

## **DEVELOPMENT OF PRIVATELY MANAGED PENSION FUNDS IN THE CONTEXT OF PENSION REFORM**

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**ABSTRACT:** *The development of privately managed funded pension provision reflects some trends in societies, like for instance richer societies which might favour more responsibility and choice for individuals, or the expectation that diversifying risks through funded pension might achieve higher returns than GDP growth, while it also means inevitably higher risks. With the development of privately managed funded pensions, the question of the sharing and regulation of risks becomes relevant due to the fact that such schemes may also be expected to provide pension adequacy for lower income groups.*

**KEYWORDS:** *private funded pensions; pensions reform; pensions schemes; mandatory private pension; voluntary private pension*

### **1. INTRODUCTION**

The role and development of private funded pension provision is very diverse and some important decisions remain to be made, notably regarding the organization of the pay-out phase.

Further analysis appears necessary, on the basis of indicators, to assess the impact of the development of these schemes on future pension levels. In particular in the later two types of schemes private provision (be it mandatory or not) need to be analyzed in terms of coverage and amount of contribution to better understand the impact on adequacy and indirectly on sustainability. Moreover financial risks and security might also impact on future benefits. Coverage might be less of an issue in mandatory schemes but this also need to be analyzed in a context of evolving labour markets and changing societal risks leading to longer periods of non-contribution to pension schemes.

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Such reforms need to develop a comprehensive approach covering all types of pension schemes, since the ageing challenge is common to all pension systems: all pension systems need to compensate for the decline in employment of older workers and the continuous increase in life expectancy. Pay as you go systems are directly affected by population ageing as their future contribution base is shrinking while the number of beneficiaries is increasing. In funded systems, the increase in life expectancy also implies some imbalance: if contributions are not increased and/or people do not retire later, benefits would also be lower.

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## 2. THE IMPACT OF THE MANDATORY PRIVATE PENSIONS DEVELOPMENT

Financial security upon retirement can be supported through diversification of obtaining pensions, a pension scheme that is based on several components. Reform of pension system in Romania allowed besides the public pension system, called Pillar I, which is a distributive system based on solidarity between generations (regulated by Law 19/2000 on public pension system and other social insurance rights, with subsequent amendments and supplements) to implement a private pension system that records the contributions of participants in individual accounts, based on capitalization, investment and accumulation of these contributions. Private pension system is implemented in two forms:

- mandatory private pension (pillar II) regulated by Law 411/2004 on privately managed pensions, as republished;
- voluntary private pension (pillar III) regulated by Law 204/2006 on voluntary pensions.

**Table 1. Characteristics of pensions types in Romania**

Pension type	Contribution type	Type of fund management	Age of persons participating in the system
Public pension (Pillar I)	Compulsory	Public	All employees aged over 45 years old, and optionally those aged between 35 and 45 years old
Mandatory private pension (Pillar II)	Compulsory	Private	All employees aged under 35 years old and optional ones aged between 35 and 45 years old
Voluntary private pension (Pillar III)	Voluntary	Private	Employees aged up to 60 years old

In May 2009, 4,325,094 participants contributed to private pension funds and the number of participants enrolled in the Registry of participants was 4,752,942 persons (table no. 2). The number of participants increased in May 2009 by 0.8% from the previous month and 35.4% compared to May 2008, representing 86% of the total employees in Romania. Degree of concentration retains the same values recorded in previous months, the weights of the first three privately managed pension funds -69% of participants and funds within the first 5 - 82% (figure 1).

**Table 2. Pillar II Number of participants enrolled in the Registry of participants**

<b>Mandatory private pension fund</b>	<b>31.05. 2008</b>	<b>31.12. 2008</b>	<b>31.01. 2009</b>	<b>28.02. 2009</b>	<b>31.03. 2009</b>	<b>30.04. 2009</b>	<b>31.05. 2009</b>
AIG	261,47	282,54	285,12	288,65	291,70	293,93	295,22
ARIPI	389,95	427,16	431,88	438,07	443,37	447,05	449,59
AZT VIITORUL TAU	1.065,87	1.158,21	1.170,68	1.185,62	1.199,06	1.208,81	1.213,56
BCR	124,17	145,03	148,12	151,14	153,68	155,93	157,59
BRD	99,32	107,41	108,46	109,78	110,98	111,87	112,42
EUREKO	264,33	287,04	289,87	293,10	296,23	298,48	299,46
ING	1.380,56	1.504,29	1.520,21	1.541,66	1.558,86	1.571,17	1.578,84
KD	7,58	8,11	8,19	8,26	8,35	8,41	8,28
OTP	20,61	22,12	22,33	22,52	22,75	22,92	22,83
PENSIA VIVA	306,20	332,53	335,84	339,88	343,71	346,42	347,61
PRIMA PENSIE	17,42	20,69	21,04	21,33	21,62	21,81	22,04
VITAL	131,60	141,99	143,37	145,20	146,76	147,89	148,93
<b>TOTAL</b>	<b>4.156,32</b>	<b>4.531,86</b>	<b>4.580,79</b>	<b>4.642,00</b>	<b>4.693,93</b>	<b>4.731,54</b>	<b>4.752,94</b>

Net assets of the 14 pension funds, administered by the 14 directors authorized by CSSPP in Pillar II, was in May 1.437.225.124 Lei, 8% higher than April 2009 and approximately 17 times higher than May 2008.

Also regarding the net assets, the degree of concentration was maintained in May 2009, top three funds have recorded 70% of the total, and the top five funds 84%.

In May 2009, transferred contributions worth about 113 million lei to 3.413 million participants. In these months contributions were transferred to 28% of total participants in the Registry of participants. Maintaining the last year and the first months of this year trend, the number of empty accounts in Pillar II continued to decline in May representing 9% of total registered participants accounts.

Average contribution / participant were in May 2009, as the previous months, 26 lei. If we relate to the number of participants for which contributions were paid in May 2009 average contribution was 33 RON, which represented approximately 1.72% of gross wages in March 2009.

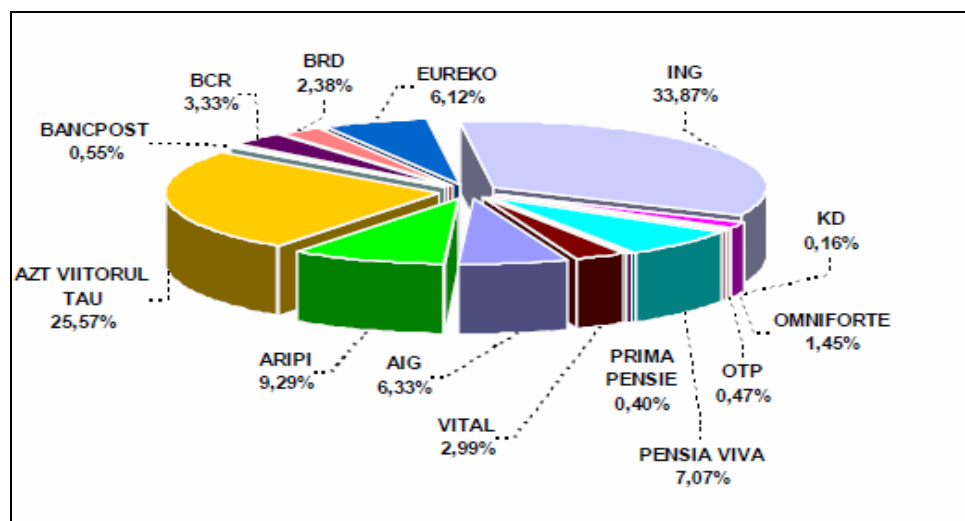


Figure 1. Pillar II Participants % of total-May 2009

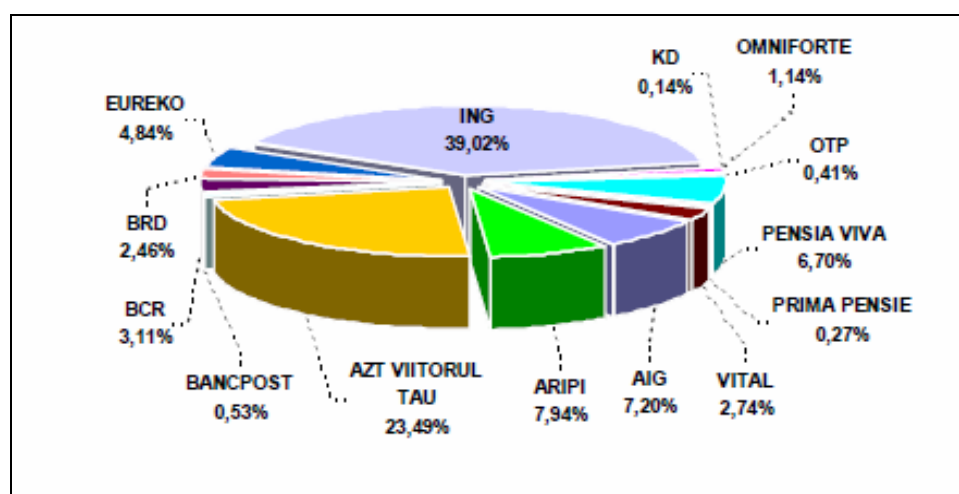


Figure 2. Pillar II % of total net assets-May 2009

In May, of all participants registered in the Register of Participants - 4,752,942 people, 64% were aged up to 35 years and 36% aged over 35 years old (table 3). Regarding the gender structure, 52% of the participants were male and 48% female, in both cases, gender and age, maintaining the values recorded in previous months (table 4).

Contribution to private pension funds, currently 2%, is deducted from monthly gross income, which represents the basis for individual social security contribution.

During May 2009, private pension fund managers continued to invest mainly in low-risk assets, as in 2008 and the first months of 2009. Thus, 53.39% of the assets

of privately managed pension funds were government securities, in constant decline over the previous months.

**Table 3. Pillar II Participants in the register-age structure-May 2009**

Mandatory private pension fund	31.05.08		31.12.08		31.01.09		31.05.09	
	until 35 years	over 35 years	until 35 years	over 35 years	until 35 years	over 35 years	until 35 years	over 35 years
AIG	162,33	99,14	177,18	105,36	178,83	106,28	184,94	110,28
ARIPI	201,48	104,72	281,75	145,42	284,89	146,99	295,97	153,62
AZT VIITORUL TAU	691,11	374,76	753,96	404,25	761,39	409,29	783,35	430,20
BCR	13,92	9,72	86,93	58,10	89,00	59,12	94,68	62,91
BRD	62,29	37,03	67,92	39,50	68,59	39,87	71,04	41,38
EUREKO	255,31	134,64	187,56	99,48	189,47	100,40	195,66	103,80
ING	86,31	45,29	966,68	537,61	974,97	545,25	1.000,37	578,47
KD	171,15	93,17	5,13	2,98	5,19	3,00	5,26	3,02
OTP	4,75	2,83	14,21	7,91	14,36	7,97	14,67	8,16
PENSIA VIVA	40,44	23,17	220,76	111,77	222,99	112,86	230,46	117,15
PRIMA PENSIE	13,12	7,49	13,59	7,10	13,85	7,19	14,48	7,55
VITAL	11,21	6,20	93,74	48,25	94,64	48,73	97,93	51,00
<b>TOTAL</b>	<b>2.683,42</b>	<b>1.472,90</b>	<b>2.929,04</b>	<b>1.602,82</b>	<b>2.958,45</b>	<b>1.622,34</b>	<b>3.048,96</b>	<b>1.703,99</b>

**Table 4. Pillar II Participants in the register-gender structure-May 2009**

Mandatory private pension fund	31.05.08		31.12.08		31.01.09		31.05.09	
	Female	Male	Female	Male	Female	Male	Female	Male
AIG	128,80	132,67	137,48	145,06	138,63	146,49	143,63	151,59
ARIPI	186,61	203,35	202,41	224,75	204,58	227,30	213,24	236,36
AZT VIITORUL TAU	515,78	550,09	554,46	603,75	560,13	610,55	581,21	632,35
BCR	58,60	65,56	67,97	77,06	69,46	78,66	74,17	83,42
BRD	46,72	52,60	50,06	57,35	50,54	57,91	52,52	59,90
EUREKO	126,78	137,55	136,12	150,92	137,38	152,48	142,08	157,39
ING	701,46	679,10	754,09	750,20	761,36	758,85	790,73	788,12
KD	3,43	4,15	3,63	4,48	3,66	4,52	3,70	4,58
OTP	9,30	11,30	9,92	12,20	10,01	12,32	10,29	12,54
PENSIA VIVA	148,89	157,31	159,73	172,79	161,21	174,63	166,85	180,76
PRIMA PENSIE	8,01	9,40	9,63	11,06	9,79	11,25	10,30	11,74
VITAL	61,89	69,71	66,18	75,81	66,82	76,56	69,55	79,38
<b>TOTAL</b>	<b>2.037,88</b>	<b>2.118,43</b>	<b>2.196,37</b>	<b>2.335,49</b>	<b>2.218,69</b>	<b>2.362,09</b>	<b>2.303,82</b>	<b>2.449,13</b>

In May 2009, approximately 73.7% of the assets of privately managed pension funds were placed in the country, and the remaining approximately 26.7% were foreign investments.

### 3. CONCLUSIONS

The role and development of private funded pension provision is very diverse and some important decisions remain to be made, notably regarding the organization of the pay-out phase.

Pensions' reforms need to develop a comprehensive approach covering all types of pension schemes, since the ageing challenge is common to all pension systems: all pension systems need to compensate for the decline in employment of older workers and the continuous increase in life expectancy. Pay as you go systems are directly affected by population ageing as their future contribution base is shrinking while the number of beneficiaries is increasing. In funded systems, the increase in life expectancy also implies some imbalance: if contributions are not increased and/or people do not retire later, benefits would also be lower.

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