



SOCIETY OF ACTUARIES

Article from:

In The Public Interest

January 2011 – Issue 3

SOME THOUGHTS ON THE FRENCH PENSION REFORM

By Florian Léger*

One cannot discuss the French pension system without going back to 1983 when President Mitterrand generalized the possibility to retire at 60, which was a great social advance for many. It became a symbol that no government dared to touch, until this year. The mid '80s also coincide with the first years of the deficits in the social security system in general and the pension system in particular. Funnily, the first study pointing out the future deficit of the pension systems was prepared in the mid '80s by Dominique Strauss-Kahn, the current Managing Director of the International Monetary Fund (IMF). A report ordered by Prime Minister Rocard in 1989 also pointed out the ageing of the population and the necessity to reform the system.

The first reform came during the summer of 1993, in the form of a unilateral decree from the Government (there was no discussion with the employers' and employees' representatives). It moved from wage to price indexation, progressively increased from 37.5 to 40 years—the required number of years to get a full pension—and progressively based the calculation of the pension benefits on the salaries of the 25 best years (instead of 10). In aggregate these reforms resulted in a decrease in pension levels today, estimated to be about 20 percent.

In 2003, a further major reform was passed, this time after lengthy discussions between the government and the social partners (employers and employees), the support of one trade union, and a series of strikes. The 2003 reform aligned the parameters for civil servants who had not been affected by the 1993 reform, and further increased the number of years required to get a full pension to 41 years. In addition, it also opened the possibility for those with lengthy careers (more than 40 years) to retire before the age of 60. That possibility has been largely used at a cost far above what was estimated.

Just after the presidential election in 2007, another reform, mainly concerning special schemes which still had not been reformed, was voted on. France has a very fragmented pension system with still today more than 30 different



compulsory public pension schemes. The main one is the National Old-Age Insurance Fund (CNAV) for employees in the private sector. Besides it, there are pension schemes for farmers, self-employed (several schemes for different categories of self-employed), civil servants, employees of the public companies (railways, metro, Electricité and Gaz de France, Opera, Bank of France, etc., have their own schemes), employees of local authorities, public hospital workers, etc. Some are considered to be first pillar systems, others include both first and second pillars (often with different provisions for both pillars) and some schemes are only second pillar, like the General Association for Pension Institutions for Managerial Staff and the Employees' Complementary Retirement Schemes Association (AGIRC-ARRCO) which is the compulsory second pillar scheme for employees in the private sector.

SOCIAL SECURITY AND PENSIONS IN FRANCE, FROM DEFICITS TO DEFICITS

France's public pension system can be categorized as very strong as it provides for more than 85 percent of the income sources of older people (the highest share in OECD countries after Hungary). The poverty rate among the elderly is lower than the OECD average (8 percent against 13.3 percent) and is equivalent

France has a very fragmented pension system with still today more than 30 different compulsory public pension schemes.

CONTINUED ON PAGE 8



Florian Léger is a qualified member of the Institut des actuaires (France) and Project Manager, International Social Security Association. He may be contacted at legerf@ilo.org.

to that of the general population, meaning that the French pension system meets its objective of poverty alleviation. The gross replacement rate varies between 58 percent and 65 percent and the net replacement rate varies between 71 percent and 80 percent depending on the income, but is declining as a result of the past reforms. In addition, life expectancy at birth in France is one of the highest in the world, with 78 years for males and 85 for females. These pension levels can only be provided through high expenditure. In 2007, France spent 13 percent of its GDP on public pension, the second highest among the 27 member states of the European Union (EU).

As a result, the social security system in general and the pension branch in particular has been confronted with deficits for several decades already, with only a few years of surpluses. In the mid '90s when the deficit was particularly high following the 1993 economic crises, the government decided to create a fund (the CADES) responsible for amortizing the social debt of the country. This fund, financed by a special contribution based almost entirely on income from work and capital was supposed to run until 2008 when the deficit would have been entirely covered. Unfortunately, following the continuation of the deficits in the late '90s and early 2000s, the existence of the CADES has already been extended on several occasions. Up to now, this is about EUR 140 billion that the CADES has had to refinance and its existence is expected to continue until at least 2025.

In addition to the CADES (which does not refinance only pensions, but all other branches), based on the example of the United States and Canada, the Government created in 1999 a Reserve Pension Fund (Fonds de Réserve pour les retraites, FRR) that aimed at easing the pension deficit due to aging after 2020. The idea was to have some prefunding, but it was not clear from the beginning if the FRR was supposed to be a sustainable fund or just a smoothing fund with its assets depleted over a period of time. It quickly became apparent that only the second solution would be possible as the funds transferred to the FRR (from priva-

tization and others) were far from what was once expected (but still amounted to EUR 33 billion in June 2010). In 2009, during an ISSA Technical Seminar on Pensions held in Paris, the Chairman of the Supervisory Board of the FRR, Mr. Raoul Briet, said that compared to the mountain of debt, the FRR was a small sandbox.

THE 2010 REFORM

Obviously, the financial and economic crises of 2008 – 2009 changed things. From an already significant deficit of EUR 5.6 billion in 2008, the deficit for the first pillar of the main pension schemes alone grew to EUR 7.2 billion in 2009, and is expected to be EUR 8.6 billion in 2010. The total deficit of the public pension system in France is estimated by the government to be about EUR 30 billion, but half of it comes from the Civil Servant schemes that are financed directly from the government budget.

As part of the 2003 reform, a review of the situation was planned for 2010, based on the work of the “Pensions Advisory Council” (Conseil d’orientation des retraites, COR) created in 2000, which is a permanent body that brings together members of Parliament, representatives of the social partners, experts, and representatives of the State. Its main purposes are to monitor the French retirement system and to put forward recommendations.

The COR did its homework and based on new projections until 2050, the Government submitted a draft bill to the parliament in June this year with the aim to restore the financial balance of the pension schemes by 2018. The reform was approved by the lower chamber of parliament on Sept. 15, 2010. The upper house discussed it in October of 2010 and a vote for a common text was held on Oct. 26, 2010. It is expected that the President will promulgate the law in mid-November.

The main changes are summarized below:

- The statutory retirement age is to be raised from 60 to 62 by 2018 at a rate of four months per year beginning July 1, 2011.
- The minimum age for payment of a full pension without reference to career span is cur-

rently 65. Starting on July 1, 2016, this age limit will be raised at the same rate as the statutory retirement age until it reaches the age of 67 in 2023. The new retirement age will also apply to civil servants. The age of retirement will also be raised by two years for those subject to a different age limit.

- The “extended careers” scheme which enables those who started work very young to retire before the age of 60 will be amended in line with the reforms.
- Beneficiaries suffering from health problems as a result of occupational exposure to hardship will still be entitled to retire on a full pension at age 60. It is expected up to 10 percent of a cohort could qualify.
- Several new sources of funding have been identified: high income earners will contribute through a one point increase in the top income tax bracket, also taxes on stock options and executive pension top-ups will increase significantly; capital income will also be targeted, with an increase in capital gains tax on gains from the disposal of securities and real estate and on dividends and interest. At the corporate level, the method of calculation of tax relief on employers’ contributions and tax on company dividends will change.
- The employee share of the contribution rate for civil servants will gradually be aligned with the private sector, rising from 7.85 to 10.55 percent by 2020.

THE ROLE OF ACTUARIES

The role of actuaries in the French social security system is rather limited. This comes from the weird fact that when Social Security was created in France in 1945, it was believed that actuaries were not strictly necessary as they would be for Social Insurance. That being said, there were some famous actuaries working in the Ministry for Social Security like Francis Netter, but very few in the schemes themselves.

From the 2010 Yearbook of the French Institute of actuaries, only two actuaries work at the National Old-Age Insurance Fund (CNAV) and one of them has actually retired (CNAV is the biggest pension scheme in France accounting for 15 million salaried workers

from the private sector and 11 million beneficiaries (old-age and survivors) and pays EUR 100 billion a year of benefits). There are five working at the General Association for Pension Institutions for Managerial Staff and the Employees’ Complementary Retirement Schemes Association (AGIRC-ARRCO), one at the Insurance Scheme for the Self-employed (RSI), none at the Central Fund of Social Agricultural Mutual Benefit Societies (MSA), none at the Complementary Retirement Pensions Institutions for Unestablished State Employees and Employees of Public Administrations (IRCANTEC). However, some of the first pillar schemes (mainly the small ones) ask private consulting actuaries to undertake their actuarial valuations.

Financial projections of the pension system are called long-term projections, there is no use of the word actuarial. Actuaries are mentioned when describing how financial projections are made abroad.

The French Institute of Actuaries is heavily trying to have a voice in the debate but much still has to be done in that respect.

CONCLUSION

Opinion polls have indicated that the French people massively supported the strikes against the reform but that they have unhappily renounced the right to retire at 60 years of age. Sadly, strikes in France resemble “déjà vu” and like any tradition, a reform without a strike cannot be named so. It is even thought that President Sarkozy did in that respect support the strikes, but his government did not change much of the plans as an answer to them.

Nevertheless, it can already be said that this pension reform will not be the last reform. Without making any projection about the future majority (presidential and legislative election will take place in 2012) the reform covers the deficits until 2018. But as one can expect life expectancy to continue to increase (among other factors influencing the financial situation of pension schemes), more will have to be done. 🙏

The role of actuaries in the French social security system is rather limited.