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Recent developments in financing social security in Latin America

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Introduction

Social security has evolved across the world during the last century, as general industrialization, urbanization and the formalization of economic relationships by markets have characterized current development patterns. Our understanding of social security has also changed during this time. Social security began as a social policy for workers, to collectively insure against the risk of losing an individual's source of income (in the Bismarckian model). It has evolved towards the Beveridgian goal of "freedom from want" or as expressed in the statement that "everyone, as a member of society, has a right to social security ... indispensable for his dignity and the free development of his personality" (Universal Declaration of Human Rights of 1948, art. 22).

Within the Bismarckian conception social insurance was institutionalized for salaried workers, on the basis of employers' and employee contributions. Affluent individuals were left to private insurance schemes. Public employees were provided for through state pensions, a relationship that aimed to assure their special loyalty toward the State. The poor (among them orphans, widows, disabled) and the destitute had to rely on family transfers and a "poor-law" type of social assistance, often with the obligation to accept work.

The development of the "Welfare-State model" was a policy consequence of sequentially broadened interpretations of the concept of social security, that accompanied the evolution of social-democratic ideals in a wide sense and that was based on a corporate and statist framework. However, the costs of growing social security structures have risen significantly at a time when unemployment has increased due to changes in technological patterns and at a time when the global economic integration of societies has caused greater sensitivity to international economic shocks. Increasing poverty and deprivation have been observed in both developed countries and the Third World. Claims have been advanced for a "Regulatory-Subsidiary-State model", in which the State would hand over, as far as possible, the insurance function to the private sector. It is argued that this would ensure greater efficiency and lower costs. These private arrangements would be supplemented with a poverty-targeted public policy. The "Regulatory-State model", based on liberal ideology and directed towards the affluent, is thus in line with the "subsidiarity" principle of the Catholic social doctrine, supplemented with a reduced, targeted Welfare-State component towards the poor.

The previous Latin American model has its roots in a corporatist organized State, from its early beginning in the 20th century. An evolutionary expansion has taken place in concentric circles, ultimately resulting in the present truncated and sui generis Welfare-State(1). Coverage with generous conditions was granted first to well-paid salaried employees. It was extended afterwards to include weaker groups, usually with the intent of legitimizing national governments and development strategies. The financial basis that made a generous expansion possible was the young demographic structure together with the possibility of progressively enlarging the "coverage circles" to include new contributing clusters. As the schemes became mature and reached the limits of coverage expansion (growing informal sectors, decreasing possibilities of extending salaried occupation patterns), compounded by demographic changes in the age structures, the fundamental dynamics of the structure broke down and social security in Latin America fell into crisis. This occurred first in Uruguay, the "pioneer" of social security of this type in Latin America.

The need for social security reform in Latin America exists and a controversial debate about the shape it should take has also occurred. Several countries have already taken steps to restructure their social security systems, compelled by all the above-mentioned problems. However, the choices have been different from country to country.

The goal of this paper is to provide an overview of the main features of reforms or reform attempts in the recent past. In the following section, some general comments will be made regarding the history and characteristics of Latin American social security systems. This is followed by a report of some experiences and their current reforming situation. Finally, a few conclusions are drawn based upon these case reviews.

Chapter 1

Social security in Latin America

If social security is understood as covering those risks listed in the 1952 Social Security (Minimum Standards) Convention No. 102/ILO[(2)] together with social assistance (Income Security Recommendation No. 67, 1944), modern social security's origins in Latin America can be traced to the first decades of the current century. Coverage expansion was a response to pressure groups along professional lines; generally those first covered were the military, public, industrial and salaried urban occupations, followed (but not in all cases) by other groups in the services sector (household employees) and finally (in some instances) the rural sector and the workers in the agricultural sector. Another sequence frequently observed was that provisions for work injury insurance came first, followed by sickness-maternity programmes, then old-age-disability-survivor pensions and finally unemployment insurance[(3)].

Despite its current problems and shortcomings, social security in Latin America has genuine achievements worthy of recognition. One of the examples that can be given is that universal coverage of social security and social assistance in several countries of the region (see Table 4) helped avoid a further deepening of the profound social wounds inflicted during the economic crisis of the 1980s. This happened mainly through investment in public health structures and health service delivery[(4)]. One of the main shortcomings that needs to be emphasized has resulted from the concentric coverage expansion pattern mentioned above. Depending on the political influence of the insured[(5)] extremely generous entitlements (relative to historical contributions) and the possibility of the cumulation of social security benefits, have been assured to a minority thus creating inequality of treatment.

In most cases, social insurance programmes were thus prevented from achieving financial and actuarial soundness after the completion of the phases of horizontal and vertical coverage expansion. As entitlements, mainly of pension schemes, came due, reserves were run down and the financing switched to a pay-as-you-go basis. Developments in the 1980s contributed to magnify the impact of earlier structural mistakes and brought the following general tendencies, that pointed to a potential crisis: A growth in unemployment, larger rates of labour markets and increased demand for social services, falling real salaries, declines in general government revenues, difficulties in increasing social spending and in many cases [(6)] monetary devaluation of reserves of social security agencies..

The following brief examination of a few important dimensions of social security is intended to give an idea of the implications and mutually conditioning effects social security structures have, as well as to establish a preliminary overview of the numerous aspects that reform proposals must deal with.

1. The role of the State in the provision of social security

Historically the State has been the major force behind the inception and expansion of social security in Latin America. Since current social security structures are subject now to great stresses, the function of the State has been put into question by the "Regulatory-State" approach to social security system. Will a withdrawal of public action in the provision of social security actually diminish the role of the State? A new arrangement in the functions that the State and private institutions perform in social security schemes would change more than mere ownership, since coverage and access patterns, compliance incentives and compliance restrictions may acquire new meanings. Traditionally, agreed decision structures such as tripartite institutions may also be subject to change. The institutionalization of social security under a "Welfare-State" or a "Regulatory-State" regime will bring with it a debate about new functional reassignments and illustrates the dimension of social security, that one may call its para-statal character.

2. Fiscal effects

Financial imbalances are the main reason pressing for an urgent reform of social security systems in Latin America today. Social reforms, however, are not typically cost-neutral for the State. One component is the "invisible debt" accumulated to those insured and the "Social Debt" to those who themselves have never paid social security contributions, but who have indeed suffered from "adjustment" and "fiscal austerity" following the "lost decade of the 1980s". A second cost component is associated with closing down the old system and starting up a new one. A third cost is related to the provision of social services and income-replacement to those who are unable to be insured and those who are not qualified to receive benefits under the new systems. Thus, one question posed is, if the State is getting "rid" of financial commitments when implementing a reform, then what are the net fiscal effects of a transition to a new arrangement between the State and private sector? Are there alternative forms of financing social security expenditures, especially those targeted to more vulnerable social groups than payroll taxes?

3. Social targeting

The concept of "targeting" social expenditures and contributions has been conceived as a means to reallocate resources towards the promotion and reintegration, of the most vulnerable and other poor groups into a changing social environment. An initial question is where to draw the line between social insurance (on a contributory basis) and social assistance (on a non-contributory basis)? What would constitute a better targeting of both types of social security expenditure in Latin America and where would the contributions have to come from? What have been the privileges some groups have accumulated in the past and what should be the function of social security with regard to poverty alleviation in the future? What is the role of social security in the provision of services and income: Should its main goal be the maintenance of current living standards or the provision of a basic level of income, to be supplemented by the insured through private insurance, if desired? On the contribution side, what should be the weight labour earnings are assigned in financing social security, as opposed to the use of general or specific taxes (e.g. energy taxes)? Last but not least, what have been the effects of social security contribution structures on wage costs and employment?

4. Women and social security

Formal institutions of social security are generally not the first providers in moments of need. In most cases, personal resources, community, local associations, the family and herein especially women take a large part of the burden of caring for the elderly, raising children and nursing the sick. ECLAC (1993b) reports that in general women work 12-13 hours/week more than men in Latin America, due to their twin set of responsibilities. Moreover, when women are observed to have access to labour markets (1990: Women constituted 22 per cent of the Economically Active Population (EAP) in Latin America), wage discrimination and the assignment of women to less productive activities remain issues of deep concern. Furthermore, women in Latin America are strongly represented in the most vulnerable population groups: i.e. as part of the elderly population and special circumstances of widowhood (women live longer than men; see Table 1), as migrants, and as female heads of households (between 20-40 per cent of households in Latin America) or as teen-age mothers.

A consequence of these conditions is an accumulation of gaps in the social security contribution periods of women and, as entitlement conditions tend to become stricter in the future, one should ask if women deserve special treatment in recognition for their direct contributions to the care of the sick, young and elderly [(7)] to avoid an unintended exclusion from social security and exposure to the danger of poverty.

5. Fully-funded versus pay-as-you-go systems

A major argument advanced against pay-as-you-go schemes has been that they allegedly dissave society's resources and that fully-funded methods could contribute to a higher aggregate saving rate and, consequently, to higher investment levels. The considerable amount of resources that have already been redirected towards funded schemes raises some doubts: Is funded social security an appropriate way to increase aggregate saving in a society? Has social security in fact attained this goal in Latin America where this argument was presented by its reformers?

A first point is to recognize that social expenditure can only be financed out of current national income. Thus, the problem of sharing national income between those who are active and those who have retired (in the case of pensions) always remains, no income can really be shifted from the past to the present nor to the future.

A second point that remains ambiguous is whether the saving effects, which fully-funded schemes are said to have, in fact occur. Here one should ask whether mandatory pension saving crowds out other personal saving. One also wonders whether a myth of a "savings fund" as a prerequisite of investment utterly shattered by Keynes is about to be re-established. What have been the initial results achieved (or not achieved) in Latin American reforms?

Thirdly, one should consider the fact that mature funded schemes acquire the same characteristic as a pay-as-you-go system, becoming an economic equivalent. The differences that remain are matters of convenience and administration.

Finally, the funds acquire considerable power with large accumulated resources, especially within financial structures historically driven by national "grupos financieros" and foreign conglomerates, as has been the case in Latin America. What then are the rules warranting a socially responsible management of funds?

Chapter 2: Reform case studies

1. Chile: A capitalized pension scheme and the universal minimum assistance promise

1.1 Situation before reform

Chile was among the "pioneers" of social security in Latin America; the inception of its modern scheme was in the 1920s, when the first programme for railroad workers was created. A piecemeal, but steady evolution resulted in an institutionally fragmented ensemble providing for almost all risks and covering around 75 per cent of EAP (1970). Some remarkable inequalities characterized the system: Average pension values of public employees were two times higher than those in the private sector and almost 7 times above the general average. There existed early-retirement schemes, that allowed retirement after only thirty years of contributions. Moreover, extremely favourably indexed pensions (the "perseguidoras pensions") were accessible to a restricted group, which included the military.(8)

The adverse trend in dependency ratios (1960=10.8 contributors to 1 pensioner; 1970=4.4:1) and the 15 to 20 per cent (1965-75) supplementary resources that the Chilean social security needed from the public budget were other negative aspects(9). In 1971, total social security expenditure reached a record peak of 17.5 per cent of GDP(10). Despite several attempts in the past, including one under President Eduardo Frei in the 1960s, intentions of improvement failed to lead to a reform.

After the military coup, the main sources of inequalities (early-retirement, "perseguidoras pensions") were abolished, except for the armed forces and the police. Retirement ages were raised and set nationwide at 65 years for men and 60 for women, a unification process of the various agencies began under the Pension Normalization Office and contribution rates were reduced by abolishing the employers' contribution with the intent to lower the cost of labour(11). Witte (1995) argues that it was the military government which exacerbated the social security crisis in the 1970s by means of this last measure.

1.2 The switch to a fully-funded pension system: Reform and comments

In 1980, Decree-Law No. 3500 introduced a new private-based fully-funded pension system, which was to substitute the public pay-as-you-go programmes in the long run. The latter were not closed immediately, but would be gradually phased out as its pensioners died and the currently insured switched to the fully-funded programme, while new entrants to the labour market were mandatorily affiliated to the private scheme.

The role of the State was redefined under the key-words "subsidiarity" and "regulative function". The State was to leave the economy to the private actors and assume only a subsidiary role in regulating and supervising banks, insurance companies, etc., and in "targeting" its social expenditure on the "absolutely poor". On the other hand, the Gini income distribution coefficient increased from 0.50 to 0.55 between 1970 and 1984(12) and constituted a striking indicator of the massive impoverishment that took place in Chile. In the 1990s the new democratic government decided to give greater emphasis to the poverty "targeting" aspect of the social reforms initiated by the military regime.

The central elements in the new system are the AFPs - private enterprises which each manage one pension fund and provide pension rights to its insured(13). The whole system has a controlling supervisory body (SAFP), subordinated to the Ministry of Labour. Further duties of the State comprise: The orderly closing down of the former system, including the assumption of its financial burden; the provision of regulations and guarantees to endow the new programme with trustworthiness through security standards for the insured; and the promise of "assistential pensions" financed out of general revenue to those who might fail to acquire the right to a certain minimum level pension, subject to the test of neediness.

The private pension scheme is compulsory for all salaried employees. Self-employed can join on an optional basis. Employees pay a 10 per cent contribution over their gross wages to an AFP, plus approximately another 3 per cent to a life-insurance company elected by the AFP, thereby covering also against disability-survivorship risks. Voluntary additional contributions are also possible within a ceiling and enjoy preferential taxation. Another 7 per cent must be paid for health insurance. The sum of contributions owed under the new regime was significantly lower (by around 7 per cent) than the ones fixed for the old programme(14). Employers are exempt from mandatory contributions to the new system, but upon the introduction of the AFPs, they were required to raise wages by the amount they would have had to contribute, were the employee still under the former scheme. The resulting net wage increase was an incentive for the insured to change to an AFP. Other incentives to switch were that entitlement conditions in the old system were toughened and "recognition bonds" would be issued by the government, that represented the insured person's rights accumulated while associated with the former scheme. Recognition bonds earn a real interest of 4 per cent/year and would become due at the moment its bearer retires(15).

In the first year (1981), 39 per cent of the EAP switched from the public to the private pension scheme and this number has been growing constantly, until reaching close to 90 per cent coverage of EAP by May 1993(16). Less than 10 per cent of EAP were still contributing to the old scheme. However, at that time, only 2.77 million (that is 61 per cent) of the currently 4.54 million affiliated were contributing regularly. Mesa-Lago (1993) reports particularly great coverage weaknesses among autonomous (i.e. self-employed) workers. Thus, the real coverage rate is now lower than it was under the old system. The reason why compliance has been low is not at all clear. Diamond and Valdés-Prieto refer to the high rotation in the labour market. Witte (1995) mentions the possibility of employers delaying or withholding contributions collected from their employees and also that for a majority of autonomous workers (mostly in the informal sector and among the less wealthy) the need to contribute completely from individual resources without a salary adjustment might have made switching too costly. Furthermore, competition between the AFPs makes any sanction for non-complying clients highly improbable.

Retirement is set at the age of 65 for men/60 for women with the right to a pension, being open if the condition of years is fulfilled. However, it may open earlier, if accumulated funds satisfy certain legal standards.

Affiliates of the private scheme can change their savings account from one AFP to another up to 4 times a year and, in fact, 25 per cent of the accountholders have exercised this right at least once a year until 1993(17). One important feature with which AFPs are supposed to compete are the fees they charge their affiliates for services of collecting contributions, administering and informing about the insured's situation, as well as payout amounts upon retirement. Fees are currently twofold: One flat amount for the maintenance of the account and another one proportional to the contributions deposited. Since 1983, total fees have sunk from 3.6 per cent (1983) to 3.1 per cent (1991)(18). A critical point has been the regressive effect that a fixed charge has on the lower income brackets among the insured: For affiliates with a contribution-salary of US$ 250 in 1991, the return over the period of 1981-91 was almost one-quarter lower than that for a taxable income of US$ 1,500(19).

AFPs also differ by their return on investment; however, a strong regulation was created to limit risky portfolios, distribute the expected development effect among the various investment instruments and to avoid losses for the insured. On the other hand, these boundaries have been extended, as the Chilean banking system and financial markets have evolved. Currently, AFPs are not allowed to hold more than 45 per cent of assets in governmental instruments and 30 per cent in domestic equities. In 1995, the permitted share of foreign instruments has been raised to 10 per cent.[(20)]

Rates of returns of AFPs have been very high, reaching an average of 13.6 per cent in the period of 1981-93[(21)]. However, Chilean and international experts reckon that these return levels will not be sustained in the long run, when typical international rates are more likely to prevail. Recent forecasts show a "reasonable maximum" of 4 per cent/year (Ruiz-Tagle, 1994) or a more optimistic 5.5 to 6.5 per cent (Diamond and Valdés-Prieto, 1994). Ruiz-Tagle (1994) thinks that investment portfolios may become riskier, since accumulated funds are forecasted to reach 80 per cent of GNP in 1999 (situation in Dec. 1993: Around 40 per cent of GNP) and the supply of safe high yielding investment instruments tends to run out.

Retirement benefits can be paid out in three different variants. First, at the appropriate age, the insured person is paid a lump-sum equalling his or her savings in the AFP from which an annuity (monthly pension) at a life-insurance company (insurance broker's fee: Around 3.5 to 4 per cent of total insured value[(22)]) must be purchased; the monthly pension is ensured until death. The second mode is a phased withdrawal, where the AFP maintains the affiliate's account and pays out a monthly sum until depletion. This version has risks for the insured, should he or she "survive" longer than his/her account can guarantee payment for. A third possibility is the combination of both.[(23)] The State guarantees pensioners against insurance company or AFP bankruptcy.

This essentially private system is complemented with a "targeted" social assistance component by the State, the so-called "assistance pensions", amounting to around 10.5 per cent of average national wages in 1990. Besides the capitalization in private pension funds, such social assistance pensions for needy elderly persons to which, at least in principle, everybody is entitled, constitute the main social innovation of the "Chilean Model". However, first experience also shows how shaky the foundations of the Chilean type of a "targeting" Welfare-State still remain. First of all, for fiscal reasons the total number of persons to be covered was limited rather arbitrarily to 300,000 at the end of the 1980s, with a large non-satisfied demand by legally eligible persons[(24)]. Secondly, the real value of those pensions fell sharply between 1987-89, since they are not regularly indexed. In June 1990, however, there was a nominal value increase of 82 per cent under the Aylwin government[(25)], showing how susceptible such transfers are to swings in the political pendulum.

The second "targeting" feature is the minimum pension guarantee: If any AFP-insured person fulfils 20 years of contributions but does not meet the legislated minimum pension value, a top-up pension is paid out of general revenue (as assistance pensions are). This leaves public financial commitments open-ended and unforeseeable[(26)].

Among the most important arguments in favour of this reform was that pensions under the AFPs would be higher than in the past. De facto, new pensions granted are around 43 per cent above the old ones. Several factors, however, have been at work and a direct comparison is problematic. After all, the fiscal reason for introducing the new system was that the accumulated pension claims of the insured were too high to be honoured by the State. So the Chilean State went partially bankrupt, writing off the "invisible" claims of its pensioners while continuing to serve its external and internal "visible" debt to bondholders and others - exactly the opposite to the monetary reforms after the First and Second World Wars in Europe, particularly Germany, where monetary systems were rebuilt by reducing visible debts and leaving the invisible claims of the pensioners, veterans and war victims intact. Because the new fully-funded scheme is only at its beginning and still far from maturity[(27)], the incentive structure of the minimum pension guarantee has not yet come in full play. The already high contribution failure rate leads one to expect that the minimum pension guarantee will be claimed extensively in the future. Ruiz-Tagle (1994) reports that in Dec. 1992 only 27.9 per cent of those aged over 40 among AFP affiliates (presumably with 10 years or more of affiliation) had accumulated savings in excess of US$ 5,000, a sum that would hardly achieve a minimum pension without a topping-up. Thus all projections are highly conjectural.

The fiscal effects are also not yet clear. The goal of the reform was to release the State from further deficits accrued under the old system. On the other hand, phasing it out involved not only drastic curtailments in the claims of present and future pensioners under the old system, but bearing a huge accumulated debt as well. Arrau (1992; see Table 7) projects that the total fiscal deficit associated with the reform and the issuance of recognition bonds will remain at a very high level (over 4 per cent of GNP until the year 2000, falling down to 1.5 per cent in 2015); the way chosen to finance this deficit was to issue debt bonds - to be held mainly by the AFPs, thus closing the circle between the young and the elderly. This forecast does not yet include the likelihood of higher public expenses caused by a larger than anticipated minimum pension guarantee demand, much less a further expansion of the "assistance pensions". One can conclude that the fiscal savings of the Chilean State are not as clear as expected by the reformers.

Women are among the main losers of the Chilean pension reform[(28)]. The individual contribution failure rate of female affiliates to an AFP in May 1993 was at 55.5 per cent (compared to a general failure average: 39.0 per cent of all affiliates[(29)]). This can be explained by the argument that during the deterioration of the social environment in the 1980s, women were first hit by labour market problems (resulting in more "contribution gaps") and increased duties within the family arrangements. Another aspect is that their taxable monetary incomes are around 25 per cent lower than those of men. Furthermore, their average life expectancy at time of retirement is higher than the one for men (19.4 years against 13.2 for men in the early 1980s) (Mesa-Lago, 1991a), resulting in lower pensions.

Finally, reform was expected to increase national saving, develop capital markets, and thereby stimulate investment. It seems that indeed, its foremost successful influence was towards the deepening, institutionalization and specialization of the capital markets[(30)]. Diamond and Valdés-Prieto (1994) argue that most of the recent capital market developments would have probably occurred also without the contribution of pension funds, due to the general opening of the Chilean economy since the 1980s. These authors also doubt on the importance of the role pension funds might have played on capital market price trends in the 1980s. On the one hand, it was common that legislative changes concerning the AFPs' portfolio composition induced immediate speculative rises in prices and one can suspect that the funds' invested volume (35.4 per cent of aggregate financial assets in June 1992), might have contributed to artificial price booms in the Chilean exchange stock markets. On the other hand, price increases were often so high, that various AFPs surpassed the limits set by the Supervisory Body on the share of individual instruments in their portfolios. Prices for those financial assets, in which AFPs were forbidden to invest or had already reached their maximum investment share, continued to increase at the same pace (so some AFPs were even forced to sell stocks in order to maintain their allowed portfolio composition)[(31)].

A final doubt concerns the effect on investment and national aggregate saving. Arrau (1992) systematizes Chilean aggregate saving data for the period 1980-91 showing that while pension fund saving increased slowly from 0.0 (1981) to 3.3 per cent of GNP (1991), government saving fell sharply during the early and mid-1980s and returned to a lower level than before by the end of the decade. Total national saving also dropped during the 1980s and returned in 1989-91 to a somewhat lower level than at the start of the social security reform. In conclusion, to date there is no evidence to prove a positive effect of pension reform on national aggregate saving in Chile. Rather the standard Keynesian argument that investment and consumption are the autonomous variables leaving aggregate saving ("S") as a residual, seems to be reaffirmed.

2. The reform in Peru: Following the Chilean model

2.1 Arrangements prior to reform

The origins of the formal Peruvian social security system date back to the period 1936-60, when the fundamental legislation was passed. Mesa-Lago (1991) classifies it among the intermediate countries with a relatively unified system. Its centrepiece is the Peruvian Institute of Social Security (IPSS), which integrated all existing programmes (except that of the armed forces) starting in 1980. Coverage figures for 1985 showed that mainly salaried urban and public sector employees were covered, totalling 39.1 per cent of EAP or around one-fifth of the total population.

Benefit entitlement conditions in 1985 were as follows: One could retire at age 60/55 (male/female), given a minimum of 15/13 years of contributions. The resulting pension ranged between 50 and 80 per cent of the average salary of the 3 to 5 best years within the last 5 years. Sickness-maternity benefits were also among the most liberal in a Latin American comparison[32].

The revenue structure of the Peruvian social security system depended primarily on a 22 per cent payroll tax, divided between employers (16 per cent) and employees (6 per cent of which 3 per cent for the pension programme). The financing method adopted by law was the "scaled premium" system (pay-as-you-go with accumulation of reserves for a mid-term period, followed by an actuarial reassessment of the contribution "premium" for the following term). During the 1980s economic crisis, many indicators plunged: Real salaries dropped, unemployment rose, evasion of social security contributions among private employers was estimated at 33 per cent, high inflation combined with interest and exchange rate manipulation exhausted IPSS reserves (governmental debt held by social security institutions devalued), social security deficits developed in 1982-84 and 1987-88. Mesa-Lago (1994) includes the further problems: Low real value of pensions, lack of continuous actuarial evaluation of all programmes, bureaucratization and high administration costs. Summing up, the IPSS saw its worst crisis in history and there was certainly need for reform by the end of the 1980s.

2.2 Pension programme reform

Although pensions were historically only a relatively small part of the Peruvian social security system (pension programme expenditure totalled only 34.1 per cent of the benefit expenditure in Peru in 1983, while 58.7 per cent went to the sickness-maternity programme, the latter subsidized with revenue generated from the pension programme), Peru decided in 1991 to introduce a private pension system. Mesa-Lago (1994), as well as the Lima-based journal Análisis Laboral (1994), point out that public debate, to the extent that it existed, centred around the type of system (public vs. private vs. mixed) desired rather than on urgently needed steps to reform and consolidate the benefits of those insured with the IPSS and the whole social security programme itself.

In December 1992, under the suspension of constitutional rights, the Peruvian Government issued Decree No. 25897/1992, which established June 1993 as the launching date for a private pension system (SPP), inspired by the Chilean model. However, there are some important differences:

(1) Legally, the old system continues to exist but the vesting period was raised to 20 contribution years (for both men and women); social security affiliates have the choice between the IPSS and the AFPs;

(2) switching from an AFP to the IPSS was allowed only through Dec. 1994; thus, after that time,

the only way to enter the IPSS was at the precise start of one's working life;

(3) recognition bonds would be issued under tougher conditions than in Chile[33]:

* the insured must have been affiliated with the IPSS on Dec. 6th, 1992;

* the insured must have contributed during the 6 months immediately prior to requesting bond-issue;

* and, most important, the insured must have contributed to the IPSS for at least 4 years between Dec. 1982 and Dec. 1992.

This means that those who had contributed before 1982 but did not have four contributing years afterwards or those who began contributions in Jan. 1990 or later had no right to a recognition bond. One should remember that the 1980s were a decade of crisis (poverty and extreme poverty grew to hitherto unknown levels between 1985 and 1991[34]) and that the general trend in Peru was towards growth of informal employment or even subsistence production;

(5) the recognition bond had a ceiling of 60,000 soles (around US$ 40,000); it is inflation-indexed but yields no real interest;

(6) contributions assessed on the salary of the employee: Besides a 10 per cent contribution to the old-age pension fund and a non-specified contribution for disability-survivorship insurance, there is a 1 per cent solidarity contribution to finance assistential pensions to the old non-entitled and those disabled over age 18;

(7) there is no minimum pension guarantee;

(8) AFP portfolio composition rules allowed a maximum of 60 per cent in government securities (Chile: 45 per cent) and 5 per cent in foreign instruments (Chile: Since 1992 3 per cent, beginning 1995 10 per cent)[35].

Half a year after its start, there were 8 AFPs functioning with roughly 650,000 affiliates (Table 9). By February 1995, this number had increased to around 965,000[36]. Three-quarters of AFP insured were between the ages of 20-40 years. Even if the age structure of the Peruvian population is still very young, it appears that the older cohorts of the insured population are under-represented among AFP affiliates. The main reasons for young people to want to join the AFPs are the possibility of escaping from the financial crisis of the IPSS, the perspective of better pensions and possibly the pressure of employers, who pay no contribution under the private pension scheme (however, with the switch of an employee to an AFP, employers do have to raise the salary by 13.5 per cent, the amount of the employee's old-age, disability and survivorship insurance contribution; in return, they become exempted from any other mandatory contribution to the pension system). Reasons to remain in IPSS for the older employees are the unfavourable conditions of the recognition bonds, the more liberal entitlement conditions (retirement age 60/55 years for males/females instead of 65/60 in SPP) and a lower employee contribution.

The reformed system faced serious problems during its initial year, mainly due to the financial shortcomings from the governmental side, but also administrative ones. The government budget had no provision for the salary increase owed to state employees who wanted to change to the SPP, for example, resulting in a temporary prohibition of affiliation for public employees in the AFPs. According to Análisis Laboral (1994), another problem was that until Jan. 1994 no recognition bond had been issued, because of incomplete records of contributions made at the IPSS and the virtual impossibility on the side of Peruvian workers to fully document their own working lives. The longer affiliation period and the new tougher conditions required with regard to documented formal periods of salaried income hit women relatively hard. The issue of an "automatic recognition bond" under "adverse conditions"[(37)] and the possibility of postponing the recognition of State liabilities towards future pensioners did not increase confidence in either the new, or the old State system. Furthermore, a Pension Normalization Office, foreseen by law and empowered to take over the IPSS pension administration, was crippled by a lack of budget for 1994, and is supposed to start its activity only in 1996[(38)]; it was also not known where the US$ 35 million needed to pay the 300,000 pensions owed under the IPSS rules[(39)] should come from. On the other hand, the IPSS is already said to run a 50 per cent current deficit in its total budget[(40)]. The way out of this financial crisis, namely to issue State bonds to the AFPs in order to pay the IPSS pensions which would fulfil the generation contract again, encounters a serious problem: At the beginning of 1995, it was reported that 50 per cent of AFP affiliates failed to contribute on a regular basis[(41)]. The shrinking revenues from contributions are thus endangering the already low and reduced level of the IPSS pensions.

2.3 Comment

It appears that the Peruvian reformers were primarily moved by the desire to alleviate the crisis of the public finances (the recognition bond conditions and the absence of minimum pension guarantees will surely make this reform considerably less expensive for the State than the Chilean one) and simultaneously develop the Peruvian capital market. Whether the latter aim will be achieved remains to be seen and requires a strong and continuous effort to modernize and enlarge the rather thin financial market existing up to now. The portfolio composition of AFPs (Table 10), in 1993, shows that investments were concentrated in government bonds and fixed-term deposits. Privatization of public enterprises do not seem to be used to improve capital markets nor has the introduction of the private pension system been tied to the State enterprise privatization process (as it was the case in Chile). Furthermore, if one believes the AFP representatives' forecast of accumulated assets of US$ 25 billion by the year 2005[(42)], the question arises where these amounts could and should be invested without being exposed to high risks or being involved in speculation in either real estate or stocks. The overall development strategy of the Peruvian State has been to simply open markets without bringing economic agents together by means of some form of sectoral policies.

Attacking the historical coverage weakness of the IPSS has not been a goal of the reform, and it is not very probable that coverage will increase. One large part of the non-covered labour force under the public social security system has been that of workers in agricultural sector, whose very low per capita income makes their cost/benefit assessment unattractive for private AFPs even in the longer run. If the tendency of a contribution failure rate of 50 per cent continues, even the promise of decent pensions in the future becomes doubtful for the urban population in covered employment. The 1 per cent solidarity contribution, whose elimination has been demanded by the AFPs because it increases affiliation costs[(43)] and which, on the other side, has already been suggested to be used to fill the IPSS pension hole[(44)], is certainly much too small a blanket to cover all the elderly and the disabled in need.

3. Reform in Colombia: Strengths and weaknesses of a parallel model

3.1 Situation before reform

Modern institutionalized social security was first established in Colombia in the early decades of this century, but the first nationwide institution for public employees was founded only in the 1940s. Since then, social security has evolved along the lines already described for the other countries, putting Colombia among the "intermediate" group. An extended public pension programme for private employees started in 1967 under the ICSS, renamed ISS (Social Security Institute) in 1977. During the early 1990s, the system was fragmented and stratified with over 1,000 institutions in existence and public employee programmes offering several advantages in comparison with the ISS, which concentrated on private sector affiliates. Colombian social security relied on a partial capitalization method - accumulating bonds of the treasury or the national industrial development bank and of the public holding company IFI (Instituto de Fomento Industrial) - and on the Bismarckian insurance principle, almost solely focusing on wage and salaried employees (self-employed affiliates are extremely under-represented).

Problems of the old system included, on the revenue side, a very low contribution rate(45), as well as low coverage (1993: 28.6 per cent of EAP(46)) poor investment returns and extensive contribution gaps in affiliates' records. The gaps in the records were due to several reasons: Employers withholding contributions or paying them late, State failure to pay its share of contributions and labour market characteristics in Colombia - the average Colombian worker's career path tends to move towards the informal sector in the mid-life period(47). On the expenditure side, eligibility for normal retirement began at age 60/55 (men/women) at the ISS and 55/50 at Cajanal (the largest public employee institute). The pension would be calculated over the last 2 or 3 years of a minimum contribution period of 10 years (raising moral hazard problems). Average pensions at the ISS were around 1.3 times the minimum wage, while in the public employee programmes the average was between two and up to five times the minimum wage(48). Other factors contributing to the crisis were adverse demographic developments (dependency ratio fell and life expectancy increased), corruption and inefficient administration(49).

3.2 The reform in 1993: From the Chilean model to a parallel system

The new national Constitution of 1991 reinforced the Constitution's social mandate to the State and included an explicit article proclaiming that social security is a right of every citizen. Furthermore, the State was charged to provide the institutional mechanisms and regulate private suppliers of social security services. The principles that are to guide public policy are: Solidarity, universality and efficiency(50). At the end of 1991, the Government proposed to Congress a Chilean model project, which found its supporters in the financial community and its opposition mainly in the ISS, as well as in the trade unions, and in the National Accountancy Court (Contraloría General de la República) establishments, that advocated the reform of the existing system. When the ISS directorate resigned spectacularly in 1992, discussion had already spread to Congress and, finally, in 1993, a compromise model was achieved. Under Law 100 (1993) a parallel model (reforming public schemes and implementing private fully-funded programmes) would begin in April 1994.

According to the reform law, social security remains mandatory for all wage and salaried workers and employees. Self-employed workers can join voluntarily. The public scheme, which would adopt a pay-as-you-go method of financing, had the following characteristics(51):

(1) for men/women aged over 40/35 at the moment of the reform, nothing would be modified under the public schemes, except for changes in contribution rates;

(2) contribution rates were raised to 12.5 per cent of the payroll (1995) and 13.5 (1996), including old age-disability-survivor insurance. Employers pay 3/4 and employees 1/4 of the contribution. There is a ceiling of 20 times the minimum wage for the contribution basis;

(3) all affiliates earning above four times the minimum wage must pay an additional 1 per cent to a solidarity fund; this fund also receives contributions from the State and has the goal to expand coverage;

(4) minimum retirement age will be raised by 2 years for both men and women in the year 2013, should life expectancy figures point to this need;

(5) entitlement conditions: Vesting period is raised to 20 years (formerly: 10 years). The old-age pension payable is calculated as 65 per cent of the contribution basis of the last 10 years, plus additional percentages for time worked after entitlement begins, up to a maximum replacement rate of 85 per cent;

(6) other public employee institutions must adapt to the ISS rules and will be absorbed starting in 1995 by a National Public Pension Fund Administration. Exceptions are made for teachers, military, oil industry employees and congressional pension schemes;[(52)]

(7) minimum pension guarantee: The State guarantees a minimum pension of 1 time the minimum wage, given 20 years of contributions made to the ISS;

(8) the public scheme is coordinated through a National Council, whose directorate is based on a tripartite organization, including also representatives of the retired;

(9) outside the social insurance scheme, but under Constitutional mandate, the State provides a 0.5 minimum wage "public assistance pension" for the aged very poor and aged Indian population;

(10) the State assumes the costs for those pensions under the former public scheme that existed at the moment of the reform and for the amount exceeding current public agencies' reserves.

A private alternative system was also implemented, almost identical to the Chilean one. Its features are:

(1) the SAFPs (pension fund administration societies) are fully-funded and every person who so desires can opt out of the ISS and affiliate with a SAFP. Switching to another SAFP is possible and returning to the ISS is allowed after a 3 year period;

(2) contribution: The same as in the ISS. Additional voluntary contributions are possible;

(3) solidarity-contribution: The same as in the ISS;

(4) retirement age: No age was established; it is possible to retire when accumulated funds permit a pension equalling 110 per cent of the minimum wage;

(5) pension levels will depend on accumulated funds and future interest rates. These run at about 4 per cent between 1987 and 1992[(53)];

(6) SAFPs are regulated and supervised by the Bank Supervision Authority. SAFPs must guarantee a minimum positive return rate, established on the basis of a capital market index calculated ex-post by the Bank Supervision Authority[(54)]; if a SAFP fails to achieve the minimum return, it is mandated to cover the shortcoming out of its own resources;

(7) the State supplements pensions up to the minimum wage, if this level is not achieved at age 62/60 (men/women) and after 23 years of contributions have been made;

(8) the insured have 2 non-voting representatives in the advisory board of each SAFP;

(9) a ceiling on the maximum equity of the SAFP (10 times the minimum foreseen capital) was established, which is thought to set limits to market concentration (as occurring currently in Chile and Peru);

(10) "Pension bonds" recognize the public debt towards former affiliates, paying the average interest rate. Since there also existed supplementary private pension funds before the reform, these too issue "pension bonds", if the affiliate wants to quit and capitalize his accumulated pension rights into a SAFP;

(11) in the case an affiliate returns to the ISS, accumulated funds are recalculated into "contribution weeks" to construct the affiliate's contribution history.

3.3 Results and comments

It is too soon to come to a definitive judgement about the success or failure of this reform. However, a few tendencies can already be identified for a preliminary evaluation.

Witte (1995) reports that the attractiveness of private funds appears to be rather low, since only 25 per cent of Colombians earn more than two times the minimum wage, and interest rates are not expected to be as high as in Chile. This means that the ISS replacement rates (65 to 85 per cent of the contribution basis) will not be easy to attain in private funds. These should be only interesting for those affluent individuals, who can achieve a pension right in a relatively short time or for those who expect to have a very long formal activity period (40 years or more), because in the ISS scheme the replacement rate does not increase after 28 years of contribution. Most Colombians do not meet these criteria. However, as of Dec. 31st 1994, about 1 million persons were affiliated with a SAFP (85 per cent of them aged under 35 years and 80 per cent of them earning less than 2 times the minimum wage). The ISS affiliation figures at the same time remained slightly above 3.5 million persons.[(55)]

The financial situation of the public schemes will improve, since increases in contribution rates, unification (hope for greater administrative efficiency) and a higher vesting period are expected (but only in the long run). Kleinjans (1995) emphasizes that these changes are technical ones, unrelated to the issue of privatization.

The new schemes, that continue to be based on a Bismarckian pattern, will probably not contribute to enlarge population coverage significantly. Moreover, the already mentioned working life-cycle in Colombia results in an average contribution period in covered employment of only about 50 per cent of one's entire active economic life. Since this working life-cycle is expected to continue and informality probably will remain high or even increase[(56)], compliance levels in the public scheme should not be expected to improve, unless voluntary contributions become attractive (which is rather improbable for any compulsory system). In the private scheme a somewhat higher compliance might be realized, but since there are no data available, this assertion must remain a conjecture. Until now, private funds have established themselves only in the largest urban centers of Colombia, which might indicate rather restricted coverage also in the future.

Witte (1995) expects the minimum pension guarantee to become the rule rather than the exception. On the one hand, this would add further costs on the State; on the other hand, several calculations for pension values under the private scheme[(57)] show that an adequate replacement rate and even a minimum pension for the average Colombian worker can only be achieved if unrealistic assumptions concerning interest rates, contribution compliance and/or contribution rates are included. Thus an incentive problem could emerge: If you receive a minimum pension via the guarantee of the State, your own contribution can be minimized, since even a relatively large effort would not result in a significantly higher pension.

The Colombian reform compromise, with its minimum pension guarantee and its public assistance pension supplementing the social insurance system, has strong elements targeted towards alleviating poverty, but the fiscal burden will probably be so high, that the "Estado Social de Derecho" of the 1991 Constitution will remain a long-run hope rather than immanent reality.

The fiscal costs which the State incurs are very difficult to predict. Various studies for the former "Chilean model"-project arrived at different results, ranging from "fiscal suicide" to "beneficial consequences"[(58)]. In the current model, they will depend on the number of "pension bonds" issued, future interest rates, the minimum pension guarantee realization, the current deficit of the ISS and the contributions made by the State as an employer (which have also increased after the reform), and on the decision of the workers and employees to prefer private to public institutions or vice versa.

Women seem to be among the losers of the reform here, too. They retire earlier, have longer life expectancy[(59)] and more contributory gaps, resulting in an even lower probability of fulfilling the entitlement conditions. Other losers are those not covered, since the State's liabilities vis-à-vis the insured are very large and will be financed to some extent out of general revenue (the governmental structure of revenues depends quite heavily upon indirect taxes). Furthermore, future generations will be mortgaged through increased public debt. The maintenance of special regimes also does not contribute to increasing progressivity. On the other hand, the solidarity fund and social assistance pensions are indeed redistributive elements, even if doubts are justified about the sufficiency of their volumes. As a concluding remark, it seems that a pension reform including privatization (even partial), a high public financial commitment and low coverage tends to be regressive as a whole. With a parallel structure, total administrative costs are likely to increase, particularly when compared with a reformed unitary public system.

The financial sector in Colombia is oligopolized with the dominance of the "grupos financieros". Chilean AFPs and international financial institutions are establishing joint-ventures with national groups to run the SAFPs[(60)], leaving the alleviation of structural poverty, much less "empowerment" of the poor, far from their concerns - but still managing the compulsory savings of wage and salary employees.

In a final preliminary evaluation, it does not appear as if a mixed scheme, in which private and public institutions run parallel programmes, is a preferable solution for Latin American countries, that are characterized by high income concentration, poverty, regional imbalances and a large "social debt" accumulated as a result of the development model of the last decades. The principal point is that a parallel model allows adverse selection - the poor (those who cost) remaining inside the public schemes and the better-off opting for the private sector, but nonetheless relying on the State's guarantees.

Different from the case of non-democratic 1981 Chile, the Colombian reform design was the result of compromise under mutual pressure from the actors involved - on the one side, the ISS and public institutions and the "social front" defending a publicly-run scheme, on the other side, the financial institutions and those arguing that privatization would bring greater efficiency and make pensions safer, contributing to larger aggregate saving and investment. Witte (1995) writes that Colombia is going through a learning process, and it appears to be an open question which of the parallel systems will prevail in the evolutionary dynamics or whether both will eventually converge in the future.

4. A briefing on Costa Rica's experience

The present Costarican Social Security Institution (CCSS) was preceded by the approval of the Workmen's Compensation Act in 1924 and the creation of the Ministry of Labour, the Emergency Fund and the Insurance Bank (INS) in 1928. The Bank, in 1941, was transformed into the CCSS and in 1943 social rights became a part of the Constitution. In 1961, the Constitution was further amended in order to introduce the State's obligation to provide for universal health care benefits after a transition period of ten years. Although belonging to the "intermediate countries", Costa Rica, by means of this strong political commitment, reached almost universal health care coverage by the end of the 1970s. Starting from 38.4 per cent of the total population (1970), coverage reached 84.4 per cent in 1979 and maintained this standard until 1989 (85.4 per cent)[(61)]. According to official sources, health care (contributive) coverage was 86.2 per cent in 1994.[(62)] The non-covered population is said to be partially the most affluent, who can afford to pay for protection out of pocket. This enables one to speak of "virtual universal coverage". It is important, though, to note that in real terms public health care benefits have been persistently reduced. That is why the quality of services has been declining over time, shifting the wealthy part of the population to the (very limited) private health care sector. Also, the coverage figures refer to the national domestic population only, excluding aliens, especially illegal immigrants who, according to unofficial estimates vary between 0.3 and 0.5 million people.

Universalization relies principally on extension and targeting of public health and pension assistance mechanisms to the indigent and rural populations. Due to the privileged treatment accorded in the Constitution, health care coverage has to be strictly separated from old-age benefit schemes. Official pension coverage figures draw the following picture for 1994: 49.3 per cent (in 1988: 47.3 per cent) of the economically active population, 66.6 per cent of salaried employees and 5.2 per cent of the self-employed were insured. The contrast between official figures and reality, though, seems to be considerably high in certain respects: e.g., due to huge delays in file processing (of reportedly up to 8 years), stemming from very limited administrative resources, many public servants die before they obtain a pension.

Pension programme coverage is basically payroll-tax financed[(63)]. Besides social insurance pensions, there is further coverage by the social assistance pension scheme (subject to a means test, financed out of a 5 per cent payroll tax paid by employers and partly from a sales tax). Outside the CCSS pension programme, there were 19 different pension schemes, mainly paying benefits to civil servants (42 per cent of total pension costs to 20 per cent of pensioners, participating in these special programmes)[(64)].

The pension system in Costa Rica was reformed stepwise during the 1980s and early 1990s[(65)]:

(1) Minimum early-retirement ages were raised by 5.5 years to 62.5/60.5 (male/female);

(2) the payroll contribution rate (currently 7 per cent for both employer and employee) was left flexible in order to allow for future adjustments, if actuarially needed;

(3) early-retirement disincentives were created by scaling the required contributions in unfavourable proportions (the earlier the retirement desired, the higher the contribution needed);

(4) in 1992, special pension programmes outside CCSS were closed to new entrants. All new civil servants had to join CCSS under general conditions;

(5) evasion was more strictly repressed and outstanding debts (unpaid contributions) to CCSS rescheduled and enforced.

Costa Rica's public health programme, which has a large merit share in social security coverage achievements, is focused mainly on the urban poor, the rural sector and on maternity and child health care. Integration and mutual complementation between the health programmes and facilities of both the Ministry of Health and the CCSS has been taking place since the 1980s. Furthermore, coverage has been extended by agreements with cooperatives and other rural organizations. Financing health programmes for non-salaried and indigents is based on solidarity transfers from the payroll contribution tax, lottery and general public revenues[(66)].

The financial structure supporting this framework is somewhat precarious. Firstly, the system is strongly dependent on state revenues and, as a consequence, on national economic performance and annual budgetary allocations. Real average value of public assistance cash benefits fell sharply during the 1980s (by 60 per cent); within the pension scheme, the CCSS had to make use of part of its accumulated reserves in 1987-89. Reaction to this situation came by the pension programme reforms on the one hand and, on the other hand, health programmes were increasingly contracted-out and decentralized, together with various other measures to reduce costs and improve efficiency [(67)].

The preliminary conclusions that can be drawn from Costa Rica's experience are the following:

(1) There must exist a strong political commitment to social security and public health in order to reach high coverage and standards with relatively few resources;

(2) different revenue sources should be tapped without relying solely on payroll taxes to achieve universal coverage;

(3) the targeting of health and assistance programmes appears to have contributed to Costa Rica's high social and health standards (among the best in Latin America).

5. Brazil: Fulfilling the Welfare-State dream?

5.1 Origins and current structure of "Previdência"

Brazil has the largest Latin American social security system and is classified by Mesa-Lago (1991) among the "pioneer countries". The origins of Brazilian modern formal social security are commonly dated back to the 1920s, when railroad employees were first covered, followed by a process of concentric enlargements to include further professional groups. The latest, and in absolute numbers most significant, extension of coverage was achieved in the 1970s through the inclusion of rural workers (by means of a then still separate regime called PRORURAL/FUNRURAL) and domestic employees. Statistical EAP coverage indicator jumped from 27.0 per cent in 1970 to 87.0 per cent in 1980; whole population coverage was declared as high as 96.3 per cent in 1980, by far the highest figure in Latin America[(68)], if not in the world. During the 1980s, coverage apparently diminished, at least for the urban sector. A recent study by the National Statistics Institute[(69)] shows a decrease of EAP coverage in the urban formal sector from 67.4 per cent (1980) to 62.6 (1990) and for the industrial formal sector from 82.3 per cent (1980) to 78 per cent (1990).

The whole pension system has largely been unified at the national level since 1967, when all public programmes for private employees were merged under the INPS (National Institute of Social "Providence", also called "Previdência"), which currently uses a pay-as-you-go system. In 1977, pension, health and public assistance programmes were integrated into the "SINPAS" system. The institution in charge of cash benefits remained the INPS. There continue to exist many social security institutions at regional and local levels for public employees, that enjoy a certain degree of freedom concerning the establishment of contribution and benefit features. Furthermore, there are separate programmes for the military and federal civil servants, paid from the budget or special provisions of the former employing ministry or institution. Parliamentary pension schemes also allow benefits independent of other regulations.

After the end of military rule, the new civilian Constitution of 1988 maintained for the most part the previous structure of social security. The Constitutional Assembly decided to write into the Constitution extensive citizenship rights and goals concerning social security, going from general principles to rather specific statements of entitlements. It was established that social security is a social right of each citizen and that the "organization of social security is a duty of the State", defining the following targets: Universality of coverage, redistribution ("distributividade"), financial equity, democratic and decentralized administration (explicitly referring to tripartism - in a 1991 law the retired were also included in the Social Security National Council), as well as uniformity and equivalence of benefits between urban and rural populations. Therefore, the expansion of social security to the general population and the maintenance of a high coverage of risks under the redistribution-principle are both Constitutional mandates. The text explicitly allows private institutions to "participate as a complement" to public health insurance and expresses no prohibitions regarding private provision of old-age, disability and survivor insurance.

Since 1991, indeed, public social security is mandatory for all employees, domestic servants, entrepreneurs, self-employed and rural workers; before 1991, the last named were covered by the "rural regime", within which the contribution and benefit structures were distinct from the urban structures. In the urban sector benefits were contribution-related and their financial basis drew heavily on earmarked payroll taxes, whereas the rural regime granted old-age, disability and survivors pensions on a flat-benefit basis, revenues coming from payroll taxes on urban enterprises, taxes on the value of agricultural sales to towns and cities and taxes on uncultivated farms; in the 1980s, part of a tax on the gross revenue of all enterprises (this contribution is called FINSOCIAL) became an additional source of finance[(70)]. The Constitution of 1988 doubled all rural pensions from 0.5 to 1 times the minimum wage and introduced an article guaranteeing that any income-replacement benefit would have to match this minimum. In 1991, in pursuance of the constitutional obligation of greater equality between the urban and rural sectors, Laws 8212 and 8213 ended the rural programme, and instead moved the rural affiliates within the general contribution-related scheme, defining their contribution at 2 per cent of the commercialized production and extending all the other vesting conditions as well as the possibility of acquiring the right of an early pension, as in the former urban regime.

Currently the revenue of the INPS includes (i) payroll taxes, 21 to 23 per cent of nominal wage paid by the employer, including disability insurance, and 8 to 10 per cent by the employee, according to income (maximum taxable basis is 10 times the minimum wage); (ii) taxation of gross turnover (2 per cent) and gross profit (10 per cent) of all enterprises, and (iii) a State contribution from general revenues, which has a legal ceiling of 10 per cent of the social security budget starting in 1995. The State contribution is intended to cover administrative costs and an eventual deficit. Within the INPS revenue, earmarked contributions have accounted historically for 80 to 90 per cent of pension programme revenues, the rest coming from general treasury and other revenue sources (i.e. investment revenue, interest on overdue contributions, etc.; data are for the 1970s and 1980s by Portocarrero de Castro et al., 1993).

Evasion is thought to be quite high. Official figures in fact indicate that only 50 per cent of the employed population contributed to social security in 1990(71). Furthermore, according to press information, around 2 million employers were estimated to be evading social security contributions and only one million were paying contributions on a regular basis(72). Until 1993, official efforts to contain evasion had registered 260,000 enterprises as social security debtors, with overdue contributions renegotiated in roughly 100,000 cases. The sum of annual evasions has been estimated to be US$ 6 billion, over 1 per cent of GDP. It seems reasonable to accept Mesa-Lago data (1991) of around 60 per cent evasion plus delinquency for Brazil in the 1980s, one of the highest figures for the whole of Latin America.

The Constitution of 1988 and the 1991 laws largely maintained and improved pension benefits, but the vesting period will be increased gradually from 60 to 180 monthly contributions until the year 2012. Increased benefits included:

(1) Old-age pensions: At age 65/60 (male/female in urban activities) or age 60/55 (male/female in rural occupations); benefit of 70 per cent of the contribution base of the last 3 years plus 1 per cent for each year worked, not to exceed a maximum replacement rate of 100 per cent.

(2) Early retirement pensions: After 30/25 years of activity (male/female); benefit of 70 per cent of the contribution basis of the last 3 years plus 5 per cent for each year worked after reaching the entitlement, not to exceed the maximum replacement rate of 100 per cent.

(3) Special retiring regimes:

> (a) early retirement pensions for teachers, university professors, journalists, aviation employees, justice employees after 30/25 working years (male/female); benefit equal to 100 per cent of the last 3 years basis;
>
> (b) long activity pension for dangerous and unhealthy jobs after 15, 20 or 25 working years; benefit of 85 per cent of the last 3 years contribution basis, plus 1 per cent for each additional year worked after entitlement, not to exceed a maximum replacement rate of 100 per cent.

(4) Survivor pension: Owed to the dependents of the deceased; benefit equal to 80 per cent of the insured's pension or of the pension the insured would have received if retired at moment of death, plus 10 per cent for each dependent, not to exceed the maximum replacement rate of 100 per cent. In case of death due to work-related injury, replacement rate of 100 per cent.

(5) Public assistance benefits for old-age and disability: To disabled of any age (subject to an examination by a "Previdência" physician every 3 years) and those who satisfy the age requirement for an old-age benefit, independent of vesting period, but do not qualify for standard pension; benefit of 1 times the minimum wage.

Cash benefit figures for 1989 show that more than 90 per cent of expenditure went to retirement pensions and public assistance benefits substituting for pensions (see Table 14). Urban and rural regimes were still functioning separately at that time. This figure shows why social security reform in Brazil is synonymous with pension reform - however it should not be forgotten that the health sector has enormous problems as well. One can see that early retirement pensions in the urban sector (including the special retirement regimes), accessible in most cases only to the middle and higher middle classes, obviously receive a disproportion of the benefits when compared with standard modes of retirement. In the 1980s, 28 per cent of urban pension expenditure went to 9 per cent of urban pensioners[(73)]. It is also clear that there is a need for greater redistribution towards urban public assistance and that, although working under different rules, the rural sector (where poverty is larger) receives disproportionately less expenditure, compared to its proportion of the number of beneficiaries (see Table 14).

If one considers the real average benefit value (Table 15) and the average value of cash benefits in 1989 relative to minimum salaries (Table 14) except for early retirement schemes, it is clear that "INPS-Previdência" is paying one "basic income benefit" (minimum wage) for most of the retired at the present time. In fact, according to press reports[(74)], standard pensioners in Brazil are practically obliged to continue working if possible (often in the informal sector), in order to guarantee the income levels they had expected from their contributions or even a minimum consumption level. Other reported inequalities exist between the public INPS scheme and the federal as well as certain regional civil service pensions, where around 800,000 retired earned an average pension four times higher than INPS benefits. From 13.8 million benefits paid out regularly, according to the same source, roughly 11.5 million equalled 1 minimum wage (whose value fluctuated between US$ 40 and US$ 70 at the end of the 1980s and early 1990s, according to inflation cycles and frequent changes of indexing formulae). The average pension paid under the INPS regime at the beginning of 1993 was US$ 113.

On the other hand, the fact that the financial INPS structure has not yet broken down, is largely the result of the drastic reduction of real benefits during the 1980s at almost the same pace as the reduction in the value of the real minimum wage. Other factors which allowed temporary improvements in the accounting balances were a tough personnel and social expenditure reduction policy during the Collor Government (1990-92) as well as the gradual reduction and suspension from 1993 on of the legal monetary transfers owed by INPS to the unified health system SUS (INAMPS, the Social Security Health Assistance Institute was being extinguished at the same time; see table 12). The financial needs of SUS, a merger of the health and hospital systems of INAMPS, Health Ministry and regional health institutions created by the 1988 Constitution, have been left for other budgets, mainly the Health Ministry's and regional budgets[(75)]. Nevertheless, the projected INPS deficit for 1995 is reported to be close to US$ 3.8 billion[(76)].

Before considering recent reform attempts, a short look at the role of private institutions that provide monetary benefits on a voluntary basis as a complement to public entitlement schemes can shed some light on the public-private issue. Private arrangements under the form of the so-called non-profit seeking "montepios" as well as other forms have a long tradition in Hispanic Latin America[(77)] as they do in Brazil. In 1977, Law 6,435 authorized explicitly private profit-seeking pension funds, whether under the occupational pension fund form tied to one or more enterprises (called "closed funds"), or as an "open fund" accessible to every individual wishing to affiliate. In the 1980s, due to macroeconomic instability with high inflation, lack of strict controls, insolvencies or the small-prints in contracts, open private pension programmes did not win the trust of potential affiliates. On the other hand, the "closed funds" had a greater importance and grew steadily, by the end of 1989 reaching the number of 235 accredited institutions, covering 1.8 million affiliates with total assets of US$ 14.8 billion (Table 13).[(78)] These "closed funds" held in 1987 around 7 per cent of total financial assets in Brazil, covering 4.7 per cent of EAP. In the early 1990s, private pension funds grew faster than before: The existing 42 "open funds" (mostly within a bank holding structure) increased their number of members to 800,000 (growth rate of roughly 20 per cent a year in 1992)[(79)].

The largest of the current 299 occupational plans were and still are tied to public enterprises (110 funds, 80 per cent of the "closed" funds' accumulated assets). This is not surprising, because these are the largest enterprises in the country as well. The largest "closed" fund is PREVI, sponsored by the federal-owned Banco do Brasil, with 114,000 affiliates and paying 26,000 pensions. Another large occupational fund is PETROS, covering 60,000 employees (23,000 retirees) of Petrobrás. Occupational plans were sponsored by 1,110 private and 300 public enterprises, purportedly reaching 2.8 million affiliates and with some 210,000 beneficiaries. The "closed funds" were said to control accumulated assets of US$ 35 billion. Benefits granted by "closed" funds average 70 per cent of the contribution basis, but there were some higher percentages: PETROS pays 90 per cent, with an average pension value of US$ 860[(80)].

According to press reports, a problematic side of occupational funds is the estimated potential deficit of US$ 30 billion in state enterprise-tied schemes, that being due to a lack of auditing, lack of professionalized administration and non-transparent accounting procedures[(81)]. It was also reported that the Federal Accounting Court (TCU) discovered an illegal transfer of US$ 1.3 billion to public enterprise-sponsored funds.

This short review has shown that, independent of whatever form social security restructuring in Brazil may take, state enterprise-sponsored funds should be more closely regulated and put on an actuarially sound structure. In conclusion, it should be kept in mind that "private" occupational pension funds with their growth, development, capital market effects, etc. as well as with their flaws and scandals in the 1980s and early 1990s in Brazil are for the most part a public sector phenomenon, - through its rather autonomous state enterprises (which are - not without reason - called "autarquias").

5.2 Reform proposal in March 1995

Within a constitutional reform process presently in progress in Brazil, the Government sent to Congress a constitutional amendment draft to start "Previdência" reform in March 1995. Its main features are:

(1) it would immediately eliminate early retirement pensions and all special regimes including those for parliamentary activity, except those for dangerous and unhealthy jobs;

(2) it assures maintenance of a special regime for the armed forces;

(3) it maintains administratively separate programmes for federal and local civil servants, but follows the general contribution and entitlement rules of the INPS;

(4) it forbids the accumulation of pensions (which is possible under current legislation), as well as the cumulation of a pension and remunerated public employment;

(5) it foresees a complementary pension scheme to top-up the basic pension right provided by the public system;

(6) it forbids the State or any public budget to subsidize supplementary pension funds, and if the State contributes to such a fund as an employer, public contribution must not exceed the employee's contribution;

(7) it eliminates former pensionable ages written down in the 1988 Constitution and leaves this item to be defined in complementary legislation (with the intent of unifying age rules among remaining benefits);

(8) it assures maintenance of social assistance pensions, including those disabled, subject to means tests. Determination of the benefit value will be given by complementary law, thus delinking those

pensions from minimum wage legislation;

(9) those already retired or who will have qualified for any former existing benefit at the moment of amendment approval will still have their rights protected. Contributions made up to date will be recognized and the recognition mechanism established by complementary law;

(10) it maintains the former floor of 1 times the minimum wage for any earnings-replacement benefit granted in the future.

This reform proposal appears to have been articulated since the end of the 1980s. Within the constitutional re-examination process, delayed from 1993 to 1995 and the "refreshment" of federal government legitimation with the election of Pres. Cardoso, the political momentum was thought to be favourable for a reform of the "Previdência" to make the structures defined in the 1991 laws viable in the future.

One of the features of the draft that will probably interest international observers and spur heated debates in Brazil, once congressional discussion starts, are the functional duties and opportunities assigned to public and private sector entities in supplying pension insurance. Brazil would be a unique exception in Latin America, if the powerful financial community did not exert successful pressure towards greater private weight to the provision of pensions. One must remember that the idea of a supplementary pension tier was already included in Brazilian legislation in the recent past through Laws 6435 (1977) and 8213 (1991). If the current constitutional amendment draft is approved by Congress, what was written in ordinary law will from that moment on be included in the Constitution, allowing any possible combination of public/private supplementary funds.

We do not know the features a Previdência supplementary regime will have or whether private funds would even be allowed to enter the compulsory system, following the Chilean AFP-model. Some analysts have risked predictions about the potential size that accumulated funds might reach (no reference is made if within the compulsory, supplementary or both regimes): Penteado Mendonça[(82)], from the insurance sector in São Paulo, is of the opinion that "in a very short term" US$ 30 billion could be accumulated and invested; former economics Minister Maílson da Nóbrega[(83)] speaks of US$ 250 billion in 5 to 10 years, to be invested in the capital market. The basis for these forecasts is not mentioned, but probably they are based on an extrapolation from Chilean accumulation indicators. The financial community will certainly try to obtain mandatory pension funds as well as fiscal incentives for supplementary savings schemes, but it should be remembered that a good deal of the Brazilian financial system is (still) in the hands of public entities.

Turning back to other aspects of the amendment draft, a reform with the proposed profile seems to contribute to less regression in the benefit structure, as demanded by the 1988 Constitution, because it goes straight in the direction of a standardization of the different social security programmes, eliminating the bulk of the privileged and unjustified benefit differentiation and benefit cumulation possibilities. In this sense, the elimination of the early retirement pension scheme and the unification of public employee programme rules seem to be among the most important measures proposed, although past attempts to close the early retirement programme at the beginning of the 1980s were defeated. The maintenance of a special pension scheme for the armed forces does not really contribute to greater equity, but the draft text remains ambiguous about the extension of privileges in future military pension schemes[(84)].

Speculation about future steps in the press reads as follows[(85)]: The Government wishes to propose that in the basic tier men and women will retire at the age of 65, which can be considered high for Latin America, but which lies within the general trend of current reforms. This age would eliminate one of the few advantages for women. Earliest retirement age would be 58 if a vesting period of 38 to 40 years is respected (now the toughest condition in Latin America, with the goal of restricting the number of entitled persons). With the limiting of benefit access, it is expected that average retirement age would increase from currently 54 years to 64. In any event, the intent is to establish a gradual timetable for the introduction of these changes.

A ceiling for old-age benefits would be fixed somewhere between 3 and 10 times the official minimum wage (currently the maximum pension INPS pays out). Those who so desire, can affiliate with a supplementary pension programme, which will probably be offered by the Previdência in competition with private funds.

Badly needed administrative simplification and increases in the efficiency of the INPS scheme also seem to be possible, if the draft was to be accepted. Financial consequences seem to be far-reaching, even if at the moment any calculation would be pointless, because many (if not all) important variables are still open to debate and left to complementary laws[(86)]. The transfer of INPS rules to public employee schemes at federal, regional and local levels will certainly restrict growth of future pension expenditure in several public budgets, some of which are heavily burdened with liabilities towards retired employees. The elimination of early retirement and special programmes would also have an important impact on the cost of the INPS, although no meaningful effect could be expected in the short-term, because many of those already entitled to the basic early retirement pension rate of 70 per cent and particularly those who could add 5 supplementary years (each of which results in a 5 per cent increase of earnings replacement) have immediately requested early retirement this year, as soon as the government sent the draft law to Congress.

Even if an opinion poll among Congress members published in February 1995[(87)] indicates sympathy towards the main proposals of the draft, this does not mean that the reformers will have an easy job. On the contrary: The current situation (May 1995) is that the draft has been broken into separate items in Congress, instead of a "block vote", thus opening the way to trade-offs. Furthermore, political party leaders decided to postpone any vote on this draft to a still unknown point in 1995 (or even 1996), after a series of constitutional amendments affecting other subjects has been negotiated and voted upon. President Cardoso's party (PSDB) has a minority of deputies in Congress and naturally depends on negotiation and compromise. Besides organized public protests and resistance by affected social groups, i.e. the public employees unions and national confederations of trade unions, the reform also meets general opposition from public opinion, including the National Lawyers Association OAB and the Catholic Bishops National Council CNBB[(88)], mainly due to the feeling that legitimately acquired rights would be lost. As a general tendency, one should expect that the amendment draft will suffer substantial changes in favour of the presently better-situated at the expense of the general tax-payer and poorer would-be beneficiaries.

Recent Brazilian reform attempt is a reversal of the tendency which began in the early-1980s, when democratization deepened the extension of "Welfare-State" benefits to the entire population, culminating in the detailed listing of social rights in the Constitution. The Brazilian dilemma consists in the hard choice for Government and Congress either to honour those obligations which have remained largely on paper in the past and increase taxes and contributions considerably while curtailing some existing rights (and personnel), or to honour the existing obligations of the old system and postpone the constitutional Welfare State with its massive transfers to the poor and the elderly to a later stage. The choice of the third option, namely drastic liberalization and privatization with public assistance (as in Chile) or without great social transfers (as in Peru) seems out of question in Brazil at the present time. The "implementation gap" of the Brazilian Welfare-State dream is large, but this dream has never become a nightmare (such as in Uruguay or to a certain degree in Argentina), nor has the State as such in Brazil ever become an enemy (such as in Chile and Peru) for important parts of the population. That is why muddling-through efforts towards a Swedish-type universal Welfare State are to be expected, resisted by corporatist (para-statal) privileged interests rather than by neo-liberal social forces and ideologies.

5.3 An updated overview of the Brazilian pension reform process

After the publication of the Constitutional Amendment Draft in March 1995, public discussion spread among political parties, trade unions, employer associations and academic institutions, receiving wide media coverage throughout 1995. In Congress, a tendency towards blockage of the Amendment Draft evolved under the pressure of the civil society (who was inclined towards refusing it) and diverging political parties' interests (which tended to divide the original proposal into pieces), resulting in a delay of the pension reform decision. Furthermore, constitutional amendments affecting other subjects - e.g. the role of foreign capital - which received more governmental attention, were negotiated and approved.

It was probably the French upheaval (after President Chirac's announcement of reform intentions for the French social security system) during the month of December 1995 and the publication of the Previdência's deficits in the balance sheet for 1995, which created a shift of the negotiation strategy on all sides in Brazil. The actual 1995 deficit of US$ 200 million run by INPS was not of as dramatic proportions as forecasted, but it was the first time (in 1995) after the 1980's general economic crisis that the INPS revenues did not match current benefit expenditures. The administrative costs are not included in that figure. The deficit of the Social Security Ministry as a whole for 1995 had the sizeable dimension of US$ 3.6 billion.[(89)] In January 1996, President Cardoso and his government representatives started negotiating directly with the three most important national level trade unions (Central Única dos Trabalhadores - CUT, Confederação Geral dos Trabalhadores - CGT and Força Sindical), which represent around 34 million workers, instead of limiting themselves to the rather blocked congressional channels. The results of the Government-Trade Union negotiation process were afterwards to be submitted to votation in Congress.

Throughout 1995, President Cardoso had insisted on the closure of any early retirement programmes (except for special pensions due to unhealthy jobs) and his proposals for minimum qualifying age for old-age pensions oscillated between the ages of 60 and 65. During the "Previdência Fórum" meetings with the trade unions in January 1996, this point was dropped but, in return, the unions accepted a minimum vesting period of 35 years of actual contribution as a prerequisite for early retirement. Further agreement was reached on the elimination or reduction of privileges for several professional groups: public servants, judges and congress deputies are thought to lose privileges and to be (at least in part) submitted to the general retirement rules, while elementary and high school teachers, as well as rural workers, would continue to enjoy certain exceptions. The final result of negotiations is still not clear, because the representatives of the trade unions (at the National level) are currently pressurized by the local and regional levels, as well as by pressure groups to withdraw from these concessions. The negotiations were still on in early February 1996. It seems that the Government planned to include the military under the "civil servants" label for pension rules, but there has been strong resistance to this. It appears to be clear that the cumulation of different pensions by the same person or the cumulation of a pension and a paid job will be restricted if not prohibited. In December 1995, the Social Security Ministry announced that it wishes to maintain the ceiling of 10 times the official minimum wage both as contribution basis and maximum benefit.

In early 1996, the available data pointed towards the maintenance of a basic pay-as-you-go pension system in Brazil, with a sharpened social insurance component. A first conclusion that can be drawn from this is that by introducing the requirement of 35 years of contribution in combination with the stepwise increase of the vesting period previously determined by Law 8213, and the inclusion of unemployed periods with the respective contributions being made by the unemployment insurance fund, the estimated 30 million Brazilian informal sector workers will be *de facto* excluded from the regular Previdência schemes. Certainly a significant proportion of the female workers in the formal sector will be adversely affected as well. Under the current system it is necessary to have not only fulfilled the 60-month contribution requirement (now gradually increasing to 180 months) but also to have 35 years of contributory service in the formal sector, in order to become entitled to early retirement. For aged persons with a low income profile and no social insurance entitlement, the Social Security Ministry would start operating a targeted social assistance pension programme with a monthly benefit of 1 times the minimum wage which is currently US$ 100 (requirements: age 70 and household per capita income under one fourth of the official minimum wage).(90)

A second point to stress is that, even if it is presently impossible to predict the consequences of these alterations (if approved) on the Previdência balance sheets, press commentaries claimed that the long-term imbalance of the Previdência would not be corrected and that financial trouble would soon reappear. In fact, Social Security Minister Stephanes has recently called the results of the double negotiation with the Congress and the trade unions "an adjustment, not a reform".(91)

Thirdly, it cannot be expected that the current average value of Previdência's benefits will improve significantly in a predictable future. This makes supplementary pension schemes, aided by the current macroeconomic stability provided for by the real stabilization plan, attractive for the middle and middle-high classes. The Brazilian press has recently made reference to the fact that the Ministry of Social Security and the Ministry of Economics have a voluntary, fully-funded, individual savings, supplementary old-age pension project in their drawers.(92) Those interested could open a "special savings account" at a "bank" (no specification of which type of bank), enjoying preferential tax treatment. The saved amounts could be withdrawn after 3 years for any purpose, but would lose their tax incentives. An old-age supplement would be granted after 10 years or more of saving. Reform proposals following the "Chilean" model, including fully-funded mandatory components, were made in the early stages of the Brazilian debate, but they have not had a concrete chance, having been defended only by a relatively small political minority in Congress and the civil society.

Finally, as in Colombia, one can conclude that the social security reform process, if carried out in a democratic environment with the participation of political parties, employer associations and trade unions, tends to take a longer time to be completed than would be the case in a technocratic or authoritarian environment, even if allegedly in the name of "individual liberty", such as in the cases of Chile and Peru. The overwhelming advantage shown by the Colombian and the Brazilian examples is that the negotiating, searching and learning processes help to increase public knowledge and commitment towards social security institutions, which is particularly important for social cohesion and democratic legitimacy in times of deep reorientation of the development model.

Chapter 3: Conclusions

Recent Latin American reforms have displayed several different arrangements regarding the respective roles of the State and private sectors. The Chilean reform, which seemed to be the leading pattern in the early 1990s, when a democratic government legitimized it, is no longer the sole alternative. In any case, the State continues to play the crucial roles of assuming the pre-existing social security debt, regulating mandatory as well as voluntary pension funds, as well as offering guarantees and eventually a "safety net" for those who fail to qualify for regular programmes. State functions go beyond a simple regulatory function.

Offering open-ended guarantees over the long-run has imposed considerable financial liabilities on the State, the magnitude of which is hard to estimate. Even in the case of the Chilean reform, for which the most information is available, we lack a clear picture of its fiscal costs. The fiscal burden incurred by the State in assuming the "invisible debt" to those insured under the old system will certainly be of a significant scale, and promises to back the new systems are even more difficult to evaluate.

On the other hand, in those countries which have placed a heavier and sometimes constitutionally mandated burden on the State (i.e. Brazil and Colombia), liabilities tend to surpass fiscal capacity. These countries are now challenged to decide a) whether to honour the legal claims written on paper and close the "implementation gap" by increasing social spending significantly while, simultaneously, cutting overly generous benefits and raising the social insurance contribution and taxes, or b) whether to retailor Welfare-State aspirations and to postpone them to some future time. Both alternatives will face strong political opposition by the groups affected, particularly those with cumulated benefits. These constitute difficult policy issues. It is symptomatic that the only two radical curtailments of former "Social States" in Latin America, namely Chile and Peru, have taken place under suspension of constitutional rights.

It is characteristic of the definitely privatizing reforms (Chile and Peru) that the traditionally agreed tripartite control of the social security institutions has been abandoned; on the other hand, the design of the Colombian private funds shows that representatives of the insured can be included on the supervisory boards of an AFP. In Chile, proposals have been made to give trade unions more power in controlling private funds by allowing affiliation to occur on a collective basis instead of limiting AFP-choice to strictly individual decisions(93).

The bulk of the alleged positive impact on macro-economic investment expected from the introduction of private fully-funded schemes still remains unclear. First, all Latin American reforms, that include private components have left the State with a future liability of repaying the "Social Debt" and a responsibility to close the gaps, when private schemes (even making profit) are unable to guarantee minimum pension levels and/or income security. Second, these private schemes start without any obligation towards the repayment of the "invisible debt" accumulated under the previous social security systems. This entire financial burden of existing social security commitments remains on the State. Summing up, there remains a significant fiscal burden going into future, having an unforeseeable size as well as a definitive bias toward government consumption rather than public investment.

The initial goals associated with the Latin American reforms claimed that higher investment and saving together with further development of capital markets would be achieved. The only result that seems to be realized from the Chilean experience has been a push towards further institutionalization in the capital market. However, the goal of higher aggregate saving and investment has not been achieved in the Chilean case.

Another unresolved point is the safety of pension levels in fully-funded schemes, which depend heavily on compliance and on the rates of return achieved. Within an internationally volatile financial environment and should the alleged tendency of national interest rates toward international (lower) levels become real, it is not at all clear whether fully-funded schemes can provide higher and safer pensions than the old pay-as-you-go programmes.

A further open question is the "targeting" issue: various mechanisms have been used in Latin America. In most countries, formal social security was and still is expected to replace earnings more or less completely. Living standards achieved during active years of the salaried middle and higher-middle classes can thus be supported and maintained without notable private additional savings. This pattern has led to the cumulation of rather lavish benefits for those privileged sectors, at the expense of other large groups of the population (low coverage), and an insufficient financial basis to fulfil the income-replacement function (let alone universality aspirations) once the financial crises of the States in Latin America began. At the same time, the dream of a universal Welfare-State was nourished in which everybody would be entitled to the privileges of the few. Explicit targeting on the poor through a combination of social insurance with social assistance mechanisms runs counter to this income-maintenance vision of social insurance.

Women have lost under most of the reforms conducted in Latin America, because vesting periods were raised without adequate allowance for maternity and child-rearing periods. Besides this, the pressure on women to perform supplementary functions in the provision of informal social security and maintenance of the families has increased during the course of the 1980s. A "gender perspective" in social security reforms in Latin America has not yet evolved which would allow women to conciliate productive life and reproductive specificities with an integration into development.

Looking at the reforms from the perspective of social equity, it is clear that the move towards a funded component in social security design does not exclude the biased distribution, characteristic of the former schemes in Latin America. This move also does not necessarily accompany basic social assistance services and transfers such as observed in Chile. The contrary is seen by the Peruvian adaptation of the "Chilean model" that has left those ineligible for participation in the private funds quite abandoned.

The dismantling of tripartite or government-run social security structures in favour of private funds has, of course, effects on the macro-structures and the balance of power in a society. Such long-term effects can not yet be evaluated, but initial experience suggests that "grupos financieros", national conglomerates and international financial groups have been able to play enhanced roles in oligopolized financial markets. Thus it would be essential to establish supervision of their activities and perhaps ultimately imposing conditions upon those funds, to commit them to a positive role in socio-economic progress and preventing their withdrawal from social responsibilities. The same is also valid for public and tripartite funds, that likewise require "good governance" structures, in order to prevent their degeneration into "states within the State".

Finally, taking into account the often declared need to honour the "social debt" and to alleviate poverty in Latin America, it is encouraging to see that the task of providing a certain basic minimum transfer income within pension programme reforms has been taken up in various countries. Herein, financing does not rely on a strict "Bismarckian pattern", which tends to create an obstacle to expansion of coverage beyond the salaried classes. This means that, beside redirecting social security toward the more needy classes, some young Latin American democracies have started to tap alternative financial sources other than only payroll contributions and taxes making a further step toward a "Beveridgian model" in the Welfare-State tradition.

The panorama is rather wide, stretching from the ultra-liberal Peruvian approach with private funds and virtually no social transfers, to the Chilean mix of privatization with heavy social burdens shifted to the State while providing basic coverage at least in principle, to the parallel system of Colombia, and to the Brazilian blend of a universal Welfare-State dream that coexists with glaring inequalities between the privileged and the poor in the real world. It remains to be seen what will be the outcome of these various reform efforts. In any case, the life of millions of people depend on the critical choices made by the reformers. The public, academic and political debates that accompany these processes must keep in mind the multiple facets of social security: From its fiscal and wage cost aspects to poverty alleviation and the questions of gender and family policy, as well as capital market development. Finally, tripartism as a pillar of democracy is at stake often without a serious debate on its shortcomings and merits.

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Footnotes:

1. [1] For historical information, see Mesa-Lago (1978). An interesting case study is found in Malloy (1979) which sketches the evolution of the Brazilian social security system during this century.

2. [1] Including provisions for the traditional risks: medical care, sickness, unemployment, old age, employment injury, child maintenance, maternity, invalidity and death of the breadwinner.

3. [2] Mesa-Lago, 1978. Mesa-Lago (1991a) also distinguishes among "pioneers", "intermediate

countries" and "late-comers", as referred to the inception period and general characteristics of each country's social security system in Latin America.

4. [3] ECLAC, 1991.

5. [4] Mesa-Lago, 1978.

6. [5] See, for example, Mesa-Lago (1991).

7. [6] A paraphrase of Ibn-Badis, a muslim reformist (1889-1940; "Educate a boy and you educate a person, educate a girl and you educate a nation") could be "If you extend social security to women, you extend it to a society."

8. [7] Eichler, 1992; Diamond & Valdes-Prieto, 1994; Schultze-Kraft, 1995; Mesa-Lago, 1978; 1993; Witte, 1995.

9. [8] Witte, 1995; Kleinjans, 1995.

10. [9] Mesa-Lago, 1993.

11. [10] Mesa-Lago, 1993; Witte, 1995.

12. [11] Data from Draibe (1993).

13. [12] Within the Chilean AFP-system, all account-holders are called affiliates (afiliados), but only those who meet the compliance criteria are named "insured" (asegurados).

14. [13] Witte (1994) quotes a study that argues pension contribution rates could have been lowered within the old system down to one-third of the former ones, as a result of unification and raising of retiring ages.

15. [14] Schultze-Kraft, 1995; Mesa-Lago, 1993; Witte, 1995.

16. [15] Arrau, 1992; Ruiz-Tagle, 1994.

17. [16] Ruiz-Tagle, 1994.

18. [17] Mesa-Lago, 1993.

19. [18] Arrau, 1992.

20. [19] Diamond and Valdés-Prieto, 1994; Ruiz-Tagle, 1994.

21. [20] Ruiz-Tagle, 1994.

22. [21] Diamond and Valdés-Prieto, 1994.

23. [22] Schultze-Kraft, 1995; Kleinjans, 1995.

24. [23] Schultze-Kraft, 1995.

25. [24] Diamond and Valdés-Prieto, 1994.

26. [25] Gillion and Bonilla, 1992.

27. [26] Ruiz-Tagle, 1994.

28. [27] Ruiz-Tagle, 1994; Diamond and Valdés-Prieto, 1994.

29. [28] Ruiz-Tagle, 1994.

30. [29] Diamond and Valdés-Prieto, 1994.

31. [30] Diamond and Valdés-Prieto, 1994.

32. [31] Mesa-Lago, 1991.

33. [32] Análisis Laboral, 1994.

34. [33] Dirmoser, 1994.

35. [34] Mesa-Lago, 1994.

36. [35] Actualidad Económica, 1995.

37. [36] Análisis Laboral, 1994.

38. [37] Análisis Laboral, 1994; CEDAL/APRODEH, 1995.

39. [38] Mesa-Lago, 1994.

40. [39] Actualidad Económica, 1995.

41. [40] CEDAL/APRODEH, 1995.

42. [41] Actualidad Económica, 1994.

43. [42] CEDAL/APRODEH, 1995.

44. [43] Actualidad Económica, 1994.

45. [44] According to Witte (1995), the contribution rate was originally intended to be raised from 6 per cent of the payroll until reaching 20 per cent at the present time. This contribution should be paid according to the following shares: 1/4 by the employee, 1/2 by the employer and 1/4 by the State. However, the State never contributed its share and only a slight increase of the employee-employer contributions was implemented in the 1980s.

46. [45] Coverage was also highly concentrated among activities; i.e. in the public sector: 99 per cent; rural coverage: 6 per cent.

47. [46] See López Castaño, 1992 and Kleinjans, 1995. A typical Colombian worker spends only around half of his active working life in the formal sector.

48. [47] Kleinjans, 1995.

49. [48] Witte, 1995; Kleinjans, 1995.

50. [49] Cañon Ortegón (1992), quoted in Kleinjans (1995).

51. [50] More detailed in Kleinjans (1995).

52. [51] Witte, 1995.

53. [52] Witte, 1995; in the historical long-run, 4 per cent has also been the average (Kleinjans, 1995).

54. [53] This means that the "minimum return rate" can be very low, if general capital market index did not evolve "satisfactorily".

55. [54] Witte, 1995.

56. [55] Data about the evolution of the informal sector in Colombia show a steady increase between 1990 (43 per cent of all workers) to 1993 (60 per cent); source: data from the DANE household surveys and Fedesarollo in IEPRI (1994).

57. [56] Kleinjans (1995) resumes the forecasts of Lora/Zuleta/Helmsdorff (from Fedesarrollo Institute), Carlos Alberto Naranjo (Colombian Actuarial Association) and Emmanuel Nieto.

58. [57] Studies from Fedesarrollo (Lora/Zuleta/Helmsdorff) [1992]. Viabilidad macroeconómica y financiera de un sistema de pensiones privado. Santa Fé de Bogotá; Ocampo [1992]. La propuesta gubernamental de reforma al régimen pensional: análisis y alternativas. Debates de Coyuntura Económica, Nr. 26; and Contraloría General de la República [1992]. La reforma a la seguridad social en Colombia. Una aventura económica? Santa Fé de Bogotá, are quoted by Kleinjans (1995).

59. [58] According to Mesa-Lago (1991a), women life expectancy at moment of retirement in Colombia was almost 6 years higher than the same figure for men (21.4 to 15.6).

60. [59] In August 1994, there were 8 SAFPs, several of them running under the advice of Chilean AFPs and 2 with foreign capital participation (Citibank, Chilean AFPs).

61. [60] Mesa-Lago, 1994.

62. CCSS: Social Security Indicators 1990-94. October 1995.

63. [62] Mesa-Lago, 1993.

64. [63] Mesa-Lago, 1994.

65. [64] Mesa-Lago, 1993 and 1994.

66. [65] Mesa-Lago, 1994.

67. [66] Mesa-Lago, 1994.

68. [67] Mesa-Lago, 1991. However, recent data for 1990 (FIBGE, 1994) show that 92.5 per cent of the rural working population does not contribute to social security and any visit to the Brazilian countryside confirms the suspicion that a large part of that population does not either receive the services and transfers or the physical and bureaucratical access conditions are strong impediments.

69. [68] IBGE, quoted by Gazeta Mercantil, 04.04.1995.

70. [69] Mesa-Lago, 1991.

71. [70] FIBGE, 1994.

72. [71] Veja, 31.03.1993.

73. [72] Mesa-Lago, 1991. Draibe (1993), without mentioning the year, informs that early retirement and special regimes account for 22 per cent of the retired and 50 per cent of pension expenditure. Around 60 per cent of the early-retired were aged under 55.

74. [73] Veja, 31.03.1993.

75. [74] Draibe (1993) writes that the health sector is "brutally" underfinanced; health expenditure per capita had already fallen dramatically in the period 1987-93 from US$ 80 (1987) to US$ 21 (1993).

76. [75] Folha de São Paulo, 06.02.1995.

77. [76] See Mesa-Lago, 1978.

78. [77] Over the 1980s, open funds averaged less than 10 per cent of the affiliates of "closed" funds and about the same proportion of assets (Carvalho and Faro, 1993).

79. [78] Data from Veja, 22.02.1995.

80. [79] All data for Dec. 1993 from Folha de São Paulo, 19.06.1994.

81. So Folha de São Paulo, 23.01.1995

82. [81] Folha de São Paulo, 27.03.1995.

83. [82] Interview to Banco Real News, Feb. 1995.

84. [83] Folha de São Paulo, 17.03.1995.

85. [84] Veja, 22.02.1995.

86. [85] One extremely important variable is the retirement age, whose raising determined substantial savings in the Chilean pre-reform steps of the 1970s (see for example Arrau, 1992; Witte, 1994 and 1995).

87. [86] Veja, 22.02.1995.

88. [87] Gazeta Mercantil, 23.03.1995 and 24.03.1995.

89. [88] Folha de São Paulo, 28.12.1995.

90. [89] Jornal do Brasil, 20.12.1995.

91. [90] Jornal do Brasil, 17.01.1996; Estado de Minas, 14.01.1996.

92. [91] Jornal do Brasil, 19.01.1996; Zero Hora, 25.01.1996.

93. [92] See, for example, Ruiz-Tagle, 1994.

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