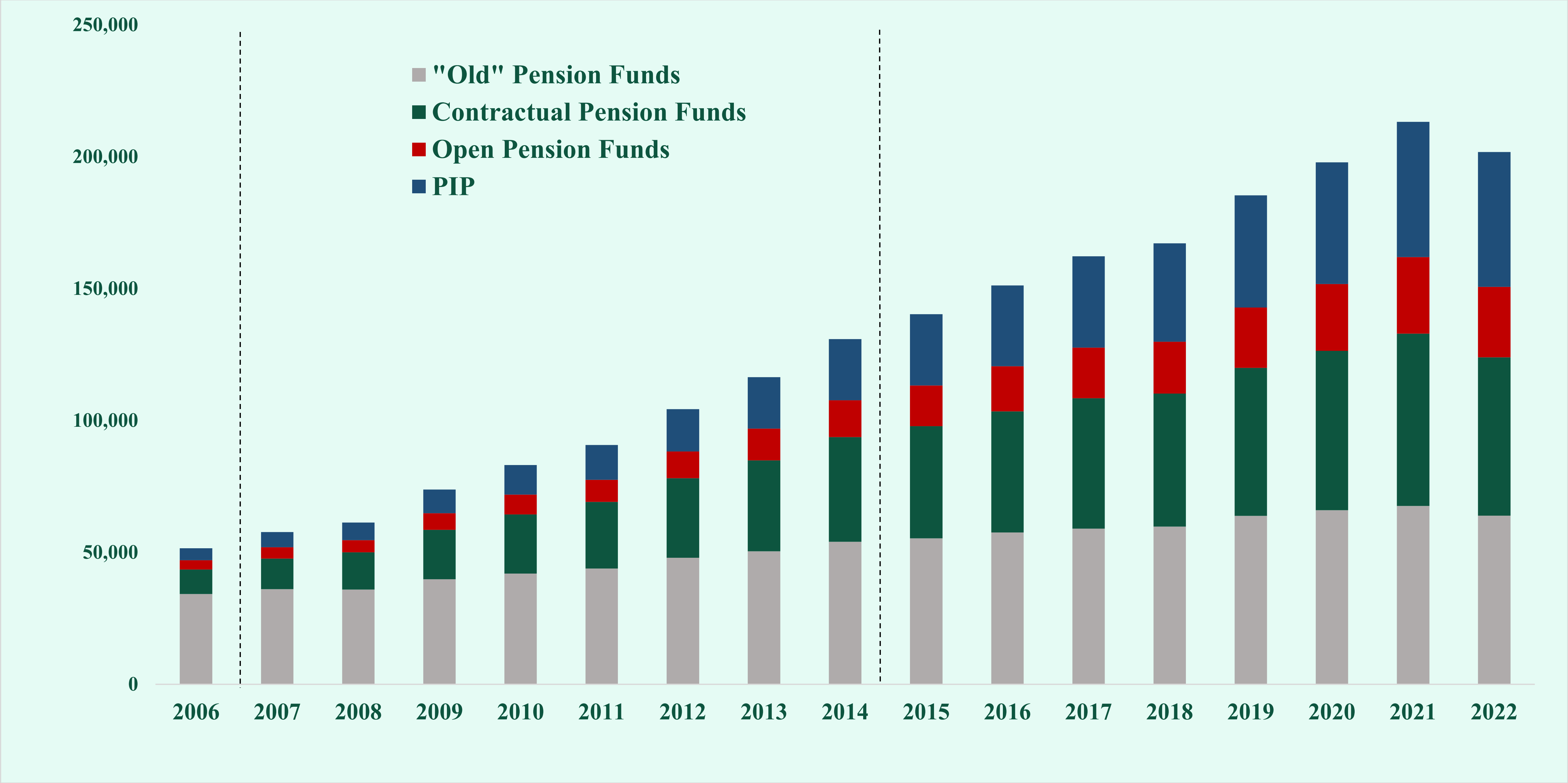
* Preliminary data

Members



12,000,000
10,000,000
8,000,000
6,000,000
4,000,000
2,000,000
0
"Old" Pension Funds
Contractual Pension Funds
Open Pension Funds
PIP
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016
2017
2018
2019
2020
2021
2022

Assets



250,000
200,000
150,000
100,000
50,000
0
"Old" Pension Funds
Contractual Pension Funds
Open Pension Funds
PIP
2006
2007
2008
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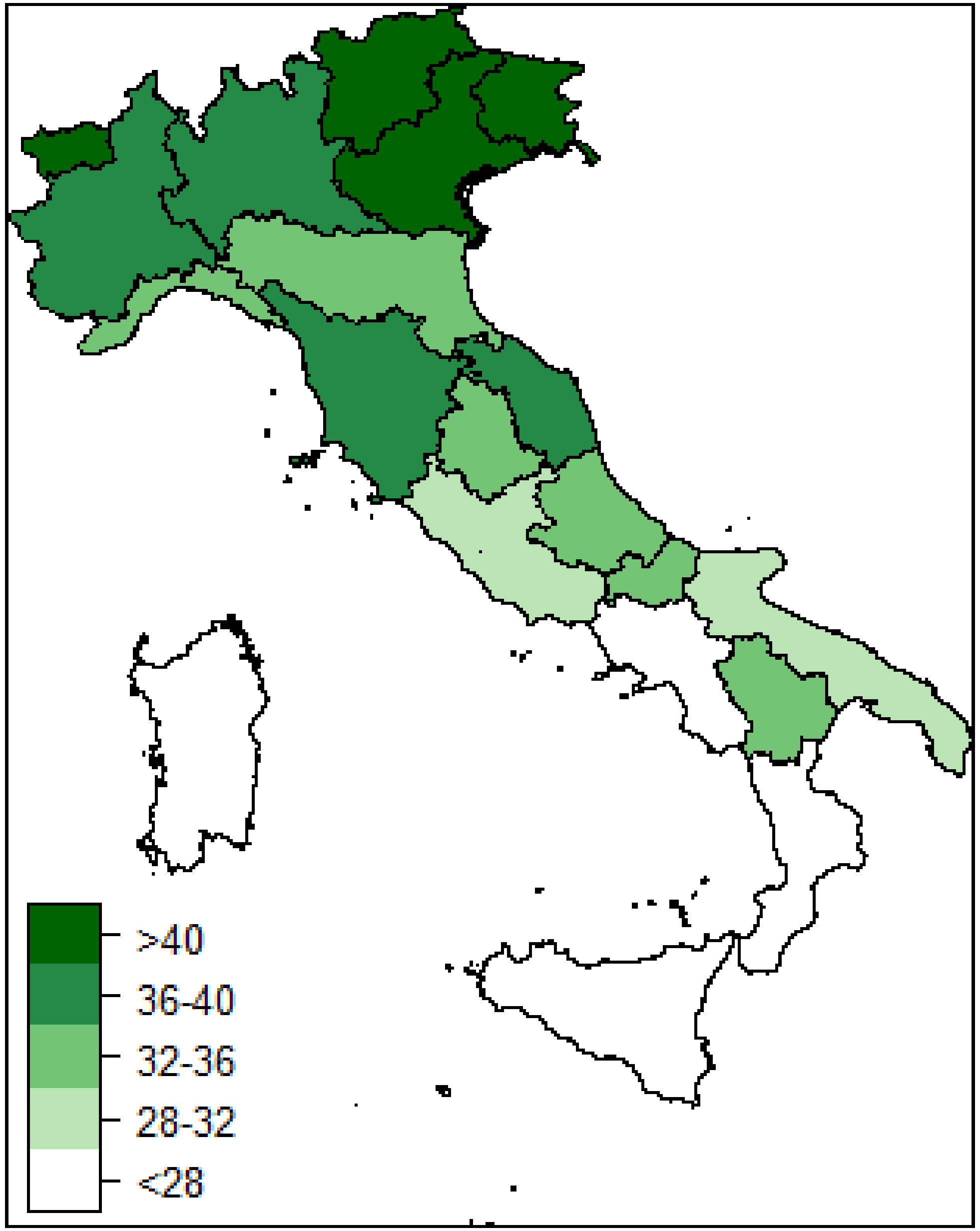
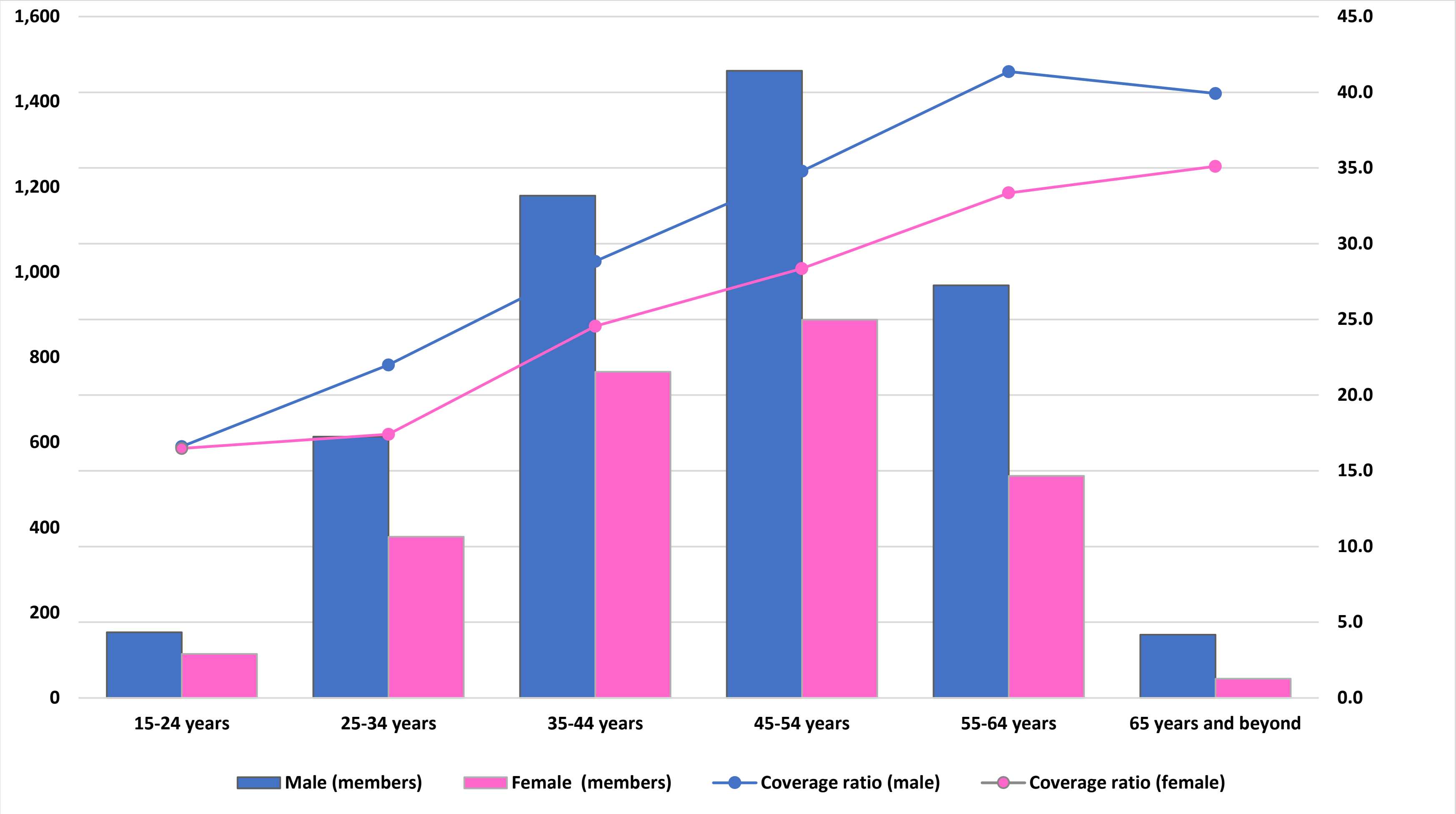
2021
2022

Participation rate by region

Pension fund members as a % of workforce, 2021

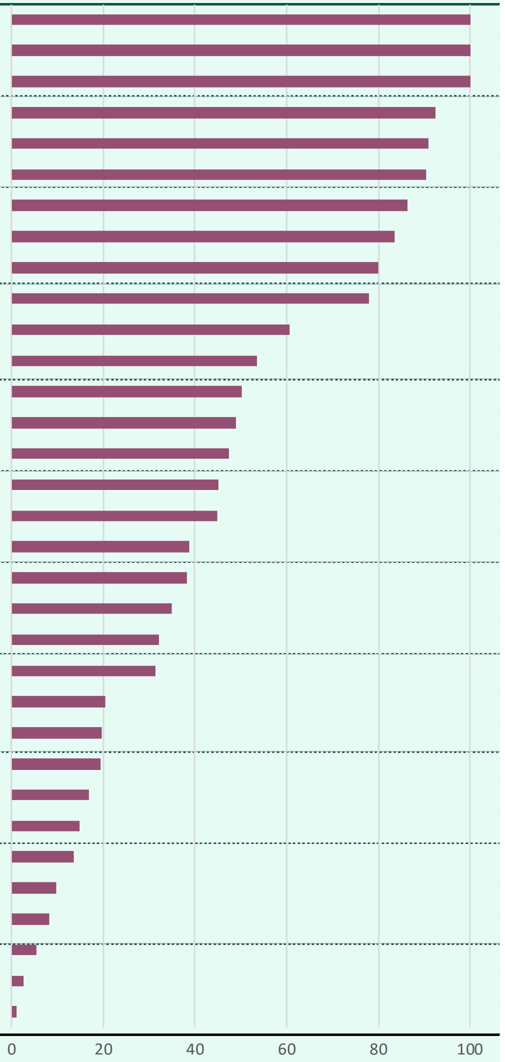


Membership and coverage ratios by age and gender



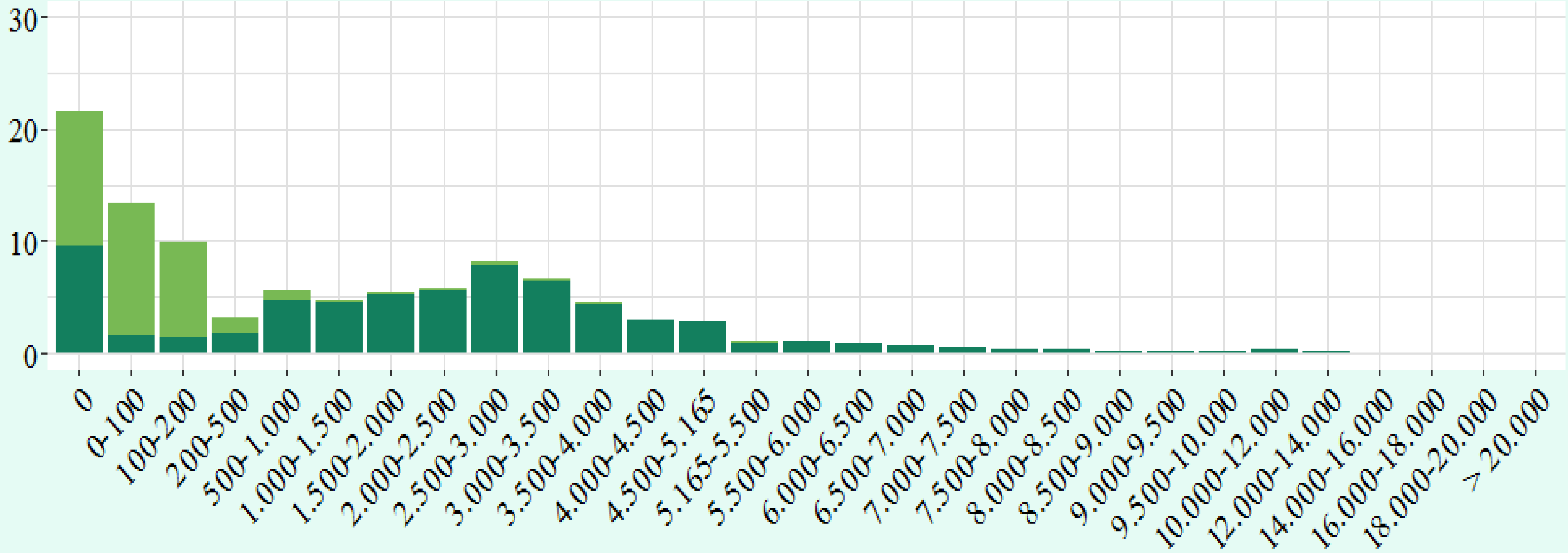
Contractual Pension Funds – Participation rate

Name of pension fund	Number of individual accounts	Potential Members	Assets (millions of euros)	Participation rate at end-2021(%)
FOPEN	47.182	47.182	2.730	100
PREVEDI	1.027.274	400.000	979	100
ASTRI	17.805	17.805	400	100
CONCRETO	7.401	8.000	229	92,5
FONDENERGIA	45.395	50.000	2.987	90,8
EUROFER	81.278	90.000	1.332	90,3
FONCHIM	165.306	191.500	8.180	86,3
FONDOPOSTE	93.195	111.662	2.778	83,5
FONDAEREO	8.635	10.800	472	80
QUADRI E CAPI FIAT	11.769	15.112	758	77,9
PEGASO	33.926	56.000	1.312	60,6
LABORFONDS	130.839	245.000	3.638	53,4
GOMMAPLASTICA	50.091	100.000	1.731	50,1
PRIAMO	112.420	230.000	2.005	48,9
PREVAER	14.729	31.000	657	47,5
COMETA	451.668	1.000.000	13.474	45,2
FONCER	13.300	29.600	558	44,9
TELEMACO	58.245	150.000	2.301	38,8
PREVIAMBIENTE	95.156	250.000	1.235	38,1
ARCO	80.737	232.050	759	34,8
MEDIAFOND	2.737	8.500	143	32,2
PREVIDENZA COOPERATIVA	109.379	349.311	2.287	31,3
FONDEMAIN	7.250	35.500	174	20,4
BYBLOS	39.140	200.000	985	19,6
ALIFOND	47.963	248.000	1.792	19,3
FONDAPI	84.028	500.000	941	16,8
PREVIMODA	59.203	400.000	1.577	14,8
SOLIDARIETA' VENETO	119.790	891.000	1.859	13,4
FONTE	242.681	2.500.000	5.012	9,7
ESPERO	97.356	1.200.000	1.351	8,1
PERSEO SIRIO	85.121	1.571.382	309	5,4
AGRIFONDO	8.538	330.000	106	2,6
FONDOSANITA'	7.765	804.000	272	1
TOTAL: 33	3.457.302		65.322	



Contractual Pension Funds:

distribution of annual contribution flows by amount (in euro) and type of membership (year 2021)



For each class of annual contribution flows, light green shows the proportion of members enrolled through the compulsory membership mechanism introduced in some industries since 2015 by national labour agreements – see above slide n.5.

Investment options: 10-year returns (end 2012-2022)