CAREFIN
Centre for Applied
Research in Finance

Università Commerciale
Luigi Bocconi

Bocconi

Via Sarfatti 25
20136 Milano

Pension Funds in Italy

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PENSION FUNDS IN ITALY

RESEARCH GROUP: Sergio Paci, Patrizia Contaldo, Claudio Fiorentino, Giacomo Nocera, Lucia Spotorno, Francesco Vallacqua

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Divisione Pensions & Insurance

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Preface

Carefin presents in the following pages the first report on "Italian Pension Funds", a comprehensive and concise analysis of the Italian complementary pension system. The aim is to give a precise picture of the structure, operating profiles, and opportunities for future development of the Italian pension fund industry.

The report is intentionally written in a concise and succinct way, presenting updated information on providers involved in asset management, depositary banks, and outsourced administrative and annuity services. It also points out shadows and lights of the system, and proposes some regulatory changes with the aim of improving efficiency. The report is addressed to professionals, research centres, regulatory authorities and those interested in gaining a better understanding the Italian pension system.

The choice of writing an English version of this report is due to the awareness that the Italian pension industry is becoming more international in terms of service provision and in regulation. In light of this, the experience of other countries can be suitably imported.

This report uses official data sourced by the Italian Supervisory Authority for Complementary Pension Schemes (COVIP) from mid-2009, in addition to pertinent information drawn from the mandatory disclosure forms of pension funds.

The report begins by analysing a number of essential features of the first mandatory pension pillar which are connected with the complementary system.The second chapter focuses on the typical features of various types of pension funds in order to understand their different nature, governance and business models. Next the central part of the report analyzes the following for each category of funds: market size, actual participation rates, assets under management, financial management and how it is delegated, asset allocation and financial returns, guaranteed sub-funds, annuity issues, the cost indicator, depositary banks, providers of administrative services, and additional insurance coverage. The final chapter highlights certain profiles of weakness of the system and makes proposals for improving it. At the end of the report, there is an appendix explaining specific or technical aspects of regulation.

PENSION FUNDS IN ITALY AT A GLANCE

The first chapter reports the essential features of the mandatory pension closely linked to the complementary pillar: the main reforms, eligibility requirements, and replacement rates. Particularly important is the change in coefficients for calculating the mandatory pension according to the contribution method. These new coefficients (in force as of this year) will further reduce the replacement rates of employees. The increasing gap between a worker's pension and his or her last salary will likely generate a significant increase in pension fund membership.

The second chapter focuses on the peculiar features of the various types of Italian pension funds. After a short analysis of pre-existing pension funds, the reports provides a concise view of the complementary pension schemes introduced in 1993: contractual funds, open funds and individual pension plans provided by life insurance companies (PIPs). First the distinct features of each are examined (establishment, governance, scheme funding, investment management, administration, depositary bank, costs), then the shared ones (benefits, annuity, fiscal treatment, supervision, rules on investment). At the end a succinct profile is given of pension schemes for public employees. It is important to realise that all types of pension funds are defined contribution schemes. A critical point of the relative regulation regards the annuity option, which is not adequately encouraged.

The third chapter presents the evolution of the pension fund industry. First, the report highlights the market size in terms of membership and assets under management, giving evidence that the system is still in an early stage in terms of worker participation. However, the assets managed are significant. The analysis reports the institutions involved as financial managers in the contractual funds segment from 1999 to June 2009. It is important to remember that contractual funds must delegate the financial management of their assets to financial institutions (banks, SGR/SIMs, or life insurance companies) selected though an invitation to tender. The analysis shows: 1) the involvement of a number of international institutions is on the rise; 2) some firms that first entered the industry have consolidated their market share by increasing both the number of funds served and mandates awarded; 3) a certain number of mandates awarded are and then delegated to another asset manager.

Usually the mandates are sub-delegated to a firm belonging to the same financial group, but a few asset managers (insurance companies) delegated a very high percentage of their mandates outside their group. Sub-delegation is typically from insurance companies to SGRs. Even though open funds and PIPs are promoted by financial institutions authorised to manage the assets of their funds directly, they frequently delegate to a third manager.

The analysis of financial management issues highlights the special features of guaranteed sub-funds. The guarantee of contractual or open funds is usually triggered when certain specified events occur, for instance a member's retirement, death, or permanent disability. Voluntary transfer to another fund is not one of these events. PIPs providing with-profit policies according to Life Insurance Business I usually offer a guarantee which is consolidated in the accounts of the company, and also triggered in case of transfer to another fund.

The report analyses the asset allocation of different types of funds. It shows the high level of debt securities in the portfolio of contractual funds and in with-profit PIPs in comparison with open funds and unit–linked provided by PIPs. A table drawn up by COVIP shows rate of return

on the different types of funds from 2003 to September 2009. The results are affected by the very wide range of asset allocation adopted by different types of funds.

Another important service for contractual and open funds is the depository bank. A list of institutions involved in this highly concentrated business segment is provided. The supply of administrative services for these funds shows the same high concentration..

A relevant part of the report is dedicated to the annuity option. The annuity market for pension funds recorded a significant innovation in 2008 when Assofondipensione, on behalf of its fund members, promoted a tender for the selection of annuity providers. The features of the winning proposal are now a benchmark of the market both for the types of annuities offered and the coefficients for their calculation, The types include with-profit single immediate with death benefits and with-profit single immediate doubled in case of LTC. None of the conditions, including the coefficients, can be changed for the whole duration of the contract (ten years) except for the maximum guaranteed rate of interest. It is important to point out that the coefficients of the above-mentioned annuities are very similar to one another and not far from the usual with-profit immediate lifetime. If this information were disclosed and properly communicated, and adequate financial information provided, the natural propensity for choosing lump-sum at retirement could be reduced in favour of the annuity option.

The last chapter highlights positive and negative features of the complementary pension system and suggests possible changes to the regulation. A positive aspect refers to the scheme's capacity to overcome the worst phase of the financial crisis with limited damage. However, the crisis has highlighted the risk that retirement dates may coincide with a period when prices are falling. A correct solution might be found in the area of asset management through the adoption of investment strategies, for example the life style methodology. In order for members to be aware of this risk profile, they must be provided with adequate information and a consistent level of financial capability.

Another positive profile of the Italian complementary pension system is its capacity to serve relevant social functions, acting as a financial cushion for different needs as in the case of unemployment, serious illness, or a high level of disability. A certain degree of flexibility is a pre-condition to entering the scheme, but the opportunity to cash in a certain amount of the pension account should be balanced without jeopardizing the annuity option.

A negative feature of the complementary pension system concerns the breakdown of membership. In fact, the number of young members is lower than their percentage in the workforce. The same applies to females, and people employed in the South of Italy and in smaller firms. The latter point is extremely significant because small-medium enterprises are the backbone of the Italian economy. The real stimulus for wider membership among workers in small firms requires more information, financial/pension capability and a set of incentives compensating the employer for the cost of employee enrolment. Another structural gap is the limited participation of public employees.

The report suggests that a number of actions should be adopted to improve the complementary pension system and protect pension fund members without major changes to the regulations.

1. A new institutional campaign aimed at promoting awareness of the new replacement ratio of the first pension pillar should be implemented.

2. Along with this information campaign, a deep, widespread and specialized financial-pension education program should be activated. This program should be aimed at explaining the risks workers face in the retirement period and the way the complementary pension system can help handle them. A specific effort should be made to develop a correct pension view. Particular importance should be given to both the investment and the distribution phase. Some basic principles of rational financial behaviour should become common knowledge of the working population. Particularly, the importance of having a recurrent lifetime income should be stressed.
3. Several profiles must to be implemented in combination:
   a) The regulation should encourage the annuity option while maintaining an adequate balanced flexibility to face important specific needs, using fiscal incentives in favour of the annuity option, and/or modifying the choices available.
   b) Pension schemes should provide different types of annuities at competitive conditions.
   c) Terms and conditions of annuities should be easily comparable. To achieve this, pension schemes should be obliged to provide a clear and complete description of the relevant variables (i.e., interest rates, periodicity, and revaluation criteria). In addition, an adequate comparison format should be implemented, for instance in a special part of the website of the Supervisory Authority.

1.
THE ITALIAN PENSION SYSTEM

1.1
The compulsory and the voluntary private pillars

The Italian pension system is composed of:

- a compulsory, public and unfunded pay-as-you-go system, and
- a voluntary, private and funded pension system which includes collective and individual pension schemes.

The genesis and the evolution of the Italian private funded pension system are closely linked to:

- reforms of the compulsory public system;
- eligibility requirements;
- replacement rates.

1. 2.
Main reforms of the compulsory public pillar

The legal/institutional framework of the Italian public pension system has been heavily reformed through a series of legislative measures adopted in 1992 (Legislative Decree 503/92), 1995 (Law 335/95), 1997 (Law 449/97), 2004 (Law 243/04), 2007 (Law 247/07) and 2009 (Law 102/09).

Calculation methods

With Law 335/95, the Italian pension system is moving gradually toward a new contribution-based calculation method applied to anyone entering the labour market after 31 December 1995. Unlike the preceding method, the new one takes into account both the amount of contributions paid throughout a pensioner's whole working life (capitalised at the rate of nominal GDP), and his/her life expectancy at retirement age, according to actuarial equivalencies.

According to Law 335/95, pension computation and the procedure a worker must follow to access retirement benefits are based on three distinctive methods (contribution-based, earnings-based and mixed), depending on the seniority that worker achieved.

1) Workers with at least 18 years of contributions at the end of 1995 will maintain the earnings-based method. But for contribution years after 1992, the number of years of annual earnings counted in the benefit calculation will increase gradually to reach the last 15 years for self employed workers and the last 10 years for others. Before the 1992 reform, these figures were 10 years for self employed, 5 years for private employees and the last monthly salary before retirement for public employees.

2) However, a so-called mixed pro-rata scheme will be applied to workers with less than 18 years of contribution at the end of 1995. Accordingly, the pension amount is obtained as the sum of two components: the first, related to the contribution years before 1995, is calculated following the earnings-based method with reference to wages for the contribution years between 1993 and 1995, gradually extended to the worker's entire career; the second is calculated according to the contribution-based method described above.

The earnings-based method characterized the first pillar until the so-called Dini Reform (Law 335/95). This method is based on the following three main points: the remuneration taken into account for pension computation (pensionable salary); the yield rate (indicating the percentage to be applied to the pensionable salary for each year of contribution); and the contribution period. Substantially, this system correlates the pension to the average retribution of the final working years, following this equation:

$$P = R \: x \: A \: x \: N$$

Here, the pension benefit P is given by multiplying R (the pensionable salary) by A (yield rate) and by N (contributive seniority). For example, for a retired person with 35 years of contributive seniority and a 2% yield rate, the amount of his/her pension would equal 70% of the pensionable salary.

3) The contribution-based system closely correlates contributions paid during working years and the pension benefit.

The accrued yield is also linked to the GDP trend and not to salary trends. The main feature of this method is that the individual amount accumulated during working years is multiplied by transformation coefficients built on actuarial parameters. This system is able to encourage workers to delay their retirement, which in turn contributes to generating positive effects in terms of savings from pension expenditure.

Transformation coefficients are available for the 57-65 age bracket. According to Law 247/07 they are revised every 3 years, depending on changes in life expectancy and GDP growth rates. These coefficients are in force as of 2010. Table 1.1 and Table 1.2 report previous and new transformation coefficients, respectively.

Table 1.1

Transformation coefficients (Law 335/95)

Age	Coefficients
57	4.720%
58	4.860%
59	5.006%
60	5.163%
61	5.334%
62	5.514%
63	5.706%
64	5.911%
65	6.136%

Table 1.2

New transformation coefficients since 2010 (Law 247/07)

Age	Coefficients
57	4.419%
58	4.538%
59	4.664%
60	4.798%
61	4.940%
62	5.093%
63	5.257%
64	5.432%
65	5.620%

1.3
Eligibility requirements

As in most countries, two different types of public pension exist: old age pension and seniority pension. Eligibility for old age pension is obtained after reaching a minimum age of 60 years for women and 65 for men, provided that a relatively modest tenure condition is met (20 years). As for seniority pension, benefits are paid at a younger age provided that a higher tenure requirement is met.

Considering their formal status, workers registered in the public retirement system can be divided in the following categories:

- employees
- self employed
- self employed professionals

Employees and self employed workers (public and private)

Old age pension

Earnings-based method:

For employees and self employed, men must be 65 years of age and women 60, and both must have a minimum tenure of 20 years to access pension.

Contribution-based method:

Under the contribution-based method accession requires at least 5 years of contributions in addition to a minimum age of 65 for men and 60 for women.

Seniority pension

Benefits are paid at a younger age than old pension, when the sum of age and tenure achieves predefined thresholds. For example, in 2009 the total amount required for employees was 95. This number can be obtained by combining 59 (years) + 36 of tenure or 60 + 35. The total amount (so-called “quota”) increases over time (from 95 in 2009 to 97 in 2013).

Table 1.3 details the qualifications required.

Table 1.3

Minimum requirements for employees to access seniority pension benefits

Benefit accession timeframe	**Employees**		
	Minimum age (yrs)	Tenure (yrs)	Quota
1 July 2009 – 31 Dec 2010	59	36 (35 if at least 60 years old)	95
1 Jan 2011- 31 Dec 2012	60	36 (35 only if 61 or older)	96
1 Jan 2013	61	36 (35 only if 62 or older)	97
With 40 years of contribution, seniority pension is possible without any age requirements			

Source: Law 247/2007

For self employed workers, seniority pension requirements (slightly less favourable than those established for employees) are detailed in Table 1.4.

Table 1.4

Minimum requirements for self employed workers to access seniority pension benefits

Time frame	**Self employed workers who are not engaged in one of the learned professions**		
	Minimum age	Tenure	Quota
1 July 2009 – 31 Dec 2010	60	36 (35 only if at least 61 years old)	96
1 Jan 2011-31 Dec 2012	61	36 (35 only if at least 62 years old)	97
1 Jan 2013	62	36 (35 only if at least 63 years old)	98
With 40 years of contribution, seniority pension is possible without any age requirements			

Source: Law 247/2007

Under the contribution-based method for seniority pension, retirement before the age of 65, in any case and for both genders, is subject a prerequisite pension amount equal to at least 1.2 times the old age allowance (5,317.61 Euro a year in 2009).

The latest reform

The latest reform to date (Law 102/09) provides relevant modifications to eligibility requirements for women employed in the public sector.

Effective 1 January 2010, the old age pension requirements for the above-mentioned workers shall be increased by one year. These requirements are further to be increased by one year as of 1 January 2012, and an additional year for each biennium thereafter, until reaching the age of 65.

Starting from 1 January 2015, the age requirement (for public and private workers) to access the Italian pension system will be adjusted to reflect the higher life expectancy of the population with reference to the previous five years, as measured by the National Institute of Statistics and validated by Eurostat.

Self employed professionals

Self employed professionals (notaries, lawyers, engineers, etc.) are required to provide for their retirement through private institutions. The pension scheme of each such institution fixes its eligibility requirements and calculation methods. Even if the schemes are private they are supervised by public authorities who monitor their solvency.

1.4
Replacement rates

The effect of the new calculation rules under the contributions-based regime is a significant reduction in replacement rates, depending on the hypothesis adopted in calculating these rates. In the following tables we refer to estimates provided by the Italian Department of General Accounts ("Ragioneria Generale dello Stato" or "RGS").

As Tables 1.5 and 1.6 show, self employed workers and young subordinate employees will be particularly impacted.

Table 1.5

First pillar gross replacement rates for private employees

Start of benefit payments / Age	2010	2020	2030	2040	2050
Contribution seniority 30 years					
63	59.1	52.5	47.7	45.2	44.4
Contribution seniority 35 years					
60	71.5	58.8	52.6	48,8	47.9
63	71.5	62.1	57.0	52.8	51.8
65	71.5	64.8	60.4	56.0	54.8
Contribution seniority 40 years					
63	81.6	71.8	66.5	61.0	59.0
65	81.6	74.5	69.9	64.7	62.5

Source: RGS 2008

Table 1.6

First pillar gross replacement rates for self employed workers

Starting of benefits payments / Age	2010	2020	2030	2040	2050
Contribution seniority 30 years					
63	48.1	36.2	28.9	27.5	27.0
Contribution seniority 35 years					
60	71.3	43.4	32.6	29.6	29.1
63	71.3	45.5	35.3	32.1	31.4
65	71.3	47.0	37.4	34.0	33.3
Contribution seniority 40 years					
63	81.3	54.7	44.6	37.0	35.8
65	81.3	56.3	46.7	39.2	37.9

Source: RGS 2008

2.
COMPLEMENTARY PENSION FUNDS

2.1
The “pre-existing” pension funds

Private voluntary retirement funds were established even before legislation covering pension schemes was first enacted in 1993. Some private employers (mostly banks and insurance companies) created internal programs for the benefit of their employees. However, as no special provision regarding pension funds existed at that time, these schemes operated semi-autonomously. To a certain extent these funds still maintain their self-governing status in spite of the current body of reforms governing these schemes.

Pre-existing funds are most numerous among private pension schemes. They enjoy favourable provisions as compared with new pension schemes as far as fiscal treatment, financial management and corporate governance requirements.

The most relevant among these can be summarised as follows:

- Pre-existing funds can directly collect and manage their members’ contributions and pay benefits without intermediaries.
- No depositary bank is required for custody and trading purposes.
- Some of the investment limits mandated for open and contractual funds do not apply.

This peculiar status will change in the future as a result of the specific intervention of the Ministry of Finance (Decree N° 62/2007), which mandates plans to adjust most of the features of these funds before 2012 in order to comply with regulatory frameworks regarding collective complementary pension schemes.

2.2
The complementary pension funds introduced in 1993

A systematic legal framework for complementary pension schemes was first established in 1993 (Legislative Decree 124/93). In the following years new rules regarding benefits, taxation and individual schemes were adopted to foster their development; the main reform was introduced by Legislative Decree 252/2005, the law currently in force.

Another important change in the regulation (Law 296/2006), enacted in the beginning of 2007, involved the devolution of the current severance package (TFR, see the appendix). According to this rule, employees can transfer their annual allocation of severance payments to a

pension scheme or keep them in their employer company. In the latter case, if the firm has more than 49 employees flows are diverted to a specific treasury fund maintained by INPS (Italian National Social Security Institute). If the employee does not take any decision, the tacit consent principle is applied and flows are transferred to a collective pension scheme, if one is contractually identified for the specific category of worker in question. If no contractual scheme is eligible, flows are transferred to a pension scheme specifically established within INPS. The devolution of TFR notably increased the number of accessions and assets under management by the complementary pension industry in 2007.

Basic principles for regulating complementary pension schemes can be summarised as follows:

a) voluntary membership

b) funded schemes

c) financial management assigned to institutional managers: banks, SGR/SIM (for the most part equivalent to UCITS and security brokerage/dealing companies), insurance companies

d) specific supervisory authority (COVIP)

There are three types of pension schemes:

A. occupational closed pension funds

B. open pension funds, with collective or individual membership

C. individual pension plans (PIPS)

All these forms of pension funds must be authorised by COVIP and are under its supervision. They receive the same regulatory and supervisory treatment (for instance as far as fiscal or benefits regimes), but operate with different legal status, governance and operating models, due to their specific nature.

Below we first analyse the most important specific features of funds; then, we discuss some relevant common profiles.

2.2.1
Special features of funds

2.2.1.1
Contractual funds

Establishment profiles

Contractual funds are also called closed funds, since only a specific group of people can join. For instance, in case of employees, membership is reserved to workers regulated by a collective agreement. In case of self employed workers, usually funds are promoted by a professional association and limited to its members. Funds for self employed workers represent a minority.

Funds for employees can be created on a territorial or a company basis, but can also be connected to any other kind of labour organization (e.g.: defining a target group with reference to a plant or a division of a given enterprise). The contractual agreement which establishes a fund can be at national, local or company level; some funds are regional.

Governance

All complimentary pension funds are independent legal entities with their own capital and organization. Corporate governance of these funds is based on the principle of equal representation; usually the Board of Directors and other collective bodies are composed of members representing employees and employers equally. If the president of the Board is nominated by the employer, then the deputy president and the president of the Audit Committee would be elected by employees. Members of the Board and the Audit Committee must fulfil specific honourability and professional requirements.

The Assembly approves the budget, the annual report, amendments to bylaws, procedures for liquidating assets, and elects the Board of Directors and Supervisory Board.

The Board of Directors is responsible for establishing strategies and investment policies, as well as choosing investment managers, the depositary bank and the provider of administrative services. The Audit Committee has a general control duty and control functions.

An important role is played by the General Director or Head of the Fund. This person executes the decisions of the Board and is responsible for the fund, checking that operations are carried out exclusively in the interest of fund members.

Membership requirements and recruitment

Workers can join the scheme only if they meet specific qualifications established in the fund bylaws which accredit them as members of an “aggregation”.

The fund charter initially sets a membership rate target to be achieved within a timeframe defined by the supervisor. If this threshold is achieved, the supervisor authorizes the fund to start its business. After this, the fund can begin collecting contributions from members.. However,

contributions are not invested until the pool reaches a minimum amount and a financial intermediary is mandated to manage fund resources.

The business model of contractual funds is based on a close relationship between stakeholders and potential members. The most common ways to recruit new members is through the efforts of employers' Human Resource offices, trade union representatives in the territory and by holding periodic meetings in the workplace. No fee or commission is due for this process. This represents an important competitive advantage when both sponsors of the fund (employers and union representatives) have credibility as far as aggregating potential members. Membership is facilitated if the fund's sector of reference is concentrated, because contacts with employees are easier to obtain and manage.

Scheme funding and contribution

At the moment all pension funds are defined as contribution schemes. The contribution amount is established by the fund's bylaws. Typically, funds are financed through contributions from both the employee and the employer, and through the TFR (for subordinate employees). Supplementary contributions are also allowed.

Investment management

Contributions flow into the individual account of each member and are invested by financial managers appointed by the fund and selected exclusively among banks, SGR/SIM or insurance companies.

On the basis of the pension needs of its potential members, the fund defines the strategic asset allocation of its investment portfolio, structures the mandates, fixes their duration, decides the number of financial managers and selects them according to a process regulated and controlled by the supervisor.

The process starts with an invitation to tender in which the fund defines the selection criteria with reference to many requirements: amount of capital; assets under management consistent with the asset class of the mandate; past experience in pension fund management; composition, stability and structure of the management team responsible for the relationship with the fund; fees required; quality of reporting.

At the end of the process, one or more financial managers are selected. They sign a contract with a service level agreement defining all the conditions regulating their respective obligations. The contract can allow sub-delegation to another asset manager.

Regulations oblige the fund to be aware of the level of risk its members are exposed to. This requires financial managers to comply with the risk profile defined by the fund with an ex-ante approach. Since the majority of mandates are based on a specific benchmark, the agreement states ex ante a level of risk to be respected in terms of Tracking Error Volatility (TEV). Some mandates have risk profiles expressed in terms of Value at Risk (VaR).

The occupational fund destined to receive flows of contributions due to tacit consent in the devolution of TFR must have a specifically established sub-fund which guarantees at

least capital repayment. An additional yield giving an annual performance in line with the one prescribed by law for TFR should be achieved on a best-effort basis.

The fund can offer other guaranteed sub-funds in different ways. The common feature of every guaranteed sub-fund is that it is given on an event-occurrence basis. Events that can trigger the guarantee usually do not depend on members' free will, such is the case for date of retirement, death, severe disability, or unemployment after a certain period. In a few cases the guarantee applies when members switch to another fund, or when the financial managers' contract end.

Another typical sub-fund offered by the majority of contractual funds is based on an asset allocation of 70 % bonds and 30 % equities, with an overweight or underweight approach and a varied composition of government/corporate bonds, rating and geographical area. Many funds offer more aggressive asset allocation for younger members or those with less risk aversion. Mobility within sub-funds is low and the majority of members belongs to the same typically conservative sub-fund.

Usually funds have a very simple structure and limited know-how in financial management, except for some board members. Therefore, in many cases the fund is supported in the selection process by external advisors; this can also contribute to controlling financial managers.

Fund and financial managers are in close contact and meet periodically to discuss results, prospects and the opportunity of changing tactical asset allocation. This cooperation is essential to the relationship and important for the renewal of the mandate on maturity.

The fund must report at least on an annual basis, but fund websites can provide information to members more frequently. The fund and the financial managers have to consider the bias that frequent reports might cause on an investment process that should be long-term oriented. More recently the duration of mandates was extended with respect to the past: initially they typically lasted three years, while at present duration is five years or even more in specific asset classes.

Trading is materially conducted by a depositary bank.

Scheme administration

Due to the small structure of its business model, occupational funds typically outsource the administration process in order to reduce the investments required for their establishment.

The role of administration is crucial because it manages all the information about cash flows coming from fund members and their employers and links them with information and cash flows coming from the investment, benefits, and annuitisation processes. Therefore, administration records new members, contributions collected, investment strategies chosen and other similar data. In addition, this function calculates the value of individual positions and amount of benefits, and pays dues to pensioners and members. Moreover, administration supplies the fund with book-keeping activity and provides the scheme with information needed to draft the annual report.

Depositary bank

As mentioned, the law requires that a depositary bank keep the assets in custody and conduct trading activities ordered by financial managers.

Trading is therefore materially conducted by an entity different from financial managers**.** This entity is charged with verifying their activities and carrying out their instructions only if compliant with the law, the regulation of the supervisor, the fund’s bylaws and the appointment agreement. Regulation does not strictly forbid the depositary bank and financial managers from belonging to the same group. However, many occupational funds require this independence. The fund must select a depositary bank through an invitation to tender, as previously mentioned for other external entities.

Costs

Pension fund costs mainly consist of administrative and financial fees due to institutions in charge of asset management, custody services and administrative activity. Overheads are generally low because members of the board usually receive token compensation. As mentioned, no fee is due for gathering memberships, but the fund bears the costs of training representatives, organizing assemblies and communicating with potential members. Financial fees are directly deducted from the schemes’ assets, while administrative costs and overheads are covered by debiting a periodic membership fee (usually directly from contributions). Moreover, new members pay an entry fee, and members who want to exercise a specific option (e.g. switch to a different sub-fund, redeem their individual position or transfer their balance to another scheme) are charged a modest commission.

As funds are no-profit organisations, if administrative costs are less than the fees collected to cover them, the difference is credited to members’ single positions.

Taking these features into account, the business model of contractual funds is efficient if a certain number of members sign on.

Cost impact on member balances is measured by an index named ISC (*Indicatore sintetico di costo* or *Cost Impact Index*); the calculation methodology for this index is established by the supervisor (see Appendix). Funds must also compute a second index called TER (Total Expense Ratio) which is the ratio of total costs over total assets at the end of the year.

While the ISC is an ex-ante evaluation of future costs, the TER is computed on an ex-post basis and therefore reflects the past impact of costs on members. Both the ISC and the TER have to be regularly disclosed to members.

2.2.1.2
Open funds

Establishment profiles

Open funds are potentially addressed to all categories of workers. They are open, in the sense that membership is not restricted to a specific group as in the case of closed funds.

Open funds are established by the same organizations that can manage financial resources of pension funds: banks, SGR/SIM and insurance companies.

The Board of Directors of these institutions establishes the fund according to a specific set of rules allowing it to operate similarly to closed funds after receiving COVIP authorisation.

Governance

An open fund is not an independent legal entity, but resources received by members have special status as they are legally separated from the entity which manages the fund, and as such can not be executed by creditors of the sponsor company (according to Article 2117 of the Italian Civil Code). Therefore the fund does not have its own administrative bodies, but does have a specific governance system.

The fund can be established for a collective or an individual membership or both. Collective membership is based on an agreement between stakeholders, typically at company level, stating the fund's membership rules. The difference with respect to closed funds lies in the lack of representatives of stakeholders in the governance bodies of open funds. In addition, these funds are not limited to the group who signs the agreement because other communities can also join. Therefore, open funds can represent an opportunity for small or medium-sized groups of workers. Since the same fund can receive both collective and individual memberships, people who join belong to various organizations.

Governance rules try to balance the power between the sponsoring institution and members. In fact, in both collective and individual membership schemes, the person appointed responsible for the fund must be independent from the establishing institution and fulfil honourability and professional requirements. She supervises all the fund's activities and ensures that the fund is operating in the sole interest of its members.

In funds with collective membership, in addition to the responsible for the fund, governance rules require the presence of another control body, made up of at least two people. In case of collective membership of more than 500 workers belonging to the same company or group, the control body is integrated with two additional members, one nominated by the employer and the other by employees. Clearly this is an attempt to replicate the typical criteria of collective bargaining, with reference to a different legal structure.

Membership requirements and recruitment

No requirement is set for individual membership. Collective membership requires employment by the employer who signed the agreement.

Due to the specific nature of the fund, the sales force of the sponsoring institution is primarily responsible for gathering memberships. Collective memberships are proposed by specialists at corporate level, while individual membership is the task of the retail sales force, spread throughout the territory.

Scheme funding and contribution

Collective membership is funded with contributions from the employer, employees and TFR. To receive TFR of workers who neglect to make a choice (tacit consent), the fund must have a specially-created guaranteed sub-fund, as previously seen for closed funds.

Individual membership is voluntary.

Investment management

Each plan offers various investment options; usually as a base package a fixed income, a mixed bond, a balanced and a stock sub-fund are offered to members. As mentioned before, the fund may allow collective membership targeting workers who fulfil specific requirements. If so, and the fund is willing to gather contributions coming from the tacit consent principle, one of the investment alternatives offered must give a guarantee for the capital linked to specific events. Contributions can be split among different sub-funds if the scheme allows members to do so.

As open funds are managed by financial intermediaries, the asset management process is directly handled by the institution that created the scheme. However, fund management can be assigned to a third party appointed to conduct specific operations.

Scheme administration

The administrative process can be outsourced.

Depositary bank

A depository bank is required as with closed funds.

Costs

Some costs are charged at the beginning of membership, while others are levied each year to absorb administrative expenses. A part of costs covers paying the sales force.

These costs and the relative incentive to sell are the most important differences between this business model in comparison with closed funds. The strong relationship between banks and the employer, reinforced by credit needs, can give banks a competitive advantage in signing collective agreements.

Costs impact is measured by ISC and TER indexes, which must be periodically disclosed to members.

2.2.1.3
PIPs (individual pension plans)

Establishment profiles

This pension scheme, operating exclusively on an individual basis, consists of an insurance contract compliant with rules on complementary pension schemes, for instance related to benefits, fiscal treatment, portability, supervision and so on.

As with open funds, the board of the insurance company establishes the scheme and asks COVIP for authorization to become fully operational.

Since 2007, a new type of insurance contract has been issued, fully compliant with the new regulation.

Two types of insurance contracts are offered: with-profits and unit-linked. In same cases, a combination of both types is possible to attain a more flexible risk profile. Usually with-profit policies give a minimum annual interest rate, guaranteed and consolidated in the accounts of the company, plus a quota of financial performance as recorded at the end of the year. Unit-linked policies normally have no guarantee and their performance depends on the value of the unit in which contributions are invested. PIPs can offer additional coverage in case death, long term care or disability, sometimes as a bundled package.

Governance

As with open funds, PIPs are not independent legal entities and the resources received by members have a special status as they constitute a separate fund from the establishing entity and can not be executed by creditors of the sponsor company.

An independent person must be appointed responsible for the scheme with the same powers and requirements as for open funds.

Membership requirements and recruitment

There are no requirements in order to qualify for accession to insurance policies besides premium payment.

As with open funds, membership is mainly driven by the commitment of the sales force.

Scheme funding and contribution

Contribution is flexible. In most cases premiums can either be paid at any time or on a monthly basis. The amount of premiums is chosen by the insured party within limits agreed upon with the insurance company. Premiums can also be inflation indexed, so that the money accrued during the accumulation phase keeps its real value. Subordinate employees can pay into the scheme both with their own money and their annual share of the severance payment. As PIPs are individual accession pension plans, there is no contractual agreement with the member's employer governing additional contributions.

Investment management

Investment activity is carried out directly by the insurance company offering the policy and no intervention by a depositary institution is required. Investments must adhere to the same rules that apply to insurance policies - whose limitations are different in part from those mandated for closed and open funds. Investment activity is primarily regulated by the Code of Private Insurance (Legislative Decree 209/2005), which governs insurance activities in general. The insurance company can delegate the investment process to a third party.

Scheme administration

The insurer handles all phases of the process, from selling to paying benefits.

Costs

Types of costs are similar to open pension funds and are influenced by guarantees and insurance coverage offered. The impact of the sales force can be relevant, but the service level given to the customer by insurance specialists can be appreciable as well.

Cost impact is measured by ISC and TER indexes, which must be periodically disclosed to members.

2.2.2. Common features of funds

Benefits

Contributions and returns from investments allow members to accumulate an amount of money that will become available at retirement or, if certain conditions are met, even before.

Provided that enrolment seniority reaches a minimum of 8 years, members can obtain an advance payment up to a maximum of 75% of their individual account for purchasing or remodelling their first house or that of their children. In addition, up to 30% of the account can be

requested for any type of need. Moreover, at any time members can demand an amount of money up to 75% for extraordinary medical expenses related to their family.

Members can use one or more of these advance payments within regulatory limits. For instance, they can use the 30% limit to face whatever their need may be, but can not receive more than 45% (30+45=75%) for the purchase of a house. Participants can subsequently reimburse the money, thus restoring their position.

The existence of different options underscores the high level of discretion given by the complementary pension system to participants, deriving from the similar social role of TFR. Since TFR has historically acted as a social safety net, the elasticity of pension options has been a pre-condition for the devolution of TFR to the complementary pension system.

In particular, the provision regarding the allowance for any need can distort the fund's role as a pension device. Of course there is a trade-off between the flexibility requested to develop complementary pension schemes and incentives given for the annuitisation option.

However, rules concerning transferring from TFR to the complimentary system bear an inner inelasticity, because this choice can not be reversed. This constraint may have induced many workers to prefer the option of leaving TFR in their firms, maintaining the status quo.

At retirement, members must fulfil requirements under the public seniority pension regime in terms of both minimum age and tenure, provided that their participation in the scheme lasted at least five years. Note that participation does not necessarily imply the payment of contributions: plan affiliation qualifies for benefit accession even when no money is paid in (e.g. if the plan member is unemployed but still in possession of membership requirements).

At retirement, fund members have the following alternatives:

I. The total individual position can be converted into an annuity.

II. Up to 50% of the individual position can be paid in a lump sum, and the difference converted into an annuity.

III. If at least 70% of the individual position converted into an annuity is less than the 50% of the public social pension (a sort of minimum public pension equaling Euro 5,317.65 annually in 2009), the member can obtain the total payment as a lump-sum.

Currently, the annuity option is not encouraged since the calculation stated by law is made on the basis of the position net of the amount received in advance and not paid back. For instance, consider an individual position of 100. If the pension member receives 40 for restructuring his/her house and does not repay this amount, the 50% rule for splitting lump-sum and annuity is applied to 60 instead of 100. In this way the pension member can obtain 70 as a lump-sum (40 plus 30), but only 30 can be used for the annuity. The same mechanism applies to the alternative which correlates the annuity to the social pension. Since a part of the advance payment is for unqualified needs, the member preferring cash payment can demand an advance payment to reduce the amount to be converted into an annuity. This rule was created to avoid very small annuities, but can be an important incentive against annuitisation.

Members can postpone their choice at will; however, several partial annuitisations are not allowed.

If a member either loses the qualifications for participation (e.g. taking a new job with an employer who is not included in the contractual fund target) or discontinues work for more than

48 months, the regime allows him/her to exercise a total surrender option. This implies liquidation of the entire individual position. Otherwise, in case of membership qualification loss, the individual position can be transferred to another pension fund or kept in the original scheme without further contributions.

Total surrender is also allowed in case of:

- death
- permanent disability reducing working capability to one third.

A partial surrender (up to 50%) is permitted in unemployment periods between 12 and 48 months, or if social welfare support provisions are in force.

In any case, after two years of participation, members are free to transfer their position to another scheme.

The annuity

All forms of pension schemes give members the opportunity to buy an annuity. Occupational funds usually select insurance companies through a tender, as for other outsourcers. Insurance companies promoting open funds or PIPs, however, are allowed to provide their own products. Other open funds draw up specific agreements with an insurance company.

Many types of annuity are provided:

a) single lifetime
b) reversible
c) certain for 5 or 10 years (or more), then lifetime
d) lifetime with reimbursement of premiums in case of death
e) lifetime, increased in case of long term care

All these products have a minimum guaranteed interest rate. The amount of the annuity can increase according to rules on extra financial returns attributed to annuitants.

Fiscal treatment

Italy adopted an ETT system as an incentive to complementary pension schemes. Therefore, contributions enjoy favorable fiscal treatment, while accrued yields and benefits are taxed.

Contributions can be deducted from workers' taxable income up to 5,164.57 Euro per year. Employers' contributions are included in the ceiling calculation.

Investment returns on funds are taxed at a 11% rate.

In order to avoid a double levy, benefits are taxed only for the share not already assessed during the accumulation phase. Therefore, taxation at the time of retirement applies only to deducted contributions, since non-deducted contributions and investment returns have already been taxed.

Both annuities and lump-sum payments enjoy the same fiscal treatment. The tax rate on benefits varies from 9% to 15%, depending on the length of member participation. The maximum

rate is charged to members whose seniority is lower than 16 years. The rate decreases yearly until it reaches its minimum at a tenure of 35 years.

Finally, if the surrender option is exercised, the accrued capital for the share not already assessed is taxed at a fixed 23% rate, corresponding to the minimum marginal personal income tax rate in Italy.

Supervision and disclosure rules

COVIP is the supervisory authority FOR all pension schemes. This organization is responsible for ensuring the transparent and fair behaviour of fund sponsors, the sound and prudent management of funds, the overall protection of members and the proper functioning of the complementary system.

COVIP regulates the sector according to principles established by law, authorises operations of funds and monitors their activity. Since Italian laws, including those on complementary schemes, leave considerable room for interpretation, the position of COVIP has heavily influenced the sector in this country.

Rules on transparency are of great interest for the protection of members and have a significant impact at operational level.

Before enrolling in a plan, potential members must be properly informed of its features, in order to choose the most suitable option . Moreover, as mentioned, the law allows members of retirement schemes to transfer their balance to a different plan, provided that a two-year participation requirement is met.

For this purpose, COVIP mandates fund sponsors to provide potential members with a form disclosing all the details needed to evaluate the drawbacks and advantages of their plans.

This form is divided in two main parts:

I. The first part summarises the most relevant features of the plan in a concise way, giving potential members the opportunity to easily compare alternatives. This section includes information such as: the plan and the name of its sponsor, qualifications requested for participating in the scheme (if any), amount and frequency of contributions; names and main features of available sub-funds (such as categories of securities in which money is invested and the level of risk exposure), past returns of each sub-fund; the existence of additional guarantees (e.g. death benefits and relative costs, if any); cost provisions; impact of costs on members' balances via the concise cost index (ISC), and its components for each sub-fund. This index shows the annual cost a member would pay for staying in the scheme for a defined period of time (for example, 2 or 5 years). The ISC index calculation is reported in the appendix.

II. The second part is more detailed and complete, consisting of many pages. Further information is provided about asset composition of each sub-fund, relative risk, past performance, and total expense ratio broken down for different cost categories. This part contains a glossary and a list of institutions involved in the plan's management, along with a detailed description of their roles and relationships with the plan sponsor.

In order to foster awareness of potential outcomes of investment activities in pension schemes, COVIP has mandated plan sponsors to supply both members and potential members

with an evaluation of the benefits available at retirement, according to various scenarios regarding the relevant calculation variables (i.e. contribution rates, accumulation phase length, sub-fund chosen and related returns, age at retirement, gender and so on). Retirement scenarios must also be accessible via sponsor websites, so that potential and active members of the scheme can assess their position and simulate changes by choosing the most suitable set of parameters.

In addition to all this, members of the plans receive an annual report that details activities of their scheme and results achieved, along with a customised assessment of future benefits should they keep investing in the plan until retirement.

Members must also be able to find information regarding the scheme and their personal situation through the sponsor's website, whose contents are strictly regulated. In addition to a detailed list of documents that must be accessible through the Internet, COVIP requires that members have the possibility to monitor their balance at any time by means of on-line inquiries on individual accounts.

Rules on investments

The financial management of pension schemes is of great concern because of the economic and social role assigned to such investment vehicles. Pension assets have to be managed according to prudent rules that should not jeopardize the value of the future pension benefits. These rules encompass, among other things, a set of constraints on pension fund management and provisions aimed at regulating any possible conflict of interest. As a consequence, open pension funds, closed pension funds, and PIPs are regulated by a single law as far as conflict of interest is concerned (involving the fund, its members and the selected financial managers). Conversely, the financial management of pension schemes is regulated by two different norms: (i) investment activities of open and closed pension funds established after 1993 are governed by Decree 703/96; (ii) financial management of PIPs is governed by Decree 209/05, which applies to all pip.

The main contents of Decree 703/96 are summarized below. The Decree includes the following:

- an array of general criteria with which the investment activity must comply;
- a list of financial instruments in which fund managers can invest relative assets and a list of permissible and prohibited activities;
- a list of quantitative limits (summarized in the appendix);
- a rule for the use of derivatives;
- a provision regarding conflict of interest (which also applies to PIPs).

Investments must comply with a general "prudent man" rule, which is very similar to the one envisaged in Directive 2003/41/CE. The fund's assets have to be effectively diversified and efficiently managed, also considering transaction costs. Investment activity must aim at maximizing net return at a reasonable risk level.

Permissible investments exclusively include the following asset classes:

- bonds;
- stocks;

- mutual and closed end funds shares;
- derivative securities;
- cash and bank deposits.

Repo operations are allowed and funds can also lend and borrow securities. Real estate investment is possible by means of participating in real estate closed end funds only. Short sales are not permitted, nor are lending and surety standing activities. At least one third of the fund's assets must be invested in the currency in which the benefits will be denominated. Derivative coverage has to be considered when calculating this limit.

2.3.
The Complementary pension schemes for public employees

The law in force (Legislative Decree 252/2005) states that the supplementary pension for public employees will be addressed in a another decree, which has not yet been issued. As a result, the sector is still regulated by the original legislative framework created in 1993.

This lack of continuity is due to the relevant differences between the public and private sectors and their compatibility.

The most important differentiation is severance pay, which is regulated in a different way and is not funded in the public sector. INPDAD (the compulsory pension provider for public employees) takes on this debt for the State and credits workers, guaranteeing future payment when due, at retirement, in case of loss of employment, or granting loans in case of defined needs.

Another problem relates to the role of the State as employer; the contributions due by the employer impact public expenditure.

For these and other complicated legal reasons, the participation of public employees in the complementary pension system is limited. While these workers can join a pension fund on an individual basis, contractual membership is currently possible only for school personnel (Espero). Two other public sectors, namely the National Health Service and regional/local authorities, signed an agreement in 2007 to set up new funds (Perseo and Sirio respectively), but these funds have not been yet established.

3.
EVOLUTION OF THE PENSION FUND INDUSTRY

3.1.
Market size and trends

3.1.1
General overview

Looking at the size of the Italian private pension industry, two main features deserve to be highlighted.

Firstly, the sector is still at an early stage. In fact, despite the continuous growth of the number of members and assets under management (as shown in Figures 3.1; 3.2.a and 3.3.a), workers participating in private pension schemes account only for 20% of the relevant population. The participation rate is negligible, a mere 2.8%, if public sector employees are considered. Conversely, private sector employees participating in pension schemes are about 26% of the working population (Table 3.1). Overall, there is still room for growth.

Table 3.1

Italian private pension schemes: participation rates (2008 year-end)

	Workers participating in private pension schemes	Workers	Participation rate (%)
Private sector employees	3,603,000	13,873,000	26.0
Public sector employees	137,000	3,573,000	3.8
Self-employed workers	1,114,000	5,959,000	18.7
Total	*4,854,000*	*23,405,000*	*20.7*

Source: COVIP

Secondly, distribution of members among the different schemes is not homogeneous (see Table 3.2). Namely, a large number of members (around 40%) participates in contractual funds, compared with 27% in PIPs, 16% in open funds and 14% in pre-existing funds, while most of the net asset value under management refers to pre-existing funds (around 60%). The reasons are easy to understand. On one hand, contractual funds are typically established by worker and firm representatives or by unions, that is by institutions that can easily reach the majority of workers. On the other hand, the longer life of pre-existing funds makes it easy for them to accumulate a significantly larger set of assets under management. For the same reason, while about half of the

policyholders own policies that are compliant with Legislative Decree 252/2005, 66% of the net asset value of PIPs belongs to "old" policies, as shown in Table 3.3.

Table 3.2

Italian private pension schemes: number of schemes, members and net asset value (2008 year-end)

	Schemes	Members	Net asset value [1]
Contractual funds	39	2,043,509	14,092
Open funds	80	798,007	4,663
PIPs	n.a. [2]	1,314,353	6,593
Pre-existing funds	411	677,453	35,941
Total	*n.a.*	*4,853,605*	*61,306*

(1) Millions of Euro.

(2) The number of PIPs is not available, since COVIP provides statistics only for those (75) compliant with Legislative Decree 252/2005.

Source: COVIP

Table 3.3

Old and new PIPs: number, members and net asset value (2008 year-end)

	Policies	Members	Net asset value [3]
Old PIPs [1]	n.a.	674,332	4,636
New PIPs [2]	75	701,819	1,958
Total	*n.a.*	*1,314,353*	*6,593*

(1) not compliant with Legislative Decree 252/2005.

(2) compliant with Legislative Decree 252/2005.

(3) Millions of Euro.

Source: COVIP

Focusing on pre-existing pension funds, it is worth noting that most of members and net asset value refer to autonomous (incorporated) funds rather than internal funds (Table 3.4). The former type of fund is twice as numerous as the latter.

Table 3.4

Pre-existing pension funds: number, members and net asset value (2008 year-end)

	Schemes	Members	Net asset value [1]
Autonomous	273	646,154	32,691
Internal	138	31,233	3,250
to banks	*121*	*30,711*	*3,121*
to insurance firms	*7*	*65*	*35*
to non-financial firms	*10*	*523*	*94*
Total	*411*	*677,453*	*35,941*

[1] Millions of Euro.

Source: COVIP

As specified in Chapter 2 most pension schemes are constituted in the form of "*multicomparto"* funds, that is they offer more than one investment option to their members, providing the possibility to choose among different sub-funds, one of which is typically a guaranteed sub-fund. Therefore, a possible investor in the Italian private pension industry would face a number of alternatives that go well beyond the number of schemes. Table 3.5 reports the number of sub-funds available for each of the three pension schemes. The table also provides: the number of non-guaranteed and guaranteed sub-funds and the number of schemes that do not offer a guaranteed sub-fund and that offer more than one guaranteed sub-fund.

It is worth noting that the number of open funds and new PIPs in this table differs from the one reported in previous tables. Such differences (which also occur in some of the subsequent statistics) are due to a difference in the date of information acquisition (June 2009 instead of year-end 2008).

Table 3.5

Italian private pension schemes: number of guaranteed sub-funds (June 2009)

	Schemes	Sub-funds	Non-guaranteed sub-funds	Guaranteed sub-funds	Schemes with no guaranteed sub-funds	Schemes with more than one guaranteed sub-fund
Contractual funds	39	122	82	40	1 [1]	2
Open funds	79	351	256	101	7	22 [2]
PIPs [3]	73	169	103	67	8	1

[1] Fondosanità

[2] Two funds have three guaranteed sub-funds.

[3] Compliant with Legislative Decree 252/2005.

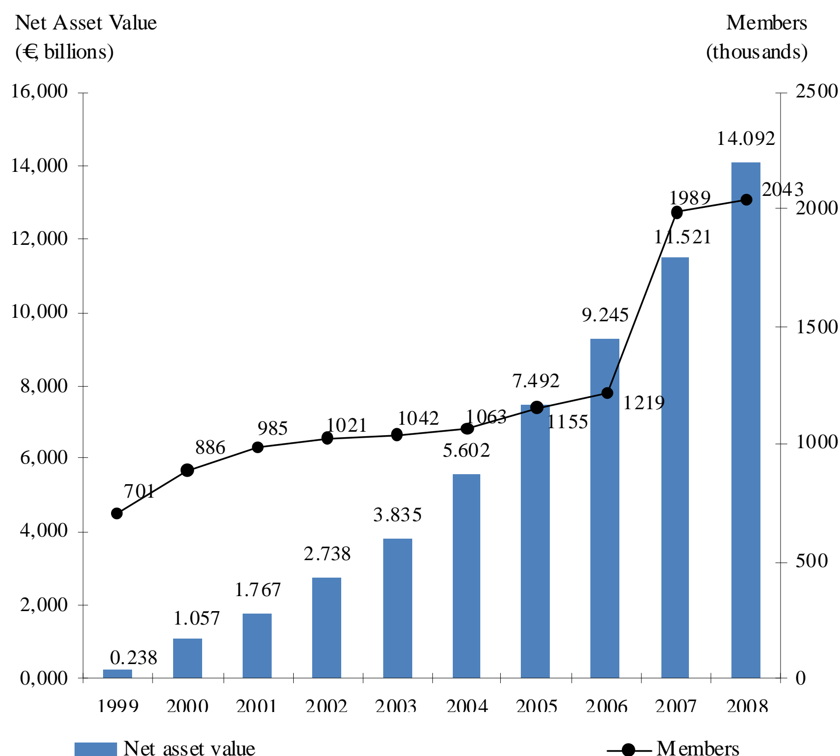
Sources: COVIP and fund prospectuses

3.1.2
Contractual funds

Contractual funds made their first appearance in 1999 when the delegated financial management of pension fund assets started for the first time.[1] Since then, as their number increased, these funds have continuously enlarged both the bulk of their asset value and the number of their members, with a huge increase in 2007 due to TFR reform.

Figure 3.1

Contractual pension funds: members (thousands) and total net asset values (millions of Euro) from 1999 to 2008



Source: COVIP

[1] *The first pension fund with assets handled by a financial manager was Fonchim, the contractual pension fund for workers in chemical, pharmaceutical and related industries.*

While on average, the participation rate in private pension schemes is 21% (26% for private sector employees), as far as the contractual pension schemes are concerned, figures are very different and change over time (Table 3.6). Of course, funds with a higher participation rate are typically older; these funds may also have sponsors who enjoy a strong influence over the potential members or a canvassing presence in the territory. Therefore, in 2008 in 6 out of 39 contractual pension funds the participation rate was above 80% but below 10% in 11 (most were newly constituted). Conversely, in 2005 no contractual fund had a participation rate exceeding 80%, and 11 out 33 funds still showed a participation rate lower than 10%.

Table 3.6

Italian contractual pension funds: members, net asset value and members as % of total maximum number from 2005 to 2008

	2005			2006			2007			2008		
Contractual funds	Members	Net asset value (€, thousands)	Members (% of total maximum number)	Members	Net asset value (€, thousands)	Members (% of total maximum number)	Members	Net asset value (€, thousands)	Members (% of total maximum number)	Members	Net asset value (€, thousands)	Members (% of total maximum number)
Fonchim	117,434	1,216,407	63.0%	122,684	1,507,580	60.7%	166,438	1,815,902	82.4%	162,659	1,940,475	80.5%
Fondenergia	29,506	408,320	71.4%	30,490	481,536	74.4%	42,315	584,347	86.4%	42,706	627,392	85.4%
Quadri e Capi Fiat	11,660	156,378	79.9%	10,587	162,789	75.6%	12,349	189,065	85.2%	12,107	201,769	83.5%
Cometa	321,882	2,505,085	32.2%	314,159	2,914,602	31.4%	476,084	3,392,711	47.6%	475,123	3,970,585	47.5%
Fondo Sanità	3,258	41,957	1.0%	3,286	50,374	1.0%	3,337	56,234	1.0%	3,445	53,089	1.0%
Solidarietà Veneto	15,959	83,752	4.6%	18,544	102,423	5.3%	44,192	151,664	12.6%	45,296	225,497	12.9%
Previambiente	21,516	127,790	51.2%	23,132	159,223	55.1%	39,440	195,856	15.8%	44,589	247,427	17.8%
Alifond	34,013	232,329	11.3%	35,104	280,877	11.7%	55,057	357,337	18.4%	54,562	407,249	18.2%
Laborfonds	76,437	366,243	31.2%	82,832	453,726	33.8%	110,980	560,815	45.3%	112,495	561,396	45.9%
Cooperlavoro	15,497	85,361	6.2%	16,421	109,567	6.6%	60,290	153,298	20.1%	69,672	229,006	23.2%
Pegaso	21,594	146,347	49.4%	22,534	177,146	51.6%	30,039	216,765	66.8%	30,130	249,661	66.9%
Fopen	42,248	460,719	76.8%	41,373	535,097	75.2%	46,485	621,536	84.5%	45,491	651,597	82.7%
Arco	20,099	70,662	8.8%	21,183	91,458	9.3%	41,602	127,184	18.2%	41,759	171,780	18.2%
Previcooper	11,876	73,726	12.3%	13,300	94,602	13.8%	32,139	133,122	33.1%	32,956	180,221	33.9%
Previvolo	2,692	141,018	77.4%	2,710	178,701	90.3%	3,089	211,780	88.3%	3,087	198,734	88.2%
Telemaco	57,269	383,484	47.7%	55,508	442,029	46.3%	65,559	511,881	54.6%	66,999	590,006	55.8%
Foncer	8,785	65,296	27.5%	9,496	78,644	29.7%	15,880	101,306	49.6%	18,559	139,108	57.9%
Previmoda	39,136	133,639	8.7%	40,078	158,099	10.0%	72,318	210,602	18.1%	71,143	280,419	17.9%
Fondapi	23,542	102,225	3.0%	23,471	125,019	4.7%	44,313	166,607	8.9%	44,785	220,048	8.9%

Fonte	22,528	131,434	1.1%	25,579	171,941	1.3%	130,811	284,283	6.5%	159,256	568,831	7.9%
Concreto	5,801	25,464	52.7%	6,012	33,570	57.3%	8,028	41,845	80.1%	8,050	56,818	80.5%
Filcoop	2,470	5,315	1.5%	2,981	7,939	1.9%	8,455	12,654	5.3%	10,461	22,332	6.5%
Prevaer	5,873	32,387	16.8%	6,455	48,112	20.8%	10,186	66,349	32.9%	11,036	95,658	35.6%
Gommaplastica	29,829	113,374	23.9%	31,394	149,121	30.8%	57,159	219,008	57.2%	57,951	297,344	57.9%
Mediafond	2,026	10,877	63.3%	2,090	13,895	34.8%	2,689	18,156	44.8%	2,783	23,941	37.1%
Byblos	25,355	96,388	14.1%	25,368	129,195	12.7%	38,926	176,877	19.5%	40,207	225,425	20.1%
Eurofer	30,640	162,859	32.4%	32,125	211,566	33.9%	44,408	265,859	43.5%	43,633	331,814	42.7%
Fondav	3,682	43,421	36.8%	3,727	57,400	37.3%	4,953	74,947	49.5%	4,965	83,578	49.6%
Prevedi	23,287	19,751	3.1%	26,491	39,271	3.5%	53,726	77,087	7.2%	55,983	148,019	7.5%
Priamo	36,018	112,820	32.7%	42,547	171,008	38.7%	60,287	252,717	54.8%	61,374	344,930	47.2%
Fopadiva	1,492	1,407	4.3%	1,804	2,710	5.2%	6,052	65,124	17.3%	6,306	66,212	18.0%
Fondoposte	31,979	48,049	21.3%	36,009	91,146	24.0%	82,545	165,668	52.2%	86,503	315,587	54.7%
Marco Polo	1,124	715	0.1%	1,252	2,105	0.2%	5,102	4,902	0.6%	6,153	14,584	0.7%
Espero	*n.o.*	*n.o.*	*n.o.*	53,151	12,000	5.6%	77,756	78,009	6.5%	82,680	153,652	6.4%
Astri	*n.o.*	*n.o.*	*n.o.*	6,166	7,210	51.4%	7,732	23,403	51.5%	7,996	40,302	53.3%
Artifond	*n.o.*	*n.o.*	*n.o.*	*n.o.*	*n.o.*	*n.o.*	7,519	2,419	0.6%	9,764	14,548	0.8%
Agrifondo	*n.o.*	*n.o.*	*n.o.*	*n.o.*	*n.o.*	*n.o.*	2,004	1,210	0.6%	2,864	5,227	0.9%
Previlog	*n.o.*	*n.o.*	*n.o.*	*n.o.*	*n.o.*	*n.o.*	7,381	4,024	7.4%	8,543	17,788	8.5%
Previprof	*n.o.*	*n.o.*	*n.o.*	*n.o.*	*n.o.*	*n.o.*	609	293	0.1%	822	1,528	0.1%

n.o. means that the fund was not operating at that time.

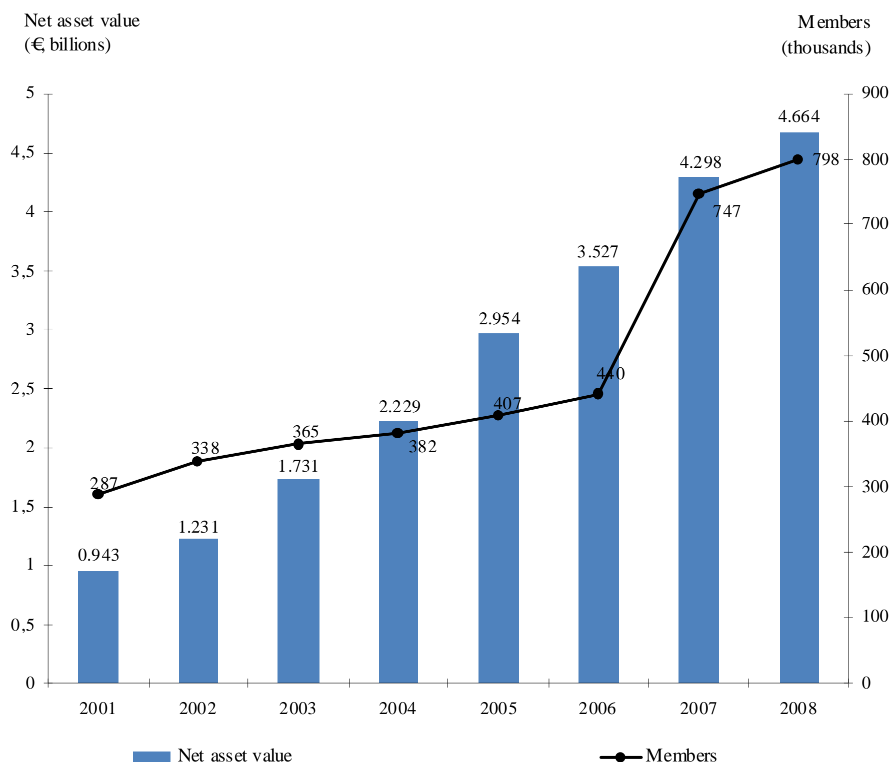
Source: COVIP

3.1.3
Open funds

Dynamics of membership and contributions of Italian open funds are quite similar to those of contractual plans: constant growth of both figures over time and a strong increase of members in 2007 (around 70%) (Figure 3.2.a).

Figure 3.2.a

Open pension funds: members (thousands) and total net asset values (millions of Euro) from 2001 to 2008



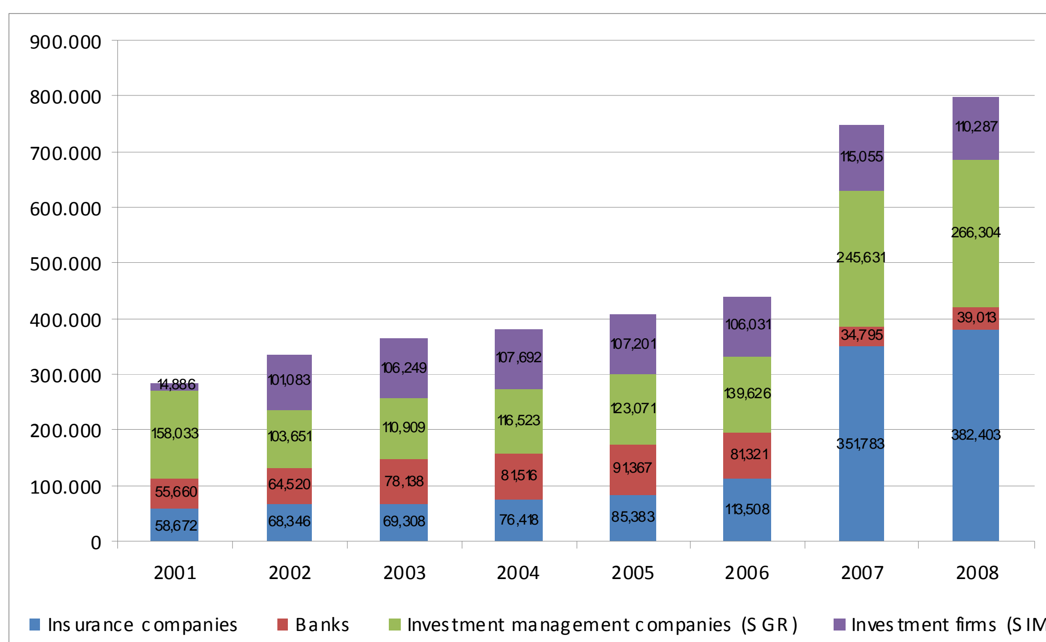
Source: COVIP

Interestingly, growth in number of members and net asset value have not increased at the same pace in open funds promoted by different financial institutions. As Figure 3.2.b and Figure 3.2.c show, 48% of open fund members were enrolled in schemes promoted by insurance firms in 2008; moreover these schemes owned around 44% of the open pension funds' total net assets. In

2005 members and net asset value of insurance firms' schemes accounted for 21% and 24% respectively and in 2001 for 20% and 21%.

Figure 3.2.b

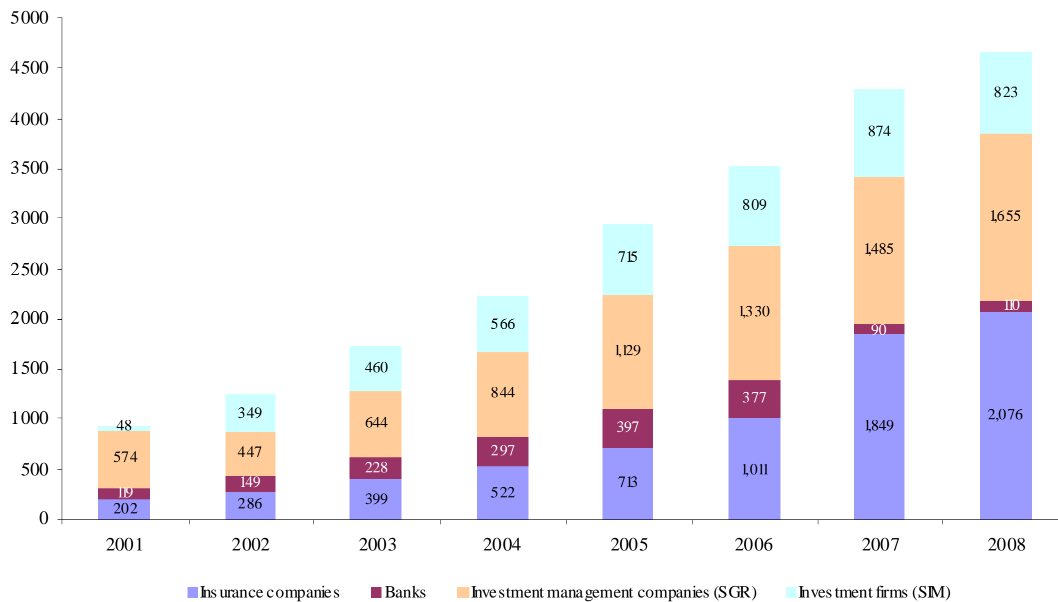
Open pension fund members: breakdown by promoting institutions (from 2001 to 2008)



Source: COVIP

Figure 3.2.c

Net asset value of open pension funds (millions of Euro): classification by promoting institutions (from 2001 to 2008)

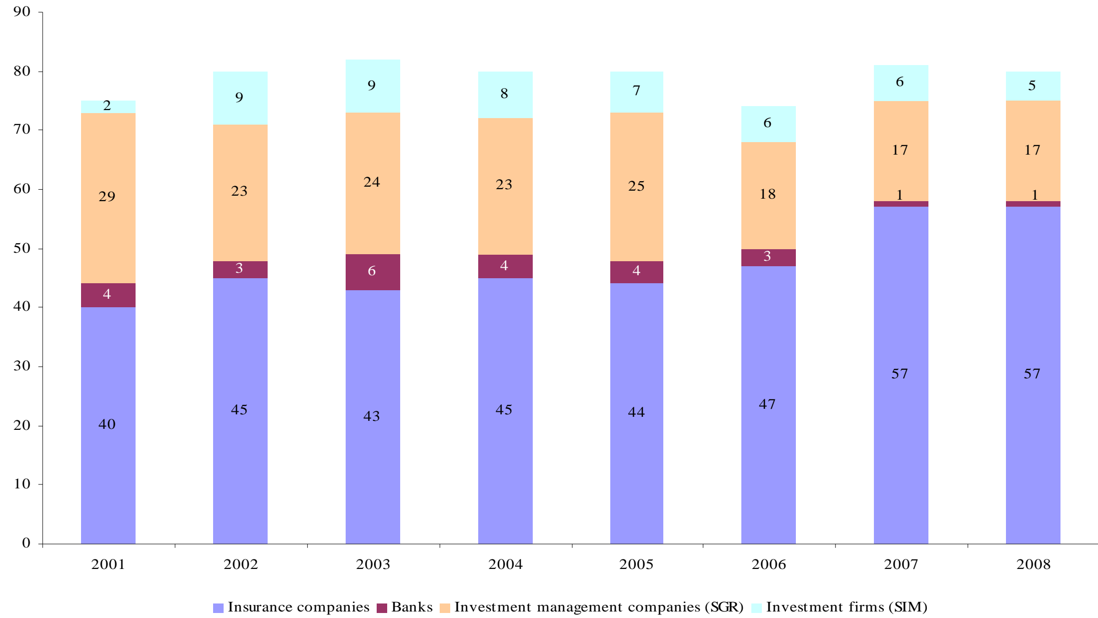


Source: COVIP

In fact, open funds promoted by insurance companies widely exceeded other funds: in 2008, 57 out of 80 funds were promoted by insurance firms (see Figure 3.2.d). This number increased significantly (by 10 units) from 2006 to 2007. Consequently, the recent increase in the number of members and size of assets under management of open funds promoted by insurance companies might be explained by both an increasing efficiency of the insurers' distributing channels and a second round of new entrants in this market segment.

Figure 3.2.d

Open pension funds: classification by promoting institutions (from 2001 to 2008)



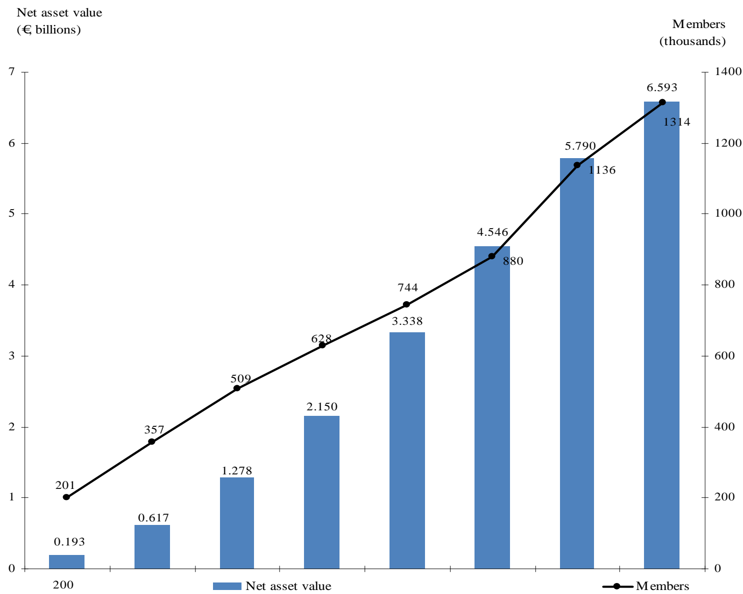
Source: COVIP

3.1.4
PIPs

The number of members enrolling in a PIP and the net asset value accumulated by insurance firms issuing these policies are rising at a high steady rate over time (Figure 3.3.a). Policyholders enrolling in policies compliant with Legislative Decree 252/2005 ("new" PIPs) are more numerous than those who enrolled in old policies, as virtually all policies issued after 2006 are already compliant. However, since a significant number of policyholders paid premiums for "old" policies for many years, 70% of insurance policies' mathematical provisions refer to old policies (Figure 3.3.b).

Figure 3.3.a

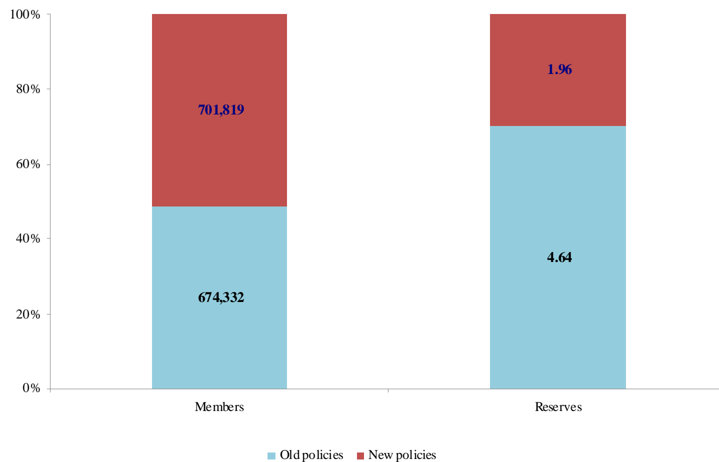
PIPs: members (thousands) and total net asset values (millions of Euro) from 2001 to 2008



Source: COVIP

Figure 3.3.b

Members (thousands) and mathematical reserves of new[(1)] and old[(2)] PIPs (2008 year-end)



(1) PIPs in compliance with Legislative Decree 252/2005.

(2) PIPs not in compliance with Legislative Decree 252/2005.

Source: COVIP

3.1.5
Recent developments

The most recent COVIP data as of the end of September 2009 show a slight overall increase in membership, mainly due to the enrolment capacity of PIPs (+17%).

This evolution can be explained considering the different impact of the financial and real crisis on various schemes and the strong commitment of the sales forces of insurance companies.

Table 3.7 shows the total amount of assets under management of different schemes. The value reflects the positive yield recorded from January to September 2009.

Table 3.7

Italian private pension schemes: members and net asset value (September 2009)

	members	net asset value [(1)]
contractual funds	2,045,238	17,79
open funds	810,864	5,823
PIPs (new)	818,498	3,16
PIPs (old)	674,000	4,600
Opre-existing funds	677,000	36,000
Total[*]	*4,997,539*	*67,397*

* double calculation of old and new PIPs is excluded

(1) millions of Euro

Source: COVIP

3.2
Financial management issues

3.2.1
Delegated investment management

According to Italian Law, contractual pension funds must delegate investment management activities to a financial manager, chosen by the fund according to certain rules. Therefore delegated investment management has proven to be the rule for contractual funds. Interestingly, in the ten-year experience of contractual funds, some delegated managers have in turn delegated asset management activities to other financial institutions. Therefore, as far as contractual funds are concerned, two types of delegated investment management relationships can be examined: "direct delegation" and "sub-delegation".

Conversely, financial resources of open pension funds and insurance policies can be directly managed by their promoting institutions. Nevertheless, examples of delegating investment management have been experimented so far also in the experience of sponsoring institutions of open funds and insurance policies. Hence, delegated investment management choices deserve some analysis.

3.2.1.1
Delegated investment management in contractual pension funds

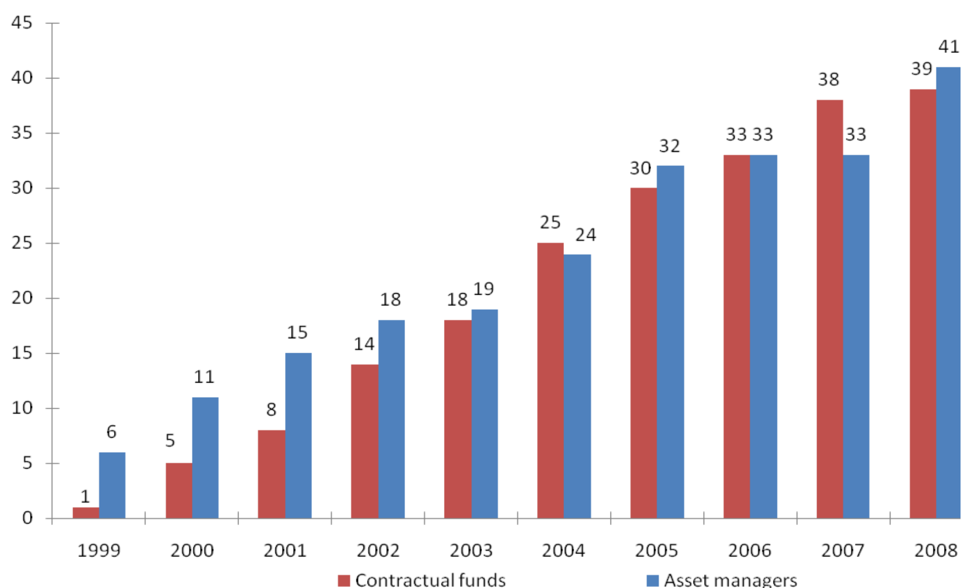
Direct delegation

Figure 3.4 reports the number of operating contractual pension schemes and financial institutions directly involved in the management of their assets. Both numbers have increased over time, demonstrating that as new contractual funds were established, new financial institutions entered the industry. The financial management activity and the relationship fund-manager is regulated by a mandate, an agreement that defines all the terms of the financial manager's assignment (e.g., the objective, the boundaries, the fees, etc.).

Typically a pension fund makes use of more than one financial manager in order to mitigate the risk of mismanagement, create competition among managers or allocate different asset classes to different specialized managers. Therefore, each fund signs several mandates with many asset managers. A manager may also sign more than one mandate with the same fund. This can be the case when the fund consists of numerous sub-funds and mandates a single financial institution to manage them (possibly under different terms).

Figure 3.4

Contractual pension funds: number of operating schemes and number of financial institutions managing contractual fund assets from 1999 to 2008



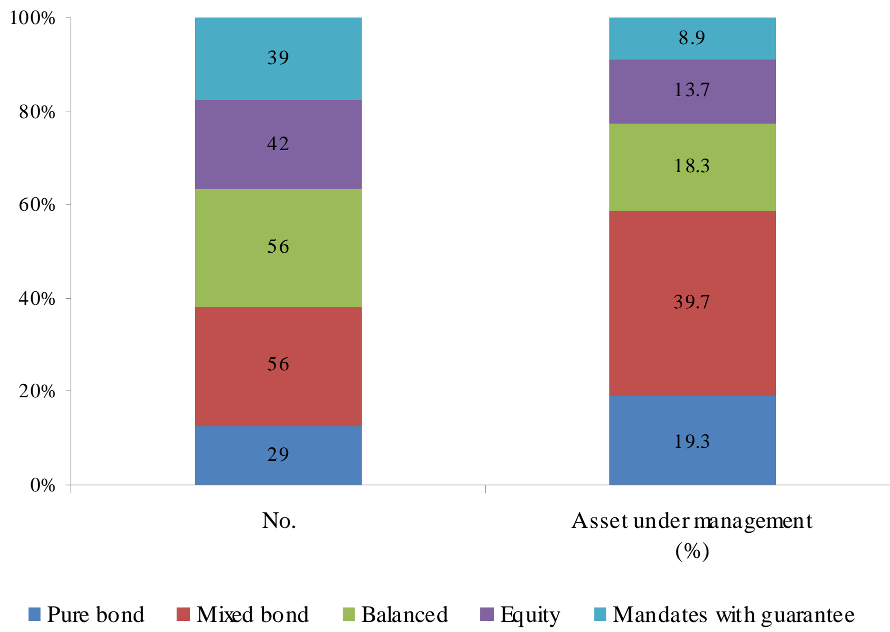
Sources: COVIP and fund prospectuses

Figure 3.5 shows the number of different financial mandates assigned by contractual pension funds. Albeit mixed bond and balanced mandates prevail, there are not large differences between the number of various mandates. However, most financial resources are predominantly managed through bond mandates, while pure equity and balanced mandates account for only 13.7% and18.3% respectively of the total net assets of contractual funds.

Table 3.8.a and 3.8.b list the financial institutions acting as asset managers for contractual pension funds from 1999 to 2008. For each manager, Table 3.8.a reports the number of funds served and Table 3.8.b the total number of mandates awarded. The number of mandates in Table 3.8.b exceeds the corresponding number of funds reported in Table 3.8.a if a manager gets more than one mandate from a single pension fund. Figures in these tables indicate that (1) the number of financial institutions involved in pension fund assets has increased; (2) after the first year of development, the Italian pension sector has attracted a number of international institutions; (3) some firms that first entered the industry have gradually consolidated their market share by increasing both the number of funds served and mandates awarded; (4) there are very few cases of financial managers exiting the industry.

Figure 3.5

Contractual pension fund mandates: types of mandates (number) and their assets under management (% over the total) at 2008 year-end



Source: COVIP

Table 3.8.a

Italian contractual pension schemes: number of funds served by each asset manager from 1999 to 2008 [(1)]

	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Pioneer Investment Management Sgr	1	3	3	3	5	9	13	15	20	23
Duemme State Street Sgr	1	2	3	4	3	3	4	5	8	7
Eurizon Capital Sgr	1	3	5	10	13	18	21	20	22	16
Generali Vita	1	2	2	3	3	2	3	3	7	2
UGF Assicurazioni	1	1	3	5	6	8	11	12	15	20
Allianz Ras	1	1	1	2	5	9	13	13	12	4
BNP Paribas		1	1	1	1	1	1	2	4	6
Invesco		2	2	2	2	2	1	1	1	0
Morgan Stanley		1	1	2	2	2	2	2	1	1
Romagest		1	1	1	0	0	0	0	0	0
Cisalpina Gestioni		2	2	2	0	0	0	0	0	0
Capitalia					3	3	2	3	1	0
ABN Amro A.M. Italy Sgr			1	1	1	2	1	1	1	3
Arca Sgr			1	2	2	2	2	2	2	2
Ing Investment Management Italia Sim			1	1	3	4	4	4	3	3
Lombard			1	1	1	1	1	1	1	0
Axa MPS Assicurazioni Vita Spa				2	2	2	3	3	4	1
Monte Paschi AM Sgr				1	2	2	3	5	7	9
Nextra				2	2	2	1	0	0	0
CDC IXIS					1	1	1	1	1	0
Dexia AM Belgium SA					1	2	2	2	5	5
Credit Agricole AM SA						2	2	2	1	2

Credit Suisse A.M.						2	2	2	7	3
Franklin Templeton						1	2	2	2	1
Rothschild						1	2	2	1	1
Société Générale						1	3	3	3	4
Azimut							1	2	1	1
Cattolica Assicurazioni							2	2	9	10
Dekabank Deutsche Girozentrale Francoforte							1	1	0	1
Deutsche Bank							3	3	2	0
Epsilon Sgr							1	1	2	1
Pictet & C.							1	1	0	0
Schroders Italy Sim Spa							1	1	2	3
Julius Baer								1	1	1
Groupama Sgr									1	4
RSF Investment Management									1	1
Ergo previdenza									1	1
Allianz Global Investors										3
Generali Asset Management SGR Spa										1
Axa Investment Managers - Paris										3
Natixis A.M. Italia										1
DWS Investment Italy SGR Spa										1
Eurizon Vita Spa										10
Groupama AM										2
Credit Suisse Italia Spa										5
Fortis Investments Belgium										1
Assicurazioni Generali										7
UGF Banca										1

Ina Assitalia										1
State Street Global Advisor										3
TOTAL	6	19	28	45	58	82	110	118	149	175

(1) 2008 figures reflect prospectus information available as of June 2009. Figures are based on prospectuses that might not be complete or updated. Asset managers' names are listed as reported in the prospectuses. Asset managers belonging to the same financial group are regarded as different entities.

Sources: Fund prospectuses

Table 3.8.b

Italian contractual pension schemes: number of mandates awarded to each asset manager from 1999 to 2008 (1)

	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Pioneer Investment Management Sgr	1	3	3	3	6	10	15	17	31	37
Duemme State Street Sgr	1	2	3	5	4	6	7	8	13	13
Eurizon Capital Sgr	1	3	5	11	14	21	24	24	30	22
Generali Vita	1	2	2	3	5	2	3	3	7	2
UGF Assicurazioni	1	1	3	5	6	8	11	12	18	23
Allianz Ras	1	1	1	2	5	20	24	39	22	4
BNP Paribas		1	1	1	1	1	1	2	4	6
Invesco		4	4	4	2	2	1	1	1	0
Morgan Stanley		2	2	3	3	3	3	3	1	1
Romagest		2	2	2						
Cisalpina Gestioni		4	4	4						
Capitalia					5	14	12	13	1	0
ABN Amro A.M. Italy Sgr			1	1	1	4	3	3	1	10
Arca Sgr			1	2	2	2	2	2	2	2
Ing Investment Management Italia Sim			1	1	3	7	7	7	3	3
Lombard			1	1	1	1	1	1	1	0
Axa MPS Assicurazioni Vita Spa				2	2	5	6	6	7	1
Monte Paschi AM Sgr				1	2	2	3	5	8	18
Nextra				2	3	2	1	0	0	0
CDC IXIS					1	1	1	1	1	0
Dexia AM Belgium SA					1	2	2	2	9	9
Credit Agricole AM SA						2	2	2	1	2

Credit Suisse A.M.						5	5	5	10	8
Franklin Templeton						1	2	2	3	2
Rothschild						1	2	2	1	1
Société Générale						1	3	3	4	5
Azimut							1	3	1	1
Cattolica Assicurazioni							2	2	9	10
Dekabank Deutsche Girozentrale Francoforte							1	1	0	1
Deutsche Bank							3	3	2	0
Epsilon Sgr							1	1	2	1
Pictet & C.							1	1	0	0
Schroders Italy Sim Spa							1	1	2	3
Julius Baer								1	1	1
Groupama Sgr									1	6
RSF Investment Management									1	1
Ergo previdenza									1	1
Allianz Global Investors										7
Generali Asset Management SGR Spa										1
Axa Investment Managers – Paris										6
Natixis A.M. Italia										1
DWS Investment Italy SGR Spa										1
Eurizon Vita Spa										10
Groupama AM										4
Credit Suisse Italia Spa										8
Fortis Investments Belgium										2
Assicurazioni Generali										8
UGF Banca										1

Ina Assitalia										1
State Street Global Advisor										3
TOTAL	6	25	34	53	67	123	151	176	199	247

(1) 2008 figures reflect prospectus information available as of June 2009. Figures are based on prospectuses that might not be complete or updated. Asset managers' names are listed as reported in the prospectuses. Asset managers belonging to the same financial group are regarded as different entities.

Sources: Fund prospectuses

As mentioned before, a financial manager who gets a mandate to manage a contractual pension fund's assets might, in turn, delegate this mandate to another asset manager, usually belonging to the same group. The fund must receive prior notification of such a sub-delegation and give its approval.

For each financial institution granted a direct asset management mandate by a contractual pension fund, Table 3.9 indicates the number of mandates sub-delegated to another firm. This information is further summarized by Table 3.10.a, which shows the number of mandates sub-delegated by each type of financial manager. This table also highlights the type of sub-delegated managers, distinguishing between those who belong to the same group and those who do not. The picture that emerges is interesting, since it demonstrates that sub-delegation is quite common, especially between firms belonging to the same group. The most frequent cases are insurance firms delegating asset management services to investment companies (SGRs) belonging to the same group. Table 3.10.b reports the same information when only guaranteed sub-fund mandates are considered. This further analysis is motivated by the fact that guaranteed sub-fund mandates might require more specific skills than other mandates, therefore most of the sub-delegated mandates are expected to be found here. All these mandates (26) refer to insurance companies that, in turn, delegate asset management services to investment companies (mostly SGRs) belonging to the same or a different group (18 and 8 cases respectively).

Table 3.9

Italian contractual pension schemes: mandates awarded and then delegated to another asset manager (June 2009)

	Funds served	Mandates granted	Mandates sub-delegated to a firm belonging to the same group	Mandates sub-delegated to a firm not belonging to the same group
Pioneer Investment Management Sgr	23	37	0	0
Duemme State Street Sgr	7	13	0	0
Eurizon Capital Sgr	16	22	0	0
Generali Vita	2	2	2	0
UGF Assicurazioni	20	23	1	15
Allianz Ras	4	4	4	0
BNP Paribas	6	6	4	1
Morgan Stanley	1	1	0	0
ABN Amro A.M. Italy Sgr	3	10	0	0
Arca Sgr	2	2	0	0
Ing Investment Management Italia Sim	3	3	0	0
Axa MPS Assicurazioni Vita Spa	1	1	1	0
Monte Paschi AM Sgr	9	18	0	0
Dexia AM Belgium SA	5	9	0	0
Credit Agricole AM SA	2	2	0	0
Credit Suisse A.M.	3	8	0	0
Franklin Templeton	1	2	0	0
Rothschild	1	1	0	0
Société Générale	4	5	0	0
Azimut	1	1	0	0
Cattolica Assicurazioni	10	10	6	3
Dekabank Deutsche Girozentrale Francoforte	1	1	1	0

Epsilon Sgr	1	1	0	0
Schroders Italy Sim Spa	3	3	1	0
Julius Baer	1	1	0	0
Groupama Sgr	4	6	5	0
RSF Investment Management	1	1	0	0
Ergo previdenza	1	1	0	1
Allianz Global Investors	3	7	0	0
Generali Asset Management SGR Spa	1	1	0	0
Axa Investment Managers - Paris	3	6	0	0
Natixis A.M. Italia	1	1	0	0
DWS Investment Italy SGR Spa	1	1	0	0
Eurizon Vita Spa	10	10	6	0
Groupama AM	2	4	0	0
Credit Suisse Italia Spa	5	8	0	0
Fortis Investments Belgium	1	2	0	0
Assicurazioni Generali	7	8	1	0
UGF Banca	1	1	0	0
Ina Assitalia	1	1	1	0
State Street Global Advisor	3	3	0	0
TOTAL	175	247	33	20

Sources: Fund prospectuses

Table 3.10.a

Financial managers delegating contractual pension fund asset management services to other financial managers (June 2009)

Financial manager	**Total**	Of which:		Of which	
		to firms belonging to the same group		to firms not belonging to the same group	
Insurance companies	**42**	**TO SGR**	**22**	**TO SGR**	**19**
				TO SIM	1
Banks	**1**	**TO SGR**	1		
SGR	**9**	**TO SGR**	**9**		
SIM	**1**	**TO SGR**	1		
Total general	**53**		**33**		**20**

Sources: Fund prospectuses

Table 3.10.b

Financial managers delegating contractual pension fund asset management services for guaranteed sub-funds to other financial managers (June 2009)

Financial manager	**Total**	Of which:		Of which	
		to firms belonging to the same group		to firms not belonging to the same group	
Inrurance companies	26	**TO SGR**	**18**	**TO SGR**	7
				TO SIM	1
Banks	**0**				
SGR	**0**				
SIM	**0**				
Total general	**26**		**18**		**8**

Sources: Fund prospectuses

3.2.1.2
Delegated investment management in open pension funds

Even though institutions promoting open pension funds are authorized to manage the assets of their funds directly, these organizations quite frequently delegate at least certain investment management activities to third institutions. As shown in Table 3.11.a, in 42 out of 79 open funds, the promoting institution grants a financial management mandate to another asset manager, half of the time belonging to a different financial group. This tendency is true in almost every case among the few banks and SIMs: 7 out of 8 pension funds promoted by a bank (2) and a SIM (5) have at least one delegation investment management agreement. Delegation can be motivated by the fund's aim to involve specialized asset managers, granting them the mandate to manage specific types of assets which they are experienced and familiar with. Alternatively, the fund's promoting institution, with a well-recognized brand and a strong distribution power, might find it useful to delegate management tasks if it lacks adequate portfolio management skills. Table 3.11.b documents that in 12 out of the 42 experiences, delegation shapes all sub-funds, meaning that this practice is well-established among funds. This may also (but not necessarily) be the case with financial institutions that delegate a various percentage of all sub-fund assets. It is worth

noting that most delegated managers are SGRs (see Table 3.11.c). Finally, Table 3.11.d focuses on delegated investment management agreements pertaining to guaranteed sub-funds. Since financial management of such sub-funds requires specific competencies and experience, one would expect that most of delegated mandates refer to these sub-funds. The number of guaranteed sub-funds handled by managers other than the fund's promoting institution is quite small. This practice is standard if the fund is promoted by a bank. (The two guaranteed sub-funds are managed by a third party.) It is also common in guaranteed sub-funds promoted by insurance companies. (34 out of 78 are managed by another institution, even if only 11 sub-funds are managed by a firm (always an SGR) that does not belong to the same financial group of the sponsoring insurance firm.)

3.2.1.3
Delegated investment management in PIPs

The practice of delegating investment management activity to another firm is common also in life insurance policy schemes. Table 3.12.a reveals that in 44 out of the 73 new PIPs, the insurance company granted at least one asset management mandate to another firm, although only 5 mandates were granted to a firm belonging to a different financial group. Table 3.12.c shows that most of the grantees are SGRs (31 out 44). Table 3.12.b documents that 37 out of the 44 cases of delegation involve all sub-funds, while in 5 cases delegation is limited only to certain sub-funds. Narrowing the analysis on guaranteed sub-funds, Table 3.12.d demonstrates that delegation of asset management activity is widespread also in guaranteed sub-funds. (31 out of 67 guaranteed sub-funds are managed by another institution, typically a SGR belonging to the same financial group of the sponsoring insurance firm.)

Table 3.11.a

Open pension funds and delegated asset management agreements (June 2009)

Promoting institutions	Open funds	Open funds with delegated asset management agreements		
		Total	*To firms belonging to the same financial group*	*To firms not belonging to the same financial group*
Insurance companies	55	33	*16*	*17*
Banks	2	2	*0*	*2*
SGRs	16	2	*0*	*2*
SIMs	6	5	*5*	*0*
Total	**79**	**42**	***21***	***21***

Sources: Fund prospectuses

Table 3.11.b

Open pension funds with delegated asset management agreements: further breakdowns (June 2009)

Promoting institutions	Open funds with delegated asset management agreements	Funds with delegated asset management agreements for all sub-funds			Funds with delegated asset management agreements for certain sub-funds		
		Total	*To firms belonging to the same financial group*	*To firms not belonging to the same financial group*	Total	*To firms belonging to the same financial group*	*To firms not belonging to the same financial group*
Insurance companies	33	27	*13*	*14*	6	*2*	*4*
Banks	2	0	*0*	*0*	2	*0*	*2*
SGRs	2	1	*0*	*1*	1	*0*	*1*
SIMs	5	2	*2*	*0*	3	*3*	*0*
Total	**42**	**30**	***15***	***15***	**12**	***5***	***7***

Sources: Fund prospectuses

Table 3.11.c

Categories of delegated financial managers in the open fund industry (June 2009)

Insurance companies	5
Banks	1
SGRs	36
SIMs	0
Total	**42**

Sources: Fund prospectuses

Table 3.11.d

Open pension funds with delegated asset management agreements for guaranteed sub-funds (June 2009)

Promoting institutions	Guaranteed sub-funds	*Agreements with firms belonging to the same financial group*				*Agreements with firms not belonging to the same financial group*			
		Insurance companies	*Banks*	*SGRs*	*SIMs*	*Insurance companies*	*Banks*	*SGRs*	*SIMs*
Insurance companies	*78*	4	1	18	0	0	0	11	0
Banks	*2*	1	0	0	0	1	0	0	0
SGRs	*16*	0	0	0	0	1	0	0	0
SIMs	*5*	0	0	0	0	0	0	4	0
Total	*101*	5	1	18	0	2	0	15	0

Sources: Fund prospectuses

Table 3.12.a

PIPs and delegated asset management agreements (June 2009)

PIPs	PIPs with delegated asset management agreements		
	Total	*To firms belonging to the same financial group*	*To firms not belonging to the same financial group*
73 [1]	44	*39*	*5*

[1] two policies have closed contributions to new members

Sources: Fund prospectuses

Table 3.12.b

PIPs with delegated asset management agreements: further breakdowns (June 2009)

PIPs with delegated asset management agreements	PIPs with delegated asset management agreements for all sub-funds		PIPs with delegated asset management agreements for certain sub-funds	
	To firms belonging to the same financial group	*To firms not belonging to the same financial group*	*To firms belonging to the same financial group*	*To firms not belonging to the same financial group*
44	35	*2*	*4*	*1*

Sources: Fund prospectuses

Table 3.12.c

PIPs: categories of delegated financial managers (June 2009)

Insurance companies	2
Banks	8
SGRs	31
SIMs	2
SIMs and SGRs (a different sub-fund each)	1
Total	**44**

Sources: Fund prospectuses

Table 3.12.d

PIPs with delegated asset management agreements for guaranteed sub-funds (June 2009)

Guaranteed sub-funds	*Guaranteed sub-funds managed internally*	*Agreements with firms belonging to the same financial group*				*Agreements with firms not belonging to the same financial group*			
		Insurance companies	*Banks*	*SGRs*	*SIMs*	*Insurance companies*	*Banks*	*SGRs*	*SIMs*
67	31	2	5	25	1	0	0	2	1

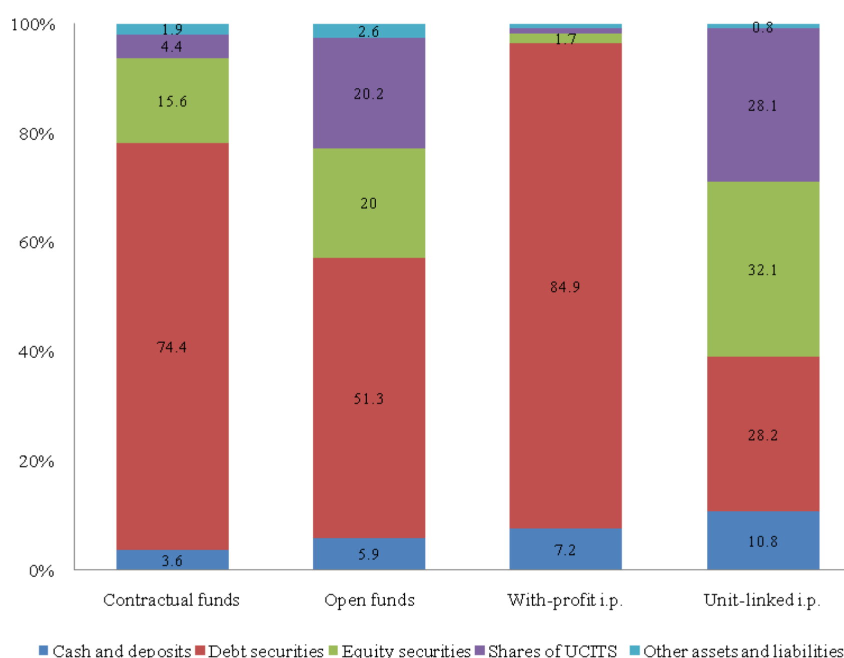
Sources: Fund prospectuses

3.2.2
Asset allocation, sub-funds' selection and financial returns

The various pension schemes also seem to differ in terms of their asset allocation policies. Figure 3.6 shows the portfolio allocations of contractual funds, open funds and PIPs at 2008 year-end. Despite the fact that these data refer to all sub-funds and therefore do not reveal all the differences in any pension scheme category, they clearly show that contractual funds invest a larger portion of their assets in the bond market (around 75%) as compared to open funds (about 50%) or unit-linked insurance policies (less than 30%). Even if all the UCITS shares of closed funds and insurance policies (which account for 20% and 28% respectively) were all invested in the bond market, contractual funds would have the larger bond asset class. However, Figure 3.7 shows that this not the case: looking closely at the basic components of pension scheme portfolios, the debt component (in red) accounts for 80% in contractual funds, about 40% in open funds and less than 45% in unit-linked insurance policies.

Figure 3.6

Private pension schemes: portfolio allocations (%) at 2008 year-end (all sub-funds)



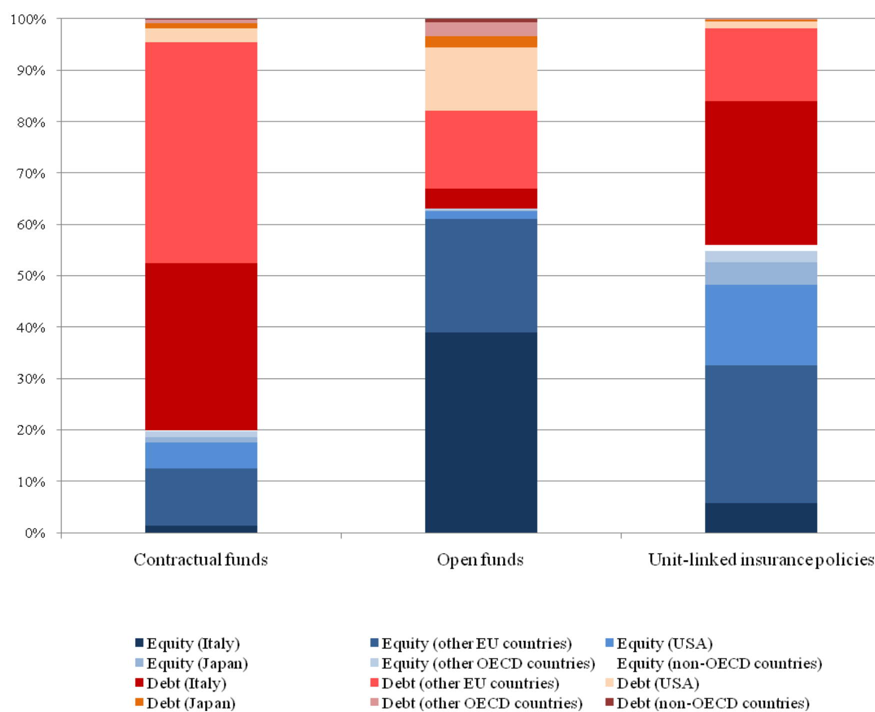
Source: COVIP

In fact, the percentage is even larger in with-profits insurance policies. However, this is not surprising for financial instruments that provide cliquet-style interest rate guarantees.

Figures 3.8.a and 3.8.b illustrate the dynamics of portfolio allocations over the 2001-2008 period for contractual funds (Figure 3.8.a) and open funds (Figure 3.8.b).[1] It is interesting to note that the asset allocation of contractual funds has been quite sticky over time (with a slight continuous increase of equities and a consequent decline of bonds from the beginning to 2006, and a subsequent reversal of this trend from 2006 onwards). At the same time, the proportion of bonds for open funds has continuously increased over the last five years with a decrease in both equities and shares of UCITS.

Figure3.7

Private pension schemes: geographic allocation (%) of equity and debt securities at 2008 year-end (all sub-funds of contractual, open and unit-linked insurance policies)

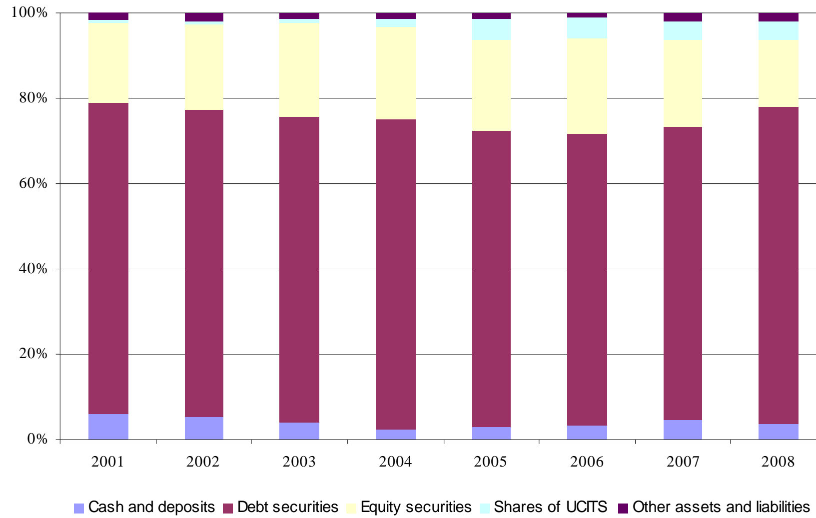


Source: COVIP

[1] *A similar time series is not available for PIPs.*

Figure 3.8.a

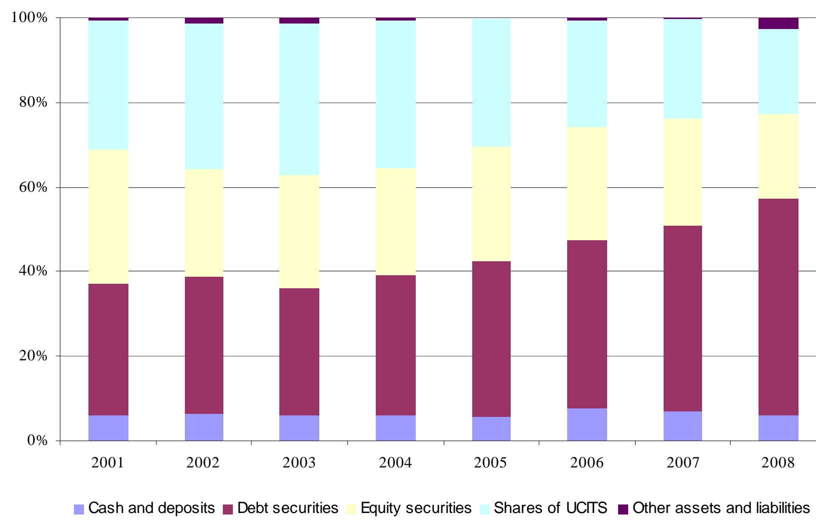
Contractual pension funds: portfolio allocations (%) from 2001 to 2008 (all sub-funds)



Source: COVIP

Figure 3.8.b

Open pension funds: portfolio allocations (%) from 2001 to 2008 (all sub-funds)

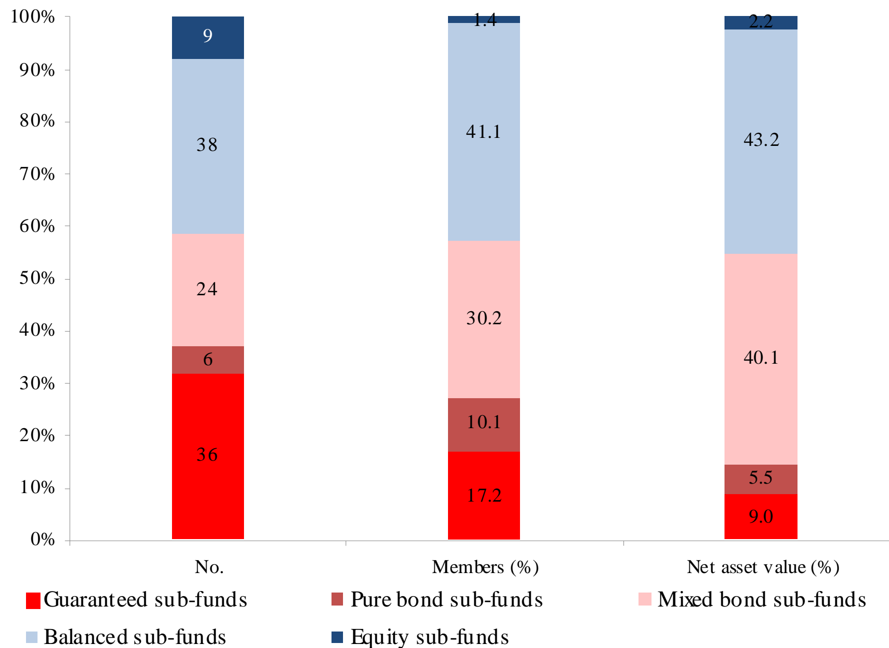


Source: COVIP

Certainly, differences in asset allocation among various pension scheme categories are mainly explained by the choices of sub-funds by their members. Figures 3.9.a, 3.9.b and 3.9.c attempt to account for these differences by displaying, for every sub-fund category, the number of existing sub-funds,[2] the percentage of members and the percentage of assets under management in the case of contractual funds (Figures 3.9.a), open funds (Figures 3.9.b) and PIPs (Figures 3.9.c). Focusing on the percentage of members and of assets under management of equity sub-funds, the difference between contractual funds and the other two schemes is clear: only 1.4% of contractual fund members chose an equity sub-fund, versus 29.2% and 23.2% for open funds and PIPs. Figures referring to assets under management do not differ appreciably: 2.2% of contractual fund NAV pertains to equity sub-funds, whereas this percentage reaches 29% and 17.4% in open funds and insurance policies, respectively.

Figure 3.9.a

Sub-funds of contractual pension funds: number, members (% over the total) and assets under management (% over the total) at 2008 year-end

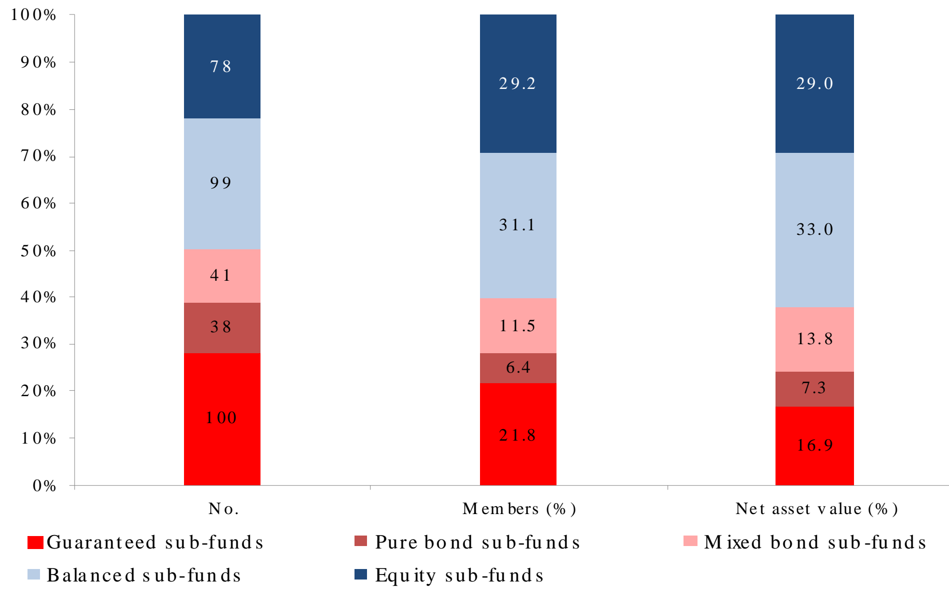


Source: COVIP

[2] *This figure is not available for insurance policies.*

Figure 3.9.b

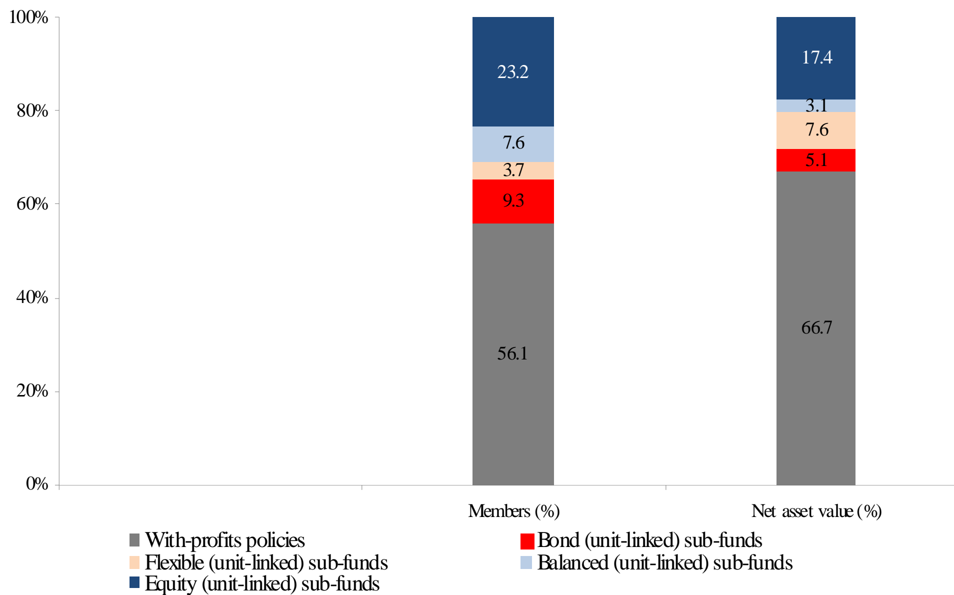
Sub-funds of open pension funds: number, members (% over the total) and assets under management (% over the total) at 2008 year-end



Source: COVIP

Figure 3.9.c

Sub-funds of PIPs: members (% over the total) and assets under management (% over the total) at 2008 year-end



Source: COVIP

Finally, Table 3.13 reports average financial returns on pension schemes. Following COVIP's annual reports, returns are compared to the TFR revaluation rate. This rate represents a sort of yardstick for pension funds, because it is the guaranteed return given up by those workers who decide to keep their accruing TFR in the employer's firm. By diverting the TFR to pension funds, workers might obtain a higher reward than the TFR return as a result of investments in capital markets.

Table 3.13

Italian private pension schemes: financial returns (2003 - Sept 2009)

	2003	2004	2005	2006	2007	2008	31Dec 2008 30Sept2009
Contractual funds	**5.0**	**4.6**	**7.5**	**3.8**	**2.1**	**-6.3**	**7,2**
"Monocomparto" funds [1]	4.2	4.4	8.3	3.7	1.4	n.a.	n.a.
"Multicomparto" funds [2]	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Guaranteed funds	n.a.	n.a.	n.a.	n.a.	n.a.	*3.1*	*4.2*
Pure bond funds	*3.0*	*2.2*	*2.1*	*2.6*	*2.2*	*1.6*	*2.7*
Mixed bond funds	*4.3*	*3.9*	*6.9*	*2.7*	*2.1*	*-3.9*	*6.9*
Balanced funds	*7.0*	*4.9*	*7.9*	*5.6*	*2.4*	*-9.4*	*8.7*
Equity funds	*8.3*	*5.9*	*14.9*	*8,2*	*1.3*	*-24.5*	*12.9*
Open funds	**5.7**	**4.3**	**11.5**	**2,4**	**-0.4**	**-14.0**	**9.3**
Guaranteed funds	*2.6*	*3.1*	*2.9*	*1.0*	*1.9*	*1.9*	*4.4*
Pure bond funds	*1.6*	*3.3*	*3.3*	*-0.2*	*1.6*	*4.9*	*3.8*
Mixed bond funds	*3.1*	*4.2*	*6.4*	*1.0*	*0.3*	*-2.2*	*5.9*
Balanced funds	*4.9*	*4.2*	*11.4*	*2.4*	*-0.3*	*-14.1*	*10.3*
Equity funds	*8.4*	*4.7*	*16.2*	*3.7*	*-1.6*	*-27.6*	*14.1*
PIPs [3]	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
With-profits policies	n.a.	n.a.	n.a.	n.a.	n.a.	3.5	n.a.
Unit-linked policies	n.a.	n.a.	n.a.	n.a.	n.a.	-24.9	12.5
Bond	n.a.	n.a.	n.a.	n.a.	n.a.	*2.7*	*3.8*
Flexible	n.a.	n.a.	n.a.	n.a.	n.a.	*-6.2*	*5.0*
Balanced	n.a.	n.a.	n.a.	n.a.	n.a.	*-16.2*	*10.7*
Equity	n.a.	n.a.	n.a.	n.a.	n.a.	*-36.5*	*17.6*
TFR revaluation rate	***2.8***	***2.5***	***2.6***	***2.4***	***3.1***	***2.7***	***1.4***

(1) Funds offering a single investment profile to their members.

(2) Funds offering several investment options to their members.

(3) PIPs in compliance with Legislative Decree 252/2005.

Source: COVIP

Obviously, the financial returns on pension schemes reflect the dynamics of capital markets, the funds' strategic asset allocation policies and members' sub-fund choices. Therefore, the differences among the average rates of return of the three categories are not surprising:

contractual fund performances look more stable than those of open funds because of the larger stake of bonds held. A more meaningful comparison calls for limiting the analysis on the performances of similar sub-funds. In such a case, differences among pension scheme categories are less univocal.

3.2.3
Guaranteed sub-funds

As a consequence of the tacit consent principle for the devolution of TFR, most pension schemes seek both to provide employees with a sub-fund satisfying those requirements and to broaden the mix of investment solutions. To do so most schemes have started providing at least one guaranteed interest rate investment solution in addition to other (usually already existing) sub-funds. Although all guaranteed sub-funds are supposed to provide a rate of return similar to the TFR revaluation rate, they may differ in terms of the minimum interest rate guaranteed and the time when the minimum guaranteed rate is due. In most cases, the scheme specifies the event rather than a fixed date that can trigger the guaranteed rate clause. The following section provides a description of all the different solutions chosen by the various pension scheme categories in terms of number and type of events triggering the interest rate guarantee. Note that a guaranteed sub-fund can be proposed not only for TFR compliance, but also for the opportunity to offer this risk profile to potential members.

3.2.3.1
Guaranteed sub-funds of contractual pension funds

All contractual pension funds but one have a guaranteed sub-fund (namely, Fondosanità, which is a closed pension fund for doctors, dentists and other professionals operating in the health care sector, for whom automatic TFR enrolment rule does not apply). However, while only one fund guarantees a return similar to the TFR revaluation rate at any time, all others specify events (typically more than one) which trigger the guaranteed return. Table 3.14.a shows the different solutions adopted by contractual funds; most provide guaranteed performance when four (14 funds) or five (17 funds) different events occur.

These events are detailed in Table 3.14.b. All funds with a guaranteed sub-fund provide a financial performance guarantee in case of a member’s retirement, death or permanent disability and all but one in case of unemployment. Other frequent events include withdraws frot the retirement account (22 funds) and the member’s surrender (6 funds).

Table 3.14.a

Number of events triggering the interest rate guarantee in the guaranteed sub-funds of contractual pension funds

No. of events	1	2	3	4	5	6	7	Guarantee provided at any time	Total
No. of funds	0	0	0	14	17	3	3	1	38

Sources: Fund prospectuses

Table 3.14.b

Events triggering the interest rate guarantee in the guaranteed sub-funds of contractual pension funds

Events	No. of funds triggering guarantee when the event in question occurs
Retirement	*38*
Death	*38*
Permanent disability	*38*
Unemployment (48 months)	*37*
Loan on the retirement account	*22*
Surrender	*6*
Switch to another sub-fund	*5*
Loss of prerequisites for participating in the pension scheme	*2*
Termination of employment	*2*
Termination of the investment management agreement	*2*
Guarantee provided at any time	*1*

Sources: Fund prospectuses

3.2.3.2 Guaranteed sub-funds of open pension funds

As indicated in Table 3.15.a, more than half of the guaranteed sub-funds of this category provide a guaranteed performance when four specific events occur (58 out of 101 funds). Two funds take into account only one event and twelve funds consider three events. As with the experience of contractual funds, the events most commonly addressed are retirement, death and permanent disability (98 funds) and unemployment (83 funds). Interestingly, three funds specify a pre-established future date, at which time the fund will provide the guarantee.

Table 3.15.a

Number of events triggering the interest rate guarantee in guaranteed sub-funds of open pension funds

No. of events	No. of sub-funds
1	2
3	12
4	58
5	17
6	6
7	4
8	2
Total	101

Sources: Fund prospectuses

Table 3.15.b

Events triggering the interest rate guarantee in guaranteed sub-funds of open pension funds

Events	No. of funds triggering guarantee when the event in question occurs
Retirement	*98*
Death	*98*
Permanent disability	*98*
Unemployment (48 months)	*83*
Switch to another pension scheme as a consequence of an unfavourable change of any contractual provision (1)	*16*
Loan on the retirement account	*15*
Switch to another sub-fund	*7*
Surrender	*6*
Unemployment (between 12 to 48 months)	*3*
Entering either the wage supplementation fund or the mobility list	*3*
Predetermined future date	*3*
Switch to another pension scheme	*2*

(1) Such as unfavourable changes of annuitization terms, increase of costs borne by the member, etc.

Sources: Fund prospectuses

3.2.3.3
PIPs with guaranteed interest rates

All PIPs that offer a guaranteed financial performance are with-profit policies. These policies grant the policyholders a given percentage of the rate of return of a special portfolio of investments,[3] covering at least the mathematical reserves of all the with-profit policies issued by the same insurance company. Should the granted rate of return exceed the technical interest rate already included in the premium calculation, a bonus computed at the excess rate is credited to the mathematical reserves of all the participating policies when they reach their "anniversary" (*i.e*., at the end of the policy year). In this way, the technical rate becomes a minimum guaranteed interest rate. The insured capital, resulting from the application of this rule, can be paid/converted into annuities as soon as the policyholder fulfils the public seniority pension requirements in terms of both minimum age and tenure, provided that his or her participation in the scheme lasted at least five years. Insurance policies usually permit policyholders to receive benefits before the maturity[4] in case of unemployment (for more than 48 months) or permanent disability.

Table 3.16.a classifies PIPs according to their life insurance business. It is worth mentioning that various investment lines might be offered through the same PIP. Additionally, these lines offered by a single PIP could be designed as either a with-profit policy (i.e. life insurance business I) or a unit-linked (i.e. life insurance business III). In fact, 37 out of 73 PIPs have both a with-profit investment line and (at least) one unit-linked investment line. Interestingly, there are only 7 PIPs whose investment lines are only of the unit-linked type. Table 3.16.b reports the technical interest rates of the 66 with-profit PIPs.

Table 3.16.a

PIPs: number of PIPs by life insurance businesses (June 2009)

PIPs	Life insurance business[(1)]		
	I	*III*	*I and III*
73	29	7	*37*

[(1)] Life insurance business I and life insurance business III denote with-profit and unit-linked policies, respectively

Sources: Fund prospectuses

[3] *Constituted and kept apart from the other assets of the insurance company.*
[4] *But not more than five years before.*

Table 3.16.b

With-profit PIPs: technical interest rates (June 2009)

PIPs	Technical interest rate				
	0.0%	*1.0%*	*1.5%*	*2.0%*	*Other rates*
66	*9*	*2*	*7*	*39*	*9*

Sources: Fund prospectuses

3.2.4.
Annuitisation agreements

Contractual funds

Initially, the primary focus of contractual funds was the investment process. Only recently the annuitisation profile has become relevant, since an increasing number of members are becoming eligible for retirement.

At the beginning of 2008, only a small number of contractual funds selected insurance companies for the provision of annuities. By mid-2008 an important innovation was introduced when Assofondipensione, the association of contractual pension funds, promoted a tender for the selection of an annuity provider on behalf of twenty of its member funds. Note that the call for tender was judged compliant with the Italian Antitrust Authority's competition regulations.

The tender requested five types of provisions:

1. with-profit single immediate life annuity;
2. with–profit single premium joint life and survivor annuity;
3. with-profit immediate life annuity with 5 or 10 years guaranteed period and single premium life annuity thereafter;
4. with–profit single premium immediate life annuity with death benefits, with repayment of the residual value to the beneficiary or the option to constitute a new single immediate premium for the beneficiary with the residual value;
5. with–profit immediate single premium annuity with long-term care insurance options.

Companies could present offers for all five types of annuities, for the first four or only for the long-term option.

Other important terms and conditions requested were the following:

- duration of ten years;
- no right to withdraw before the end of contract;

- no modification of conditions for the whole duration of the contract, except in case of a reduction in the maximum guaranteed rate of interest determined by the Italian Insurance Authority by 0.50 or more;
- conversion rates not less than those reported in the tender.

Unipol Gruppo Finanziario (UGF) was awarded the tender for the first four annuity types; the fifth went to Assicurazioni Generali and Ina Assitalia (which belong to the same insurance group). During 2009 an increasing number of funds calling for tenders through their associations signed contracts with the same conditions.

Relevant conditions can be downloaded from the websites of the insurance companies in question. These terms are of great interest for the qualified development of the complementary pension system, because they increase the number of alternatives available to members of pension funds and disclose how relevant prices are defined. Table 3.17.a reports the coefficients provided by UGF for funds calling for tenders and Table 3.17.b indicates the coefficients offered by Assicurazioni Generali for the same group .

Table 3.17.a

Coefficients provided by UGF for funds calling for Assofondipensioni tender

	RS (1)	RC5 (2)	RC10(3)	RCA (4)
Male -60	0.056544	0.056346	0.055751	0.052778
Male -65	0.065930	0.065479	0.064097	0.059553

(1) with profit single immediate life annuity

(2) with profit single immediate with 5 years guarantee

(3) with profits single immediate with 10 years

(4) with profit single immediate with death benefits

Table 3.17.b

Coefficients provided by Generali Group for funds calling for Assofondipensioni tender [(1)]

	Rate 2.50%, annual frequency		
	RS	RC5	RC10
Male-60	0.052620	0.052450	0.051910
Male-65	0.060286	0.059876	0.058635

(1) The annuity doubles in case of LTC

Note the slight differences in the amounts of various alternatives, in particular the interesting position of those with death benefits and LTC options. If this information were disclosed and properly communicated, and adequate financial education provided, the natural propensity for lump-sum payment at retirement could be reduced in favour of the annuity option.

Tables 3.18.a and 3.18.b report the types and the number of annuities proposed by contractual funds since mid-2009. Table 3.18.c lists insurance companies involved. Apart from the conditions stated in the aforementioned calls for tenders, others may change in terms of the maximum interest rate that can be guaranteed in PIPs; additional modifications may result from updated demographic tables being adopted to consider new longevity trends. However, coefficients can not be changed once the annuity starts or during a period of three years before retirement.

Open funds

All open funds offer some type of annuity option, as shown in Table 3.19. Only a few funds give the opportunity for LTC or death benefits. At present, due to the low demand of annuitants, the offering of annuities is only hypothetical and will be probably influenced by types and conditions offered by contractual funds. Coefficients used for the calculation of annuities can be changed in case of new limits on the maximum guaranteed interest rate or new trends in longevity. However, coefficients can not be modified once the annuity starts or three years before retirement.

PIPs

As mentioned, PIPs are established exclusively by insurance companies and regulations allow them to diversify their offering with reference to annuities. In fact, rules set down by COVIP allow PIPs to take some risk in fixing demographic parameters of the conversion coefficient for the calculation of the annuity. All PIPs offer some type of annuity option, as shown in Table 3.20.a. Table 3.20.b shows that some insurance companies assume this risk until a certain future date. In many cases companies can change coefficients, but only for future premiums. In other words, coefficients remain in force for each contribution period. This guarantee in terms of

coefficients is very important for the pension member considering the scenario of possible future changes in life expectancies. Consider that offering of these options is until now only hypothetical due to the negligible demand of annuities. Note that pricing of this guarantee can be highlighted in calculating the ISC, but in many cases this component is not split, reducing the signalling capacity of this indicator.

Table 3.18.a

Types of life annuity options offered by contractual pension funds

	With-profit Immediate	With-profit Immediate reversionary	With-profit Immediate with death benefits	With-profit Immediate increased with LTC coverage	5-year certain and thenceforth with-profit	10-year certain and thenceforth with-profit	Other types
No. of funds	17	17 (1)	12	11	13	13 (2)	2

(1) This option is offered by the same funds that offer the immediate with-profits life annuity option.

(2) This option is offered by the same funds that offer the 5-year certain annuity and thenceforth with-profits life annuity option.

Sources: Prospectuses and web sites of funds-June 2009

Table 3.18.b

Number of life annuity options offered by contractual pension funds

No. of life annuity options offered	No. of funds
2	2
3	2
4	1
5	3
6	8
7	1
Total	17

Sources: Prospectuses and web sites of the funds

Table 3.18.c

Number of annuitisation agreements signed by insurance companies with contractual pension funds [1]

Insurance companies	No. of annuitisation agreements
Assicurazioni Generali	*9*
Ina Assitalia Assicurazioni [2]	*3*
UGF Assicurazioni	*7*
Cattolica Assicurazioni	*2*
Fondiaria-Sai	*1*
Total	**22**

(1) Some funds have signed annuitisation agreements with more than one insurance company; therefore the total number of agreements exceeds the number of funds with annuitisation agreements.

(2) Ina Assitalia belongs to Generali group.

Sources: Prospectuses and web sites of the funds

Table 3.19

Types of life annuity options offered by open pension funds

	With–profits Immediate	Deferred	With-profit Immediate reversionary	With-profit Immediate with death benefits	5-year certain, thenceforth with-profit	10-year certain, thenceforth with-profit	15-year certain, thenceforth with-profit	with-profit immediate increased with LTC coverage
No. of funds	76	2	77 [1]	4	72	66	1	6

(1) In two funds the reversionary option might be entire or partial (50% or 75%).

Sources: Fund prospectuses

Table 3.20.a

Types of life annuity options offered by PIPS

	With –profit immediate	With –profit Immediate reversionary	With-profit immediate with death benefits	5-year certain, thenceforth with-profit	10-year certain, thenceforth with-profit	15-year certain, thenceforth with-profit	20-year certain, thenceforth with-profit	Other types
No. of funds	73	73	5	48	58	7	1	2

Sources: Insurance policy prospectuses

Table 3.20.b

PIPs: Changes of coefficients for new longevity table

Type of change	Number
Changes are not possible before 31 December 2011	1
Changes are not possible before 31 December 2017	2
Changes affect only future payments by the member	35
Changes are possible	35

Sources: Insurance policy prospectuses

3.2.5. Cost issues

The ISC index is only a rough measure of the cost assessment of the participation in a private pension scheme (see Appendix). Moreover, it would be absolutely misleading for a pension scheme member to look only at this indicator. In actual fact, any additional guarantee provided by the scheme contributes to increasing the ISC figures (e.g. death benefits, guaranteed minimum returns, cliquet-style interest rate guarantees, guaranteed mortality tables in the annuity provision, etc.). Therefore any comparison between the ISCs of different pension schemes should also take into account these guarantees. Additionally, since investments in stocks are typically more expensive than managing a portfolio of bonds, all other things being equal, the ISC index on equity sub-funds is expected to be higher than that of bond or balanced sub-funds.

The Supervisory Authority requires pension schemes to publish four different ISC figures in the scheme prospectus, with cost projections over 2, 5, 10 and 35 years, respectively. Obviously, given the long duration of a typical pension investment, the 2-year ISC is not very significant. On the other hand, the 35-year ISC might be misleading as well, because of the excessive length of the projection of costs and returns underlying the figure.

Any reasonable use of ISC as decision parameter should therefore consider a 5- or 10-year figure. Moreover, an evaluation should be restricted to very homogenous schemes, *i.e.* schemes that are similar in terms of financial management style (portfolios with a similar risk-return profile), and supplementary guarantees and additional services. (One scheme might be more expensive than another because of the consulting service provided to members by its distributors channels.)

Granted that a valuation of different pension scheme ISCs should be made among as homogenous schemes as possible, Table 3.21 shows some descriptive statistics of ISC indicators computed on four different sets: the universe of pension schemes and the subset of the contractual funds, the subset of the open funds and the subset of insurance policies. The cheapest schemes are the contractual funds, while PIPs appear to be the most expensive. This difference might be explained by the different risk-return profiles of the underlying investment portfolios.

In order to control for such a difference, the same descriptive statistics are computed, in Table 3.22, on the subset of sub-funds. The reasonable assumption is that the financial investments underlying these schemes should be more similar, namely, more bond-oriented. Again, the ISC indicators are computed on the four different sets and the previous ranking does not change.

In this case as well, the interpretation of these values is not univocal. For instance, many PIPs (34 out of 75) provide additional (embedded and not optional) death insurance coverage; furthermore, all the PIPs with a guaranteed minimum return are with-profit policies that typically provide a cliquet-style interest rate guarantee.

Table 3.21

The ISC index: comparison among different pension schemes (all sub-funds)

Pension scheme	ISC type	Mean	Std. Deviation	Min	Max
All pension schemes	2-year	2.20	1.18	0.40	5.99
	5-year	1.47	0.80	0.26	4.33
	10-year	1.22	0.67	0.18	3.57
	35-year	1.05	0.60	0.09	3.25
Contractual funds	2-year	1.02	0.61	0.40	3.32
	5-year	0.57	0.30	0.26	1.74
	10-year	0.39	0.17	0.18	1.03
	35-year	0.25	0.94	0.09	0.52
Open funds	2-year	1.97	0.75	0.54	4.87
	5-year	1.32	0.44	0.27	3.14
	10-year	1.16	0.38	0.18	2.54
	35-year	1.05	0.35	0.15	2.27
PIPs [(1)]	2-year	3.54	0.98	0.89	5.99
	5-year	2.41	0.66	0.82	4.33
	10-year	1.98	0.57	0.57	3.57
	35-year	1.61	0.54	0.38	3.23

[(1)] PIPs in compliance with Legislative Decree 252/2005.

Source: COVIP

Table 3.22

The ISC index: comparison among different pension schemes (guaranteed sub-funds)

Pension scheme	ISC type	Mean	Std. Deviation	Min	Max
All pension schemes	2-year	2.21	1.14	0.44	4.49
	5-year	1.42	0.70	0.27	2.88
	10-year	1.14	0.52	0.18	2.37
	35-year	0.93	0.41	0.11	2.01
Contractual funds	2-year	0.97	0.50	0.44	3.32
	5-year	0.59	0.25	0.33	1.74
	10-year	0.43	0.15	0.24	1.03
	35-year	0.30	0.10	0.11	0.52
Open funds	2-year	1.87	0.65	0.54	3.93
	5-year	1.23	0.38	0.27	2.53
	10-year	1.06	0.32	0.18	2.14
	35-year	0.96	0.29	0.15	2.01
PIPS (1)	2-year	3.41	0.81	0.89	4.49
	5-year	2.17	0.44	0.89	2.88
	10-year	1.66	0.29	0.89	2.37
	35-year	1.26	0.24	0.67	1.99

(1) PIPs in compliance with Legislative Decree 252/2005.

Source: COVIP

3.2.6
Depository Banks

Italian law (Decree 703/1996 of the Minister of the Economy) considers a circumstance relevant to determining conflict of interest if the fund's depository bank and financial manager belong to the same financial group. Given the increasing concentration of the banking and financial industries, such a conflict of interest has become much more likely. According to the law, the depository bank and the financial manager belonging to the same financial group is not necessarily an incompatible situation *per se;* in fact, the pension fund need only highlight the occurrence of this circumstance. However it is interesting to point out that the status of some funds has given rise to incompatibility, with depository bank and financial manager belonging to the same group. Therefore some depository banks had to be replaced. Table 3.23 reports the depository banks operating in the contractual fund industry between 2007 and 2009, indicating the number of funds served. Two institutions served more than 75% of the funds in 2009 and, even though the market experienced a similar high concentration in the previous years, one of the main players in 2007-2008 exited the market in 2009.

Finally, as far as the supervision activity of depository bank is concerned, Italian law seems to provide *ex ante* supervision. However, since the settlement rules in most financial markets require the irrevocability of orders, the depository bank's supervision activity is actually an *ex post* one.

Table 3.23

Depository banks in the contractual pension fund industry

Depository banks (1)	No. of funds served in		
	2007	2008	2009
Artigiancassa S.p.A.	1	0	0
Banca Monte dei Paschi di Siena S.p.A.	12	8	0
Bnp Paribas Securities Services	0	0	1
ICCREA Banca S.p.A.	1	1	1
Intesa San Paolo S.p.A.	8	8	16
Istituto Centrale delle Banche Popolari Italiane S.p.A.	12	13	14
MPS Finance Banca Mobiliare S.p.A.	0	4	0
Société Generale Securities Service S.p.A.	4	6	7
Unicredito Italiano	1	0	0
Total Funds	**39**	**40**	**39**

(1) Different institutions belonging to the same group are computed as single entities.

Sources: Fund prospectuses and web sites

Conversely, in the open fund industry the depository bank often belongs to the same group that established the fund. Table 3.24 lists the depository banks operating in 2009 and the number of funds served. With the exception of three banks, all the other players serve very few funds (usually one). One bank accounts for a high market share.

Table 3.24

Depository banks in the open fund industry

Depository banks	No. of funds served in:
	2009
Allianz Bank Financial Advisors	2
Banca Antonveneta	1
Banca Carige	1
Banca Fideuram	1
Banca Monte dei Paschi di Siena	2
Banca Passadore & c.	1
Banca Popolare Commercio e Industria	1
Banca Popolare di Bergamo	1
Banca Popolare di Milano	1
Banca Popolare di Novara	1
Banca Popolare di Sondrio	1
Banca Popolare di Vicenza	3
Banca Sella Holding	1
Banco di Desio e della Brianza	3
Banco Popolare Soc. Coop.	2
Bnp Paribas Securities Services	6
Credito Emiliano	1
2S Banca	2
ICCREA Banca	1
Intesa Sanpaolo	31
Istituto Centrale delle Banche Popolari Italiane	1
Société Générale – Securities Services S.p.A.	9
Ubi Banca	1
Unicredit	3
Total Funds	**77**

Sources: Fund prospectuses and web sites

3.2.7
Administrative activities

As mentioned in Chapter 2 the main administrative tasks of contractual funds are usually performed by an institution appointed by the funds themselves. Table 3.25 lists all the institutions offering such activities and shows their high level of concentration.

Even though the financial institutions promoting open funds might carry out administrative tasks, Table 3.26.a shows that for more than one third of open funds an outsourcing solution is preferred. Table 3.26.b lists the institutions appointed by open funds to perform administrative activities, clearly indicating the leadership position of Previnet Spa in this market segment. Conversely, similar outsourcing does not apply to insurance firms offering PIP schemes.

Table 3.25

Institutions appointed by contractual funds to perform administrative tasks (as of June 2009)

Institutions	Funds served
Previnet S.p.A.	*23*
Accenture Insurance Services S.p.A.	*8*
Servizi Previdenziali S.p.A.	*3*
Fondazione E.N.P.A.I.A	*2*
PensPlan Centrum S.p.A.	*1*
Fondazione FASC	*1*
Servizi Previdenziali Valle d'Aosta S.p.A.	*1*
Total	**39**

Sources: Fund prospectuses

Table 3.26.a

Administrative activities of open pension funds: insourcing vs outsourcing solutions (as of June 2009)

Promoting institutions	Insourcing	Outsourcing
Insurance companies	37	18
Banks	3	0
SGR	7	9
SIM	5	0
Total	**52**	**27**

Sources: Fund prospectuses

Table 3.26.b

Institutions offering administrative activities to I open pension funds (as of June 2009)

Institutions	Funds served
Previnet SpA	*15*
OASI Diagram	*6*
Société Générale Securities Services S.p.A.	*3*
RBC Dexia Investor Services Italia S.p.A.	*2*
Accenture Insurance Services S.p.A.	*1*
Total	**27**

Sources: Fund prospectuses

3.2.8. Additional insurance coverages

Most private pension schemes do not simply provide a complementary pension provision at retirement age, but might also incorporate other insurance coverages as additional benefits for their members. Such additional coverages, if any, can be either optional or compulsory. In the first case, the pension scheme member can choose to activate the extra coverage by paying an additional cost; compulsory insurance coverages, on the other hand, are embedded in the pension contract and their costs are included in the total cost of the pension scheme.

Additional insurance coverages are rare among contractual funds: Table 3.27.a shows that only 5 out the 39 contractual funds offer some additional insurance coverages; three funds offer compulsory disability and death insurance. As shown in Table 3.27.b the insurance firms providing such coverages are not necessarily those selected to provide annuitisation.

Table 3.27.a

Types of additional insurance coverage provided by contractual pension funds (as of June 2009)

	Optional	Compulsory	**Total**
Disability	0	0	**0**
Death	0	0	**0**
Disability and death	1	3	**4**
LTC	0	1	**1**
Total	**1**	**4**	**5**

Sources: Fund prospectuses

Table 3.27.b

Contractual pension funds with additional insurance coverages (as of June 2009)

	Optional	Compulsory	**Total**
The additional insurance coverage is offered by the same company that provides the annuity	0	1	**1**
The additional insurance coverage is offered by another insurance company	1	3	**4**
Total	**1**	**4**	**5**

Sources: Fund prospectuses

Additional insurance coverages are more common among open funds: 28 funds provide both permanent disability and death insurance coverage and another fund offers only death insurance (Table 3.28.a). All these coverages are optional. Table 3.28.b provides two lines of information. First, it shows that most of the open funds (21 out of 29) with additional coverages are those promoted by insurance companies. Additionally, Table 3.28.b shows whether the additional coverage is offered by the same insurance company that provides the annuities. This coincidence occurs most frequently (in 24 cases).

Table 3.28.a

Types of additional (optional) insurance coverage provided by open pension funds (as of June 2009)

Disability	0
Death	1
Permanent disability and death	28
Total	**29**

Sources: Fund prospectuses

Table 3.28.b

Open pension funds with additional insurance coverages (as of June 2009)

Funds promoted by insurance companies	21
The provider of additional insurance coverage is the same company that provides annuities	*20*
Funds promoted by banks	1
The provider of additional insurance coverage is the same company that provides annuities	*0*
Funds promoted by investment management companies (SGR)	6
The provider of additional insurance coverage is the same company that provides annuities	*4*
Funds promoted by investment firms (SIM)	1
The provider of additional insurance coverage is the same company that provides annuities	*0*
Total	**29**

Sources: Fund prospectuses

Finally, additional insurance guarantees are frequent in the life insurance experience. Overall, additional guarantees are 84 (Table 3.29.a), 37 of which are compulsory, embedded in the pension contract. Again, the most common forms of coverage are death and disability. As shown in Table 3.29.b, 44 out of the 73 policies for which information were available provide at least one type of additional coverage. The maximum number of different additional coverages provided by a pension scheme is 6, even though 5 of these are optional.

Table 3.29.a

Total number of additional insurance coverages provided by PIPs [1] (as of June 2009)

	Optional	Compulsory	**Total**
Disability	18	4	**22** [2]
Death (Permanent)	7	33	**40** [3]
Death (Term)	4	0	**4**
LTC	7	0	**7**
Dread disease	2	0	**2**
Accident and Health	4	0	**4**
Death caused by accident	1	0	**1**
Death caused by car accident	4	0	**4**
Total	**47**	**37**	**84**

(1) In compliance with Legislative Decree 252/2005

(2) Two PIPs offer both a compulsory and an optional disability insurance guarantee.

(3) Four PIPs offer both a compulsory and an optional permanent death insurance guarantee.

Sources: Fund prospectuses

Table 3.29.b

PIPs [1] with additional insurance coverages (as of June 2009)

	No. of PIPs	Types of additional coverages:		Total no. of additional coverages
		Compulsory	Optional	
without any additional coverage	29	0	0	0
with one additional coverage	23	23	0	23
with two additional coverages	13	8	18	26
with three additional coverages	1	1	2	3
with four additional coverages	4	0	16	16
with five additional coverages	2	4	6	10
with six additional coverages	1	1	5	6
Total	**73**	**37**	**47**	**84**

[1] in compliance with Legislative Decree 252/2005

Sources: Fund prospectuses

4.
HOT ISSUES

4.1
Shadows and lights

As of the beginning of 2010 the Italian complementary pension scheme system presents some positive and negative features.

1. The first positive aspect refers to the schemes' capacity to overcome the worst phase of the financial crisis with limited damage, thus demonstrating the efficiency of the regulations on investing contributions. Although all funds (except those with guaranteed benefits) have recorded negative results, thanks to prudent asset allocation and wide portfolio diversification, the impact of the failures of some financial institution has been minimized. This in turn reduces losses for pension scheme members. While the spillover of the crisis into the real economy has raised unemployment, calling for social security measures, requests to withdraw from the retirement account or surrender have increased only slightly. The restored confidence on financial markets and the first evidence of positive results in 2009 can be an important opportunity to further bolster the system.

2. The crisis in the real sector of the economy has boosted not only unemployment, but also the volume of unpaid contributions due by employers. According to Italian regulations, said contributions are guaranteed by the public sector (which replaces the employer when she is unable to pay), However, recent proliferation of this behaviour highlights the need of more homogeneity of such guarantee procedures across the different types of pension schemes.

3. The drop in asset value triggered by the financial crises underscores an important issue, largely ignored so far, but quite familiar to pension experts: the risk that retirement dates coincide with a time of falling financial asset prices thus decreasing pension benefits. This issue has fuelled a wide debate. Some proposals include forms of solidarity among pension fund members. Although distributing losses among workers in the same fund can be regarded as a good solution (under the assumption that an intergenerational transfer agreement is generally accepted), many difficulties still remain as far as the level, the duration and the funding of this implicit guarantee. For instance, this protection should be explicitly granted to young members whose contributions have been temporarily transferred to retired members. In addition, exiting from a pension scheme at a given date should not be considered mandatory since it could be anticipated or postponed under certain circumstances, thus avoiding or attenuating the impact of falling security prices on pension benefits. Other proposals call for public intervention aimed at funding the reduction in benefits occurring during a temporary downturn of financial markets. However, the problems arising in the case of the intergenerational solution would be further exacerbated in this case, so this option does not seem feasible in practice.

A correct and sustainable solution might be found in the area of asset management through the adoption of investment strategies aimed at reducing the investment risk in the fund as the retirement date approaches. An example is the life style methodology, which systematically

switches the equity and bond percentages in the portfolio according to the age of pension members. This is the most common fund management style in UK defined contribution pension funds. This is also the most popular default option, that is the alternative for those who do not take a specific choice on risk-return profile when they enter the fund.

The asset management industry offers many forms of this approach using different financial devices to manage risk. In the Italian experience, only a few funds have these features, including some date target funds which try to maximize the return at a specific point in time, typically the presumed date of retirement. This approach is based on automatically changing the risk profile over time and requires an accurate estimate of inflows and outflows.

Pension members must be aware of these features and should be able to understand the consequent changes in the financial accumulation process. In order for members to be aware of this risk profile, they must be provided with adequate information and a consistent level of financial capability. We believe that the gap between the actual and the ideal financial capability of Italian workers is quite large on average; therefore a significant and widespread drive toward financial education is required.

4. Another positive profile of the recent development of the Italian complementary pension system is its capacity to serve relevant social functions, acting as a financial cushion for different needs, as in case of unemployment, serious illness, high level of disability, and other forms of advance payment or withdrawal allowed by the regulation. The system, despite the fact that it mainly aims at accumulating resources over the long run, also displays high levels of flexibility, in particular similar to or more than the TFR.

Flexibility is not yet considered a relevant feature of the system by most of the population potentially interested in the complementary pension system. At present this profile has not been sufficiently emphasised or effectively communicated; this is one of the most important barriers to the further development of the system.

Many commentators have stressed the non-reversibility of the choice to transfer TFR into the pension schemes. In fact, once the choice has been taken, the flow of TFR can not be re-transferred within the firm; this is judged an important element of rigidity. As a consequence, many workers may prefer keeping their TFR inside the firm, and later evaluating the opportunity to put it in the pension system in the future, once the proper functioning of the mechanism has been tested. This issue was greatly emphasized during the 2007 TFR campaign, and now it is common knowledge.

The opportunity to rethink the destination of the TFR in some way must be consistent with the long-term view of the accumulation process of pension schemes, so as to avoid frequent changes in asset allocation triggered by short-term results. Consistent with this approach, some commentators have recently suggested that pension scheme members should be permitted to change the destination of their future TFR flows (while this choice should not affect the previous TFR flows). However, such an increase in flexibility should be consistent with the long-term perspective of pension investments. Therefore, changes in the TFR's destination could only occur within few time windows (for instance every ten years and/or only few times during the member's working life).

Such a proposal might have a positive effect on the system if it were adopted according to a new general, multi-lateral campaign of incentives for the development of the complementary pension system, together with other relevant issues discussed in the next paragraph.

5. A further positive feature refers to the size of the market, where some noteworthy schemes have emerged in each of the three typologies. A group of contractual funds has achieved relevant assets under management and a high level of participation among potential members. The breakdown of open funds shows similar development, with important positions in individual as well as collective membership. In addition, some insurance companies offering PIPs have collected considerable premiums in this business.

However only a minority of funds of different types have reached adequate dimensions, and major restructuring is expected. The membership percentage in comparison to the working population is relatively low and stationary after the 2007 TFR reform.

The membership breakdown highlights some gaps. For instance, as pointed out by COVIP, the number of young members is lower than their percentage in the workforce; the same applies to females, to people employed in the South of Italy and/or in smaller firms.

The latter point is of great importance because small and medium-size enterprises are the backbone of the Italian economy. In fact, this is one of the priorities to be considered in order to truly and completely relaunch the system. The problem is an extremely complex one. In small firms, trade unions are rarely present and the relationship between employers and the work force is direct.

The small entrepreneur is less interested in a pension scheme as a tool for industrial relations than large enterprises. In fact, she may have reasons for exploiting a direct employment relationship (which is usually intermediated by unions in larger firms) to guide the worker towards less than optimal pension choices. For instance, a small employer (with less than 50 workers) might prefer that workers maintain the flow of TFR within the firm (instead of transferring it to a pension scheme) because she would retain these financial resources for an extended period of time at very favourable conditions (1,5% plus 75% of salaries inflation index). In the same way if the worker is not enrolled in the pension scheme, the employer does not pay the contributions which are normally due when a new member joins a pension plan.

Therefore, the real stimulus for wide membership of small firm's workers is twofold: first, an increase in the perceived interest of the employees for the pension option along with adequate information, financial capability, and awareness of the relevant protection achievable through the complementary pension (the choice of membership is free); second, a set of incentives compensating the employer for the costs of employee enrolment. A number of proposals are under discussion, for instance access to a guarantee facility fund for the flows transferred to the complementary pension schemes.

6. Another structural membership gap is the limited participation of public employees. As mentioned new contractual funds will begin to operate but we need a new regulation for true development in this sector.

7. A further positive development of the complimentary pension system concerns the provision of annuities. For a long time the main interest of funds and commentators has been focused on the accumulation process while the annuity profile has been neglected. This is also due to a lack of tradition of this type of contract in the Italian life insurance market. (We refer to the overall market.) This circumstance in turn can be explained by the very low demand for such products in a context where the level of the replacement ratio accorded in the past by the first pillar pension was generous. In addition, policyholders exhibit a high propensity for the tax-favoured capital option (instead of the annuity) in life insurance contracts.

The different nature and structure of various types of funds have influenced their behaviour. In the first years of operations, only a few contractual funds selected annuity providers through a call for tender; most of them postponed the choice. Conversely open funds and PIPs, being established by financial institutions have proposed several types of annuities, mimicking the supply model adopted in the general life insurance market. However, some PIPs have borne a certain degree of demographic risk, committing to maintain certain annuity conversion coefficients till a fixed future date. In alternative, some PIPs apply all the coefficients in force each year of contribution according to a pro rata approach instead of applying only the coefficient in force at the end of the contribution period. In any case, the terms and conditions of the annuitisation agreements embedded in these pension schemes were quote favorable to the members, possibly because until recently annuity demand was more potential than actual.

The increasing number of members who have entered the phase of possible retirement has induced many contractual funds to select annuity providers through a call for tenders arranged by Assofondipensione, the association of contractual funds. As mentioned in the second chapter, this tender has become a cornerstone for competing in the provision of annuities services. Both the contractual provisions and the levels of annuity coefficients act as important and transparent benchmarks (downloadable from fund websites) for the supply of the whole market. It is worth mentioning that many new annuity policies provided by pension schemes offer death and LTC insurance coverage at conditions slightly more expensive than those of other common annuities.

If this information were widespread and properly communicated and financial education were adequate, the observed propensity to receive a lump sum at retirement could be replaced by a more rational preference for the annuity option.

8. Notwithstanding the improvement in types and conditions of annuities, the demand for this option is likely to remain very low because it is not adequately encouraged by the regulation. As mentioned in Chapter Two, the complementary system attempts to combine the long-term view of the accumulation program with the flexibility needed to meet social needs. A certain level of flexibility is a pre-condition to entering the scheme, especially when comparing the TFR option. However, we think that the level of flexibility can be partly reduced to acceptable levels without jeopardizing the annuity option. For instance, we refer to the regulation concerning the amount to be used for determining the lump sum allowed. At the present time the amount paid in advanced and not reimbursed is not included in the calculation. Thus, by requesting a lump sum, a pension scheme member could decrease the share of her pension benefits paid as annuities. If this annuity were below the minimum level, the entire amount of pension benefits could be paid as capital. Note that the lump sum and annuity options are treated equally from the fiscal point of view. We think a new rebalancing of flexibility and the long-term pension view is a requisite for consistent development of the complimentary pension system.

9. The need for further development of the complementary system is strictly linked to the adoption of new transformation coefficients of the public pension (which will come into effect in 2010). These will reduce the replacement ratio of the first pillar. This new rule requires the population to be specifically informed and calls for a stronger and more extensive complementary pension system.

4.2
Possible changes

This analysis suggests that a number of appropriate actions should be adopted to improve the complementary pension system without major changes to the regulations.

1. A new institutional campaign aimed at promoting awareness about the new replacement ratio of the first pension pillar should be implemented. The message should be truly effective; for this reason it should be addressed by those institutions that pay the public pension to workers. The awareness of the pension gap is the most effective incentive for workers to enrol in complementary schemes. Moreover, this information campaign is vitally important for the further development of the system. This project has been the subject of lengthy discussion, but the imminent impact of the new coefficients calls for immediate action.

2. Along with this information campaign, a deep, widespread and specialized financial education program should be activated. This campaign should be supported and primarily run by the institutions involved in the pension system, to both improve information levels and implement knowledge devices in a reliable *super partes* approach. This program should be aimed at explaining the risks workers face in the retirement period and the way the complementary pension system can help handle them. A specific effort should be made to develop a correct pension view adopting a long-term approach. Particular importance should be given to both the investment and the distribution phase. Some basic principles of rational financial behaviour should become common knowledge throughout the working population. Particularly, the importance of having a recurrent lifetime income should be stressed. Pension experts know that the primary purpose of a pension plan is to fund income rather than capital; an annuity, therefore, is an essential feature for a defined contribution scheme.

Several profiles must to be implemented in combination:

- First, the regulation should encourage the annuity option, maintaining an adequate balanced flexibility to face important specific needs, using fiscal incentives in favour of the annuity option, and/or modifying the choices available.
- Second, pension schemes should provide different types of annuities, including those that also include death and/or LTC insurance coverage; this should be offered at competitive conditions.
- Third, terms and conditions of annuities should be easily comparable. To achieve this, the pension schemes should be obliged to provide a clear and complete description of the relevant variables (i.e., interest rates, periodicity, and revaluation criteria). In addition, an adequate comparison format should be implemented, for instance in a special part of the website of the Supervisory Authority.

3. Real and widespread participation of public workers should be favoured through the adoption of the rules which have been under discussion for some time.

4. Summing up, the following are major steps toward significant quality improvement of the complementary pension system: (i) the stimulus coming from the new coefficients of the first pillar; (ii) an increase in the level of financial specific capability in both the investment and distribution phase; (iii) the existence of proper incentives for the annuity option in a more

transparent and competitive insurance segment, together with an adequate level of flexibility; and (iv) the extension of membership to the public sector.

APPENDIX

1.
Italian private subordinate workers severance package (Trattamento di fine rapporto - TFR)

Since 1982 Italian employment laws require private companies to set aside an amount equal to 6.91% of the wages of employees as part of a supplemental payment to which they are entitled at dismissal. Provided that a pension plan is not vested with this money, the employer is mandated to add interest to this fixed share at a rate linked to inflation (i.e. 1.5% + 0.75*yearly consumer price index change measured at the end of December) in order to preserve purchasing power over time. The amount to be liquidated to the worker is therefore the sum of annual allowances and accrued interest.

The payment is meant to be a cushion that allows the worker to face liquidity constraints arising if a period of prolonged unemployment follows a job dismissal. However, if certain conditions are met, an advance payment can be granted by the employer. The money must be needed in order to fund the following: i) special medical treatments, ii) worker's own or children's house purchase, iii) parental leaves and sabbatical leaves for professional training. This advance can be paid provided that the employee has worked for a minimum of eight years for the same firm and has never requested it before. The law applies to companies with more than 25 employees.

Since 2007 workers can decide either to send new TFR flows to a pension scheme or to leave this money in the firm. In this latter case the amounts set aside for severance payments have to be transferred to the private employees' social security institution – INPS - if the firm size exceeds 49 workers. INPS vests a special pool with these financial resources ("Fondo di Tesoreria" or treasury fund) and handles their management. INPS will then relinquish the money to the employer upon the worker's dismissal in order for the firm to physically make the severance payment.

Employers with fewer than 50 workers can keep the money and fund their business with it, provided that they pay their dues to workers at dismissal.

Moreover, payments are guaranteed by an insurance scheme managed by INPS.

If the worker does not make any choice, according to the tacit consent principle, flows are automatically transferred to a collective scheme. If no plan is contractually available for the individual employee, flows are transferred to a special complementary pension scheme established within INPS and regulated by the same conditions of other pension funds. Flows of TFR coming from the adoption of the tacit consent principle must be guaranteed. The rule requires a minimum guarantee on capital if specific events occur. An additional return comparable with TFR's total yield is granted on a best-effort basis.

2.
The ISC Index

The index aims at supplying potential and actual members of pension funds with a reasonable assessment of the annual cost of their participation in the scheme during the accumulation phase.

It is computed over a 2, 5, 10 and 35 year timeframe for each sub-fund offered.

The index is the difference between the internal rate of return obtained by investing 2,500 euro every year at the beginning of the period with an annual accrued gross interest rate of 4% which is taxed at an 11% rate (R_T) and the internal rate of return on the same investment whose cash flows are decreased by the expenses due to the pension scheme in addition to the fiscal levy (R_N).

Not all costs enter in R_N calculation. Only fees to be paid for transferring individual positions to other plans are considered among the dues linked to exercising options (switching and other option-related costs are excluded in order to simplify calculations. Performance and purchase fees the scheme may charge in order to recover costs of buying and selling securities are omitted as well. Exceptional and unforeseeable costs are not included.

On the other hand, financial and administrative costs that are usually charged directly to the member balance at the end of the year have to be estimated on the basis of the most recent past figures and have to be included in the computation. Moreover, if enrolling in the scheme implies payment of premiums for additional guarantees (e.g. death benefits, guaranteed minimum returns and so on) the relevant amounts paid must be included among the overall costs unless an opt-out clause is contractually envisaged.

In order to give separate evidence of costs linked to additional insurance and financial guarantees, the ISC index is split into two different components:

I. C_G which quantifies the weight other costs have on individual positions;

II. C_A which measures the weight of premiums for additional guarantees.

To this end a third internal rate of return is computed, including only costs of additional insurance, financial guarantees and fiscal levies (R_L). The difference between R_T and R_L is C_A while the difference between R_L and R_N is C_G.

Summing up:

R_T = yearly IRR of investing 2,500 euro every year in the plan at the beginning of the period with an accrued interest rate of 4% and a fiscal levy of 11%

R_N = yearly IRR of investing 2,500 euro every year in the plan at the beginning of the period with an accrued interest rate of 4% a fiscal levy of 11% after paying all dues contractually contemplated in the scheme (excluding some costs linked to options' exercise or performance and purchase fees).

R_L = yearly IRR of investing 2,500 euro every year in the plan at the beginning of the period with an accrued interest rate of 4% a fiscal levy of 11% after paying premiums for additional insurance and financial guarantees.

$R_T - R_N$ = ISC index (weight of overall costs on the potential member balance at the end of the year)

$R_T - R_L = C_A$ index (weight of costs for additional guarantees on the member balance at the end of the year)

$R_L - R_N = C_G$ index (weight of costs other than additional guarantees on the member balance at the end of the year).

3.
Major investment limits

Italian private pension schemes introduced in 1993: major investment limits

Security type		Investment limits
Bank deposits, cash and short term bills		Max 20% of the fund's assets
Closed end mutual funds		Max 20% of pension fund's assets and max 25% of the closed end NAV
Securities traded on regulated markets of EU member countries, USA, Canada or Japan	Issued by entities domiciled in OECD countries	Any percentage of the pension fund's net assets
	Issued by entities resident in non-OECD countries	Max 5% of the pension fund's net assets
Securities not traded on regulated markets of EU member countries, USA, Canada or Japan	Issued by entities domiciled in OECD countries	Max 50% of the pension fund's net assets, with the following further limitations: • Stocks cannot exceed the 10% of the pension fund's net assets • Debt securities issued by other entities than OECD countries and supranational organizations cannot exceed the 10% of the pension fund's net assets
	Issued by entities domiciled in non-OECD countries	Not allowed
Securities issued by the same entity (or different entities belonging to the same group) (1)	Traded on regulated markets of EU member countries, USA, Canada or Japan	Max 15% of the pension fund's net assets
	Non traded on regulated markets of EU member countries, USA, Canada or Japan	Max 5% of the pension fund's net assets
Voting shares issued by the same company (2)	If listed	Max 5% of total nominal value of all voting shares of the company (3)
	If not listed	Max 10% of total nominal value of all voting shares of the company (3)
Shares issued by an entity which is required to make contributions to the pension fund (2)	If the pension fund is a contractual one	Max 30% of the fund's net assets
	Otherwise	Max 20% of the fund's net assets

(1) This limit does not apply to debt securities issued by OECD countries.

(2) As ruled by Legislative Decree 252/2005.

(3) In any case the total amount of voting shares issued by the same company cannot be as large as the pension fund might exercise a dominant influence over the issuer company.

CAREFIN
Centre for Applied Research in Finance
Università Bocconi
via Roentgen 1
I-20136 Milano
tel. +39 025836.5908/07/06
fax +39 025836.5921
carefin@unibocconi.it
www.carefin.unibocconi.it