Current Issues in Social Security: Pensions, Poverty and Health

Karl Theodore
Althea La Foucade

Interamerican Conference on Social Security

Studies Series
53

Secretariat General

This book was published by the Secretariat General of the Interamerican Conference on Social Security. The statements contained in this book are solely those of the authors and do not necessarily express any official opinion or endorsment by the Interamerican Conference on Social Security.

Interamerican Conference on Social Security

ISBN 968-7346-80-9

Current Issues in Social Security: Pensions, Poverty and Health

Current Issues in Social Security: Pensions, Poverty and Health

Karl Theodore
Althea La Foucade

Studies Series 53

Interamerican Conference on Social Security
Secretariat General

Technical Support:
Jannet Hernández Rueda
Arcelia Martínez Ramos

CONTENTS

List of Tables

List of Figures

Acknowledgements

The editors thank the various Heads of Social Security in the region for facilitating this project. Special thanks are due to the Executive Director of the National Insurance Scheme of St. Vincent and the Grenadines and Coordinator of Sub-region IV, CISS.

The collection of readings has benefited from the editorial input of Prof. Carmelo Mesa-Lago and Prof. James Midgley. The main editors and the authors thank them for their many suggestions.

Introduction

The Caribbean context can be described as one where development is still in progress. While the external environment is changing in a way which poses many risks to the development process the internal environment is one where the demographics of the different countries present an independent set of challenges to the social security institutions of the region.

This collection is a response to the growing need to reexamine the operations of social security institutions in the Caribbean and covers a number of the issues related to these social security challenges. The issues have been categorized under the three subject areas of ***pensions, poverty and health*** with contributions being drawn from noted practitioners and researchers in the various areas. Although the papers do not all share the same philosophical perspective on social security, they all accept that there is an urgent need for reform. Of note also is that although the papers were put together more than four years ago the issues remain relevant today. In fact, it may be argued that the three subject areas identified are even more relevant and in need of urgent attention by both policy makers and researchers now.

In Chapter 1 - *Caribbean Social Security and the New Economic Order* – Karl Theodore makes the case for the rethinking of the role of Social Security (SS) in the region given the changing economic environment. The point is made that there is an explicit role for social security institutions in the development effort. Particular reference is made to the need for heightened awareness of the importance of the investment function of the social security institutions in this part of the globe. The objective of the investment function is grounded in the wider objective of the SS. Given this kind of perspective, the author is then able to make a clear case for reforms of the investment function of the SS to be seen as a fundamental component of the broader SS reforms as dictated by the changing national, regional and international landscape(s). Of note that, having reviewed the much-touted Chilean experience, the chapter ends with the suggestion that the development context and the social security history of the region do not lead to the conclusion that the Chilean experience is one that the region should try to emulate.

Chapter 2 - *The Harmonization of Social Security in the Caribbean* represents an attempt to come to terms with the new demands on the Social Security institutions. Wendell Samuel argues that the case for harmonization is even

more important now given the need to position the region securely on the international stage. Both as an integration instrument to yield efficiency gains and as a public finance instrument to enhance the human capital needs of the region, social security investments can probably do more for each country if a pooling arrangement is established. The special case of the Organisation of Eastern Caribbean States (OECS) with a common currency is a positive factor in this regard and some progress has already been made on the harmonization front.

Frank Alleyne presents us with an extremely well documented piece on the experience of the Barbados Pension system. In Chapter 3 - *The Evolution of Pensions Systems in Barbados: A Critical Appraisal* we are introduced to the case of a country continually reforming its pension system to cater to the changing needs of citizens. Of note is that this particular country seems to have made good use of the positive and negative experiences of other countries, especially Chile. The new pressures on the pay-as-you-go (PAYG) system have put Social Security reform on the table once more. There is now a need to clarify the role of the State given the emergence of the private sector role in pension provision.

Penelope Forde undertakes a discussion on occupational pensions in Chapter 4 - *Pension Arrangements in Trinidad and Tobago.* She observes that there has been enormous growth in these pensions between 1971 and 1992 and that the investment behaviour of pension managers of these occupational funds suggests a fairly high degree of conservatism. The chapter contains an interesting discussion of the legislative framework or the lack thereof. The case is made for general reforms in the regulations that govern these pensions.

Chapter 5 - *Social Protection and Poverty in the Commonwealth Caribbean* - addresses one of the main development problems of the Caribbean – poverty. In this chapter Ralph Henry discusses the notion of a safety net in a context where market forces are on the ascendancy. The chapter contains a clear statement on the evolution of social protection in the periods before and after colonialism. The major conclusion is that as presently conceived and developed, social security is not an effective protection against poverty for large sections of the population. A reformed social security system will need to take three factors on board: the vulnerability of these economies in the new international economic order; the gradual aging of the region's population; and the potential of the social security system to contribute to the development effort.

In Chapter 6 - *Social Insurance and Poverty Alleviation in a Developing Country: The Case of Trinidad and Tobago* Juliet Melville elaborates on the point made by Ralph Henry, in the specific context of Trinidad and Tobago. Melville begins with a recognition that assisting the poor was never really an explicit objective of the Social Insurance System. In fact, the evidence suggests that even in the basic area of coverage there is much to be desired. The problem of coverage is compounded by the policy of allowing the real value of social insurance benefits to fall over time. As presently constituted the National Insurance System of Trinidad and Tobago is "...irrelevant to the long-term poor and the new poor..." In a context where structural adjustment will be a feature of the country for the foreseeable future the case is made for reforms which address the twin issues of solvency and relevance of the social security system.

Chapter 7 - *The Inclusion of Health Under Social Security Coverage: Administrative, Financial and Economic Considerations* makes the case for extending coverage in a manner which reflects the understanding that social security contributors have basic needs which may call for an extension of coverage in these areas. In this chapter, Theodore and La Foucade discuss the three concerns that are likely to arise from such an extension: administrative, financial and economic. The three concerns relate mainly to the implementation of a system with universal coverage. Will such coverage of contributors' health needs be a manageable burden on social security systems? Will such coverage threaten the viability of the social security system? Finally, will such coverage negatively affect the savings and investment impact of social security in the region? The chapter argues that health coverage, appropriately designed and structured, will enhance the contribution of the social security system to the welfare of contributors.

Chapter 8 - *Financing Health Services Through Social Health Insurance: Lessons and Experience For Policy Makers* carries forward the discussion started by Theodore and La Foucade. In this chapter Stanley Lalta begins with a theoretical review of how individuals and societies respond to uncertainties. Lalta then makes the point that health must be seen as a special case. The chapter reviews the benefits that emanate from coverage of health services by means of a Social Health Insurance system and stresses the importance of design if the system is to ensure the provision of quality services at a cost that remains well under control. The chapter draws on the experience of a number of countries that have implemented these health insurance systems and

concludes that conditions in the Caribbean point to a successful adoption of this mechanism for financing health services.

CHAPTER 1

CARIBBEAN SOCIAL SECURITY AND THE NEW ECONOMIC ORDER

KARL THEODORE

Introduction

It has become almost axiomatic to state that since the onset of the international debt crisis in the early 1980s there has been a staggering pace of change in the economic system that links the countries of the world. The emergence of new trade blocs, the redirection of investment flows and the new conditionalities of financial flows have all combined to transform the environment within which developing countries like those in the Caribbean must now operate. In these circumstances it is not surprising the countries of the Caribbean would be seeking to redefine their own position in this new world order. At the same time the countries of the region will be under extreme pressure to ensure that the quality of life within our respective countries is worthy of being passed on to our children and grand children. In fact it is to this twin task of positioning ourselves in the world as well as enhancing the dignity of the life of the people within the Caribbean, that the opening quotation refers.

It is interesting to speculate whether with the new configuration of the international economic system Dr Eric Williams would have defined our task any differently. My own guess is that he would not. In fact, if we are to take a recent comment by one of the region's adopted scholars seriously, the novelty in the globalisation phenomenon is more one of form than one of substance - the hegemony of trade and finance over production has not really changed.[1] In these circumstances both the viability of the Caribbean countries and the quality of life of the people here would certainly remain the priority items on our development agenda. It is therefore this context of an outward vision with an inward focus which becomes the proper framework for considering the role of our Social Security institutions in this region.

Competing Conceptions of Social Security

For many years the dominant conception of social security was anchored in the notion of the Welfare State. Whether it was because of the enlightened self interest of the owners of capital or the altruistic concern of a string of social reformers the countries of Europe all came to adopt policies which sought to buffer the incomes of the employed classes from the risks inherent

[1] Professor Kari Levitt in an address to the Conference on Capitalism and Slavery held at the UWI, September 24th to 27th 1996.

in the very nature of employment. Essentially there were short term and long-term risks which had to be covered and these concerns were reflected in the nature of the social security institutions which developed. As documented in a recent UWI publication on social security we note that the social security institutions of the region have largely been the offspring of their European forerunners.[2]

More recently this 'welfarist' notion of social security has been challenged by Nicholas Barr who argues that social security, like any form of insurance, will only exist if it serves to make the production system operate more efficiently.[3] In particular, where the nature of the risk to be covered is dominated by considerations which will not make coverage attractive to private insurance carriers, it makes economic sense for the public sector to make arrangements for the insurance necessary. In plain language, if the level and the intensity of work effort are likely to be negatively affected if certain employment risks are not covered by insurance then social security comes into play not out of a *direct* concern with the welfare of the workers, but out of a concern for the stream of production.

It is important that we understand these different notions surrounding the rationale for social security since in the new dispensation it is our attitude to these notions which will guide both our interpretation of social security experience elsewhere as well as our approach to policy reforms in the Caribbean.

Three Questions to be Answered

There is no doubt that the greatest threat to the integrity of social schemes in the Caribbean is in respect of their capacity to fulfil their promise of decent pensions to their current contributors. Since this paper is being written from an economic perspective there are at least two questions which must be addressed:

---

[2] La Foucade, Althea, A Review of the Evolution and Performance of Social Security Schemes in the English-Speaking Caribbean.

[3] Barr, Nicolas, (1990). "Social Insurance as an Effiency Device." Journal of Public Policy 58-59.

- Is there a valid *economic* explanation for the pension difficulties which now threaten the social security systems of the Caribbean?
- If such an explanation exists, what then must be the *guiding principle* of the reform imperative facing the social security institutions of the region? That, if anything, can the Caribbean learn from *the Chilean experience* as we seek to keep our own social security systems from going under?

Pensions and the Economic System

There are at least three reasons why modern economic systems can be thought of as not being naturally supportive of the maintenance of social security systems, in general, and of pension funds, in particular:

- the secular tendency for prices to rise;
- the tendency of modern technology to modify the formal structure of the labour market;
- the perception of pension funds having a relatively low opportunity cost.

The threat posed by inflation is well known. Rising prices chisel away at the value of any accumulated financial assets thereby reducing their potential to be converted into actual consumption at a future date. It is not uncommon for social security systems to report very low or even negative real yields on their investments. What this means is that these investments are making no meaningful contribution to future consumption potential.

In one sense this is a no-win game for contributors to pension funds. To the extent that it is workers' demand pressures that keep prices rising, to that extent workers are contributing to the demise of their pensions. On the other hand, to the extent that it is workers' demand pressure that keeps employment levels from falling, the reduction of such pressure will be detrimental to the income base from which the pensions are being accumulated. In the absence of any natural tendency for the correct amount of demand pressure to be maintained it will be in the interest of any pension agency to acquire some influence over the active management of aggregate demand. We will return to this point later.

On the question of modern technology the situation here is also one where we seem to be between a rock and a hard place. On the one hand, it is well

understood that the only sustainable countervailing force where inflation is concerned is *increasing productivity*. Moreover, as Arthur Lewis first told us, the only basis of increasing incomes through international trade is improving the quality of the labour input that goes into the production of the traded goods and services. These pressures to counteract inflation and to keep incomes rising have contributed to the development of technologies which on the one hand tend to reduce the growth of labour demand, and which, on the other hand, tend to make it possible for more people to be productive outside of the traditional formal section of the labour market. This rise in informal employment has heightened the compliance problems faced by all social security agencies, thereby weakening the effective base on which pensions might be built.

Finally is the matter of the low-cost perception of pension funds. Since, by definition, pension funds will not be called upon for a long period of time there is a tendency to see them as being available to:

- smooth out current consumption streams;
- provide liquidity to capital markets that may be in pressing need of short term money;
- uphold that part of the capital market where the links with the real sector may be extremely tenuous.

With respect to the use of pension funds for current consumption activities perhaps the major player here has been the government. It is well known that governments have tended to use social security long-term funds to cover current fiscal deficits caused by expenditures which are purely of a consumption nature. This is a concern that has been documented by Samuel (1985) in the context of the Eastern Caribbean countries, and by but La Foucade (1995) in respect of the wider Caribbean, but the phenomenon of so-called "government raiding" is not limited to this part of the world. In fact Angus Deaton (1989) has argued that the lower the level of income of a country and the higher the level of uncertainty surrounding the income stream, the more likely it is that savings like pension funds will be used for smoothing out of the income flows. This means that in the Caribbean where the major income flows are sourced from exports of agricultural or mineral products in relatively volatile markets, it is perhaps not surprising that the governments have felt the need to access social security funds to make ends meet.

The use of pension funds to supplement the short term needs of the capital market or even to provide the wherewithal to bring such a market into being has been discussed by Holzmann (1995) in the context of the Latin American experience. In any case, given the fact that money is fungible, the known availability of pension funds for long term lending by finance institutions, means that these institutions are in a better position to also engage in their short term lending activities.

The perception that pension funds are essentially low-cost funds would seem to be part of the explanation of their use in relatively low-yielding portfolios. What is probably more important is the fact that pension funds are seen as part of the broader financial intermediation process which is supposed to link the financial sector with the real sector. The point here is that for some reason these funds are not usually treated in the same manner as retained earnings like depreciation allowances, for example, which are regarded as being very close to the decision making about production. Since, in a sense pension fund contributions are as much a part of surplus from current production as are depreciation allowances, their limited use to finance the strengthening of the productive process is probably a major cause of their vulnerability.

In summary, the point being made is that the economic system does not naturally foster the growth and sustainability of pension funds. It is probably not even neutral to these funds. What this means is that a very specific strategy must be in place to enhance the growth and survival of these funds. It is to this strategy we turn in the next section of the presentation.

An Economic Strategy for Pension Funds

Since it would seem that the economy itself may be hostile to the survival of pension funds there are two options open to pension fund managers. Either the funds must be protected by an appropriate system of buffers or the funds must themselves become major influences on the normal operations of the economy. It may be argued that the attempts by some countries to introduce some form of indexation for pension funds is by way of erecting a buffering system against inflation. It could also be argued that the call to privatise pension funds is really an attempt to put these funds out of the reach of fiscally-troubled governments.

In his review of the pension reform efforts in Latin America, Mesa-Lago has identified *four* types of reform:

- *reform of public schemes*, as in Costa Rica, where the retirement age was increased, the contribution rate was increased, evasion-reducing measures were introduced and administration of the scheme was made more cost-efficient;
- *introduction of purely private schemes*, as in Chile where the public *Cajas de Prevision* established since 1924 were replaced in 1981 by Administradoras de Fondos de Pensiones, AFPs, which are in fact private financial corporations;
- mixed schemes, as in Argentina and Uruguay, where the public schemes have been reformed, and provide a basic pension, but where there are supplementary pension schemes managed by public, or private non-profit institutions;
- *supplementary pension schemes*, as in Ecuador and Mexico, where there is an attempt to complement the pension of the general public scheme with separate contracts for particular groups of contributors administered by quasi-public agencies or private non-profit agencies, or even private profit-making bodies.

What all of these reform attempts have in common is their reliance on the buffering strategy. The essential feature of this strategy is the fact that the behaviour of key economic variables are taken as given and the reforms advocated are mainly in the form of administrative or managerial adjustments. Missing from this strategy is an attempt to identify a set of economic incentives which might work in favour of more directly strengthening the pension funds.

By now it should be clear that this paper will be proposing an alternative strategy - a proactive strategy of making public use of those private interests which motivate economic agents to behave in fairly predictable ways. In this context, we can identify three sets of agents:

- contributors to the pension funds,
- the government, and
- contestable pension fund investors.

We also keep in mind that in respect of pension funds there are three clear objectives:

- to maximize the real value of the fund;
- to minimize the cost of administering the fund, and;
- to ensure full access to, and an equitable distribution of the fund.

In respect of the first of these objectives - the maximization of the value of the fund there are a few necessary conditions:

- constrained maximization of the base of the fund, in particular the number of active contributors, and the effective rate of contribution;
- constrained minimization of the rate of inflation;
- constrained minimization of the incidence of "raiding" on the one hand, and political "overloading" on the other.

We include the term 'constrained' in each case in order to emphasize that for each of the conditions mentioned there would be a trade-off which at least one of the economic agents will have to come to terms with. In the case of the effective contribution rate, for example, the understanding here is that, on the one hand, there would be some politically acceptable limit to raising the contribution rates, while on the other the business of maximizing the rate of compliance is certainly not without its own cost.

Similarly, in respect of the rate of inflation, there would obviously be some level of unemployment above which the pension fund will itself be in serious difficulty. On the question of "raiding", the fact remains that in some circumstances government use of social security funds may be the socially minimum cost method of dealing with a fiscal deficit. In these circumstances the task would be to determine the appropriate cost of the borrowing and to provide an incentive for the proper repayment - the foregoing of future taxes on pensioners' incomes, for example.

The principle of Ricardian Equivalence tells us that there would be no negative growth effects on the economy if the public expenditures incurred today do not imply higher tax burdens in the future. In this context, governments should only spend today what they expect to be covered by future growth in the economy, the rate of taxation assumed to be unchanged. Similarly the limits on government borrowing from the pension funds should be set by the expected tax inflows from the fund over a period of time.

Finally, the problem of political "overload" is well known. In this case, parties vying for election compete in the extravagance of the promise made in relation to increasing social security benefits, most often with no adjustment in contributions.

In respect of the rate of inflation we probably have the best opportunity for demonstrating the value of the approach being suggested for the social security schemes - namely, active involvement of the schemes in expanding the level of domestic production of key items, as well as active involvement in the management of aggregate demand. Mesa-Lago [1994] was on the right track when he stated that

> *Adequate socioeconomic policies of a general nature would provide a sounder financial base for social security.....[and] Instead of* ***passively*** *(my emphasis) waiting for a miraculous economic recuperation, social security should actively seek to alleviate the social costs of adjustment and restructuring, particularly among the most affected vulnerable groups.*

Taking this approach to its logical conclusion would require the social security agencies to contribute to the "economic recuperation" to which Mesa-Lago refers. This would require the social security agencies to target certain critical sectors of the economy for special attention. For example, the agricultural sector, the housing sector and the transportation sector are ones where price movements have a major impact, partly because of the ripple effects on the other sectors of the economy. In these circumstances, and particularly, in the context of the small economies of the Caribbean, the opportunity is there for the social security agencies to influence the level of domestic production in each of the three mentioned sectors.

One option would be to engage, on a competitive basis, the services of existing or contestable producers in these sectors to provide targeted increases in output. The provision of low cost funds in these circumstances will not only have the direct impact on output expansion, but by thereby counteracting the tendency of prices to rise, the social security agencies would be contributing to the protection of the value of their contributors' pensions. The history of social security systems elsewhere has shown that mere legislation cannot protect the value of pensions from the ravages of a weakening economy. The intention behind indexation, for example, is no doubt a good one, but if the

level of real output in the economy does not make the indexation feasible, all that will happen is an accumulation of debt to pensioners - debt which they may never live to see repaid.

There is no doubt that this suggestion might be a difficult one for social security managers to swallow. However, in this case the importance of a public education programme, as indicated by Mesa-Lago (1994) cannot be over-emphasized. It would be instructive, for example, for social security managers to be exposed to the details of how the Indonesian Co-operative Movement within a period of five years turned that country from being an importer of their crucial staple, rice, into being a surplus producer of that commodity.

In closing this section it might be helpful to identify a few of the incentives that might be offered to the different actors whose behaviour can have some influence on the size and value of the pension funds. In the table below we summarize these incentives.

Table 1.1 - Key Economic Agents: Objectives and Incentives

Objectives	Contributors	Government	Contestables
Fund, value maximization	Reduced rates on full period compliance; creeping movement in retirement age	Use Fund to expand tax base; allow tax authorities to benefit from SS compliance system; SS to adopt select welfare programs	SS to employ private managers to carry out certain investment activities, including targeted output expansion
Administration - cost minimization	Apply multiple registration penalty;	----------	Engage private agencies to perform compliance and claims processing functions
Equitable Distribution of contributions and benefits	Remove income ceilings, adopt sliding rates above certain level of income	Wholly or partially adopt targeted training and income support programs	----------

In proposing these incentives the intention is to reduce the extent of administrative controls required to attain certain economic outcomes, in terms of both efficiency and equity.

There is no doubt that the different social security schemes in the region have always been concerned with making a greater impact on the quality of life of their contributors over and beyond the eventual pension that will arise. However, the legislative framework within which these systems operate really does not give much room for initiative or flexibility. In the name of protecting the public interest the limits placed on the investment activities of the social security systems do not give much scope for engaging in the kinds of activities suggested by the set of incentives listed.

In this context, the first order of business therefore is for the Social Security Boards of the region to get the Ministers responsible to initiate the process of changing the legislation to give them the flexibility they will need. This is a process which should be set in train in time for the next meeting of the OECS Policy Board and the next meeting of the CARICOM Heads of Government. Since what is being proposed is essentially a Caribbean approach to dealing with the threat facing our social security systems it will be necessary to combine the technical services of CIESS with those of the University of the West Indies in coming up with the set of proposals which the Ministers will need to consider. To better motivate the preparatory steps that must be taken, the regional representatives should be arrange for CIESS to declare 1997 as the Year of Social Security Reform in the Caribbean. Time is not on our side.

Having indicated the flavour of the reform strategy that would be relevant to the Caribbean it would be useful to review the now famous Chilean social security reforms and to determine the extent to which the Caribbean may benefit from adopting the Chilean model. This is a very serious question for us at this time since the major international financial institutions to which many of our countries are now tied in one way or another have made no secret of the fact that, as far as they are concerned, the Chilean model is the preferred option.

Chilean Social Security Reform with Lessons for the Caribbean

In developing this section there are five questions which will be addressed. These relate to:

1. The evolution of the Chilean social security system before the 1981 reforms;
2. The nature of the problems emerging before 1981 and the attempts made to deal with them;
3. The essence of the 1981 reforms;
4. The performance of the new system to date and prospects for the future, and;
5. The lessons for the Caribbean.

Evolution of the Chilean Social Security System

According the Mesa-Lago [1994] when the Chilean Social Security system was established in 1924 it was the first of its kind in this part of the world. At that time three mandatory programs were created: one for industrial workers, one for public employees and one for office employees. In the beginning these *Cajas de Prevision* ("Foresight Chests") enrolled only workers who earned below a certain level of income. By 1973, however, many more *cajas* were established and by that time more than 75 percent of the workers in Chile enjoyed some form of social security coverage.

The system operated under a government mandate with workers, employees and the government making contributions to the funding of the system. Moreover, while it is true that benefits were linked to the salary of workers, it has been argued that

> *redistribution occurred from higher to lower paid employees, since low-income workers received more in pensions than they had paid in.....*(also) *Workers received small wage supplements according to the number of their children, and women could retire with fewer years of payment into the system...*[Collins and Lear, 1994]

As part of the benefits provided it should be noted that the cajas owned hospitals and recreational centres to which all contributors had access and the pension funds were used to provide low-cost housing loans to affiliates.

Emerging Problems

By the early 1970s it became evident that serious problems had already emerged. The distribution of workers in the *cajas* was very uneven, with 90 percent of workers covered by three *cajas*, with the remaining ten being covered by 35 *cajas*. One implication of this was that the benefits were also fairly unevenly distributed. There were glaring inequalities between white-collar and blue-collar workers, for example. The former could retire with benefits equal to their full salary with only thirty years of service. Factory workers and others similarly placed, qualified for this benefit only after reaching the legal age of retirement (sixty-five for men and sixty for women). There were also collusion problems in the way benefits were calculated.

Apart from these problems, it was obvious that the cost of social security was simply becoming too burdensome. By 1973 the combined contributions of workers and their employers was as high as 66 percent of the wages paid. In spite of this, partly due to inflation, there were frequent instances of insufficient resources to pay out benefits. In these circumstances the government made the necessary payments.

Compounding these problems was a very serious compliance situation, especially in respect of manual workers. It has been noted that

> *Many workers and employees knowingly did not pay contributions - or else paid them on a much lower wage than actually received - because the minimum pension would be paid regardless of the level of salary on which contributions were paid.* [Myers, 1992]

Although many previous governments had noted and studied the problems it was not until the Pinochet government that certain reforms were implemented. There was a general move in the direction of uniformity of benefits, regardless of the *caja* to which individuals belonged. Another major change was first the reduction in the employer contribution and then its eventual elimination by 1980.

The 1981 Reforms

The essential characteristic of the reformed social security system was the virtual abolition of its "social" nature. The system was in effect privatized. In other words, instead of one public agency there were now a number of private Pension Fund Administrators (AFPs) which competed for employee retirement withholdings. The sole business of these AFPs was the management of the individual retirement accounts of the workers. By mid 1995 there were 22 of these private profit-making pension fund administrative companies. Workers "affiliate" with these AFPs and an individual annuity account is established for each worker. On retirement the worker could then choose to make programmed withdrawals from his/her accumulated funds or to exchange the accumulated balance for an annuity paid by an insurance company.

It was mandatory for all new workers to have one of these individual accounts. Workers belonging to existing *cajas* were given the option of remaining with their present arrangement or switching to the new system. There were clear incentives in taking the latter course of action. Two, in particular are worth mentioning. First of all, for those who switched to the new system the government provided a "recognition bond" which would collect interest and be added to their new AFP funds on retirement. The amount of the bond depended on the length of time the worker had contributed to his/her *caja*. The second major inducement was effectively lower contribution rate applied to those who switched to the new system. While for new workers the rate ranged between 26 to 31 percent of the paycheck, for switching workers the amount retained was only 21 percent.

There are three notable features of the new system.

- The first is that employers made no contributions to the workers' AFP accounts.
- The second is that the privatized system excludes the armed forces and the national police. The *cajas* for these two groups are still very much in existence.
- The third is that the new system is supported by a government-guaranteed minimum pension for insured workers with at least twenty years of contributions, but whose AFP pension falls below a certain level.

Performance of the New System

Coverage

Coverage under the new system has expanded rapidly - from close to 50% of the labour force in 1981 to almost 80% by 1990. Those not covered include:

- the military;
- the self-employed, whose participation is voluntary and who mostly do not register;
- those workers who have remained under the old system - many of whom are close to retirement;
- workers whose participation is mandatory, but who do not, for example, domestic workers

Financial Performance

The financial performance of the new system has been staggering. The Table below illustrates. By 1990 the volume of assets in the hands of the AFPs had risen by a factor of 33, to a level of $US 9.2 billion. Compared to the assets of the entire banking system this was a share of almost 25%, rising from a mere 6% in 1986. It was also close to 25% of the GDP, rising from just over 12% in 1986. By 1994 the level of the funds stood at $US 22.7 billion, more than 80 times its starting value, and was now more than 40% of the GDP.

The growth of the funds shows that, excluding the initial 1982 figure, over each of the three four-year periods, the average performance has been commendable:

- 1983 - 1986 : 45.68%
- 1987 - 1990 : 25.16%
- 1991 - 1994 : 25.61%

Table 1.2 - Pension Fund Performance in Chile (1981 - 1995)

Year	$US billions[a]	Percentage of GDP	Growth Rate (%)
1981	0.28	0.86	-
1982	0.87	3.36	215.12
1983	1.58	5.97	81.62
1984	2.06	7.88	30.38
1985	2.88	10.22	39.69
1986	3.78	12.48	31.04
1987	4.63	14.49	22.49
1988	5.64	15.39	21.94
1989	6.97	18.46	23.59
1990	9.24	24.73	32.61
1991	13.08	32.17	41.53
1992	14.59	32.24	11.50
1993	18.74	39.39	28.50
1994	22.67	41.18	20.91
March 1995	22.08	-	-2.59

Source: Bustamante Jeraldo (1995), quoted in Sebastian Edwards (1996).
[a]March 1995 dollars.

Structure and Yield of Investments

The investment portfolio of the AFPs shows a predominance of government bonds. The Table below shows that 44.1% of the portfolio was in these bonds with common stocks accounting for only 11.3%.

Table 1.3 - Structure of Investment Portfolio, 1990

Type of Investment	Proportion, %
Government-Guaranteed Investments (Treasury or Central Bank)	44.1
Time Deposits (Commercial Banks)	17.4
Mortgage Bonds	16.1
Common Stocks	11.3
Bonds and Debentures	11.1
Total	**100.0**

The table below shows the yield on the AFP accounts compared to that of the entire financial system.

Table 1.4 - Annual Real Rates of Return on AFP Accounts and on the Financial System (Percentages, 1981 - 1990)

Year	AFPs	Financial System
1981	5.3	13.2
1982	25.5	12.1
1983	19.4	7.8
1984	2.4	8.4
1985	11.6	8.2
1986	10.9	4.1
1987	4.5	4.3
1988	6.1	4.6
1989	6.7	6.8
1990	15.7	9.4
Average 1981-1990	**10.4**	**7.8**

Source: IMF, based on data provided by Chilean authorities; quoted in Sebastian Edwards (1996).

Quite clearly the AFPs have been performing on average better than the rest of the financial system.

Benefits under The Old and New Systems

In the Table below we compare the number of pensioners and the value of pensions in the old and the new systems, as at September 1990.

Table 1.5 - Comparison of Pensions and Pensioners under the New and Old Systems

Type of Pension	NEW SYSTEM		OLD SYSTEM	
	No. of Pensioners	Average Pension (pesos)	No. of Pensioners	Average Pension (pesos)
Old Age	26,393	36,047	366,378	35,746
Disability	15,369	59,403	132,886	29,519
Widow	16,310	25,784	167,097	17,925
Orphan	21,593	8,766	36,469	6,749
Total	**79,665**	**N.A.**	**702,830**	**N.A.**

Source: Robert Myers (1992)

Not surprisingly, the number of pensioners under the new system is considerably less than under the old system - about nine times less. Clearly the new system is yet to reach its maturity. It is noticeable that the average old-age pension is roughly the same under both schemes. However, the difference in disability pensions is quite remarkable - almost twice as large under the new system. This is manly a result of indexation. Pensions for widows and orphans are also significantly higher - 44% and 30%, respectively - under the new system.

Administration - Structure and Costs

By 1990 the distribution of contributors seemed to match that of the assets, with the three largest AFPs (Habitat, Provida and Santa Maria) accounting for 62.4% of the assets and 66.2% of the active contributors.

In December 1990 the average operational cost of maintaining an AFP account was 10,232 pesos ($US 31). This amounted to an expense rate of just over 10% of the retirement benefits paid out. This 1990 figures compares with a 1981-82 figure of close to 15,000 pesos. Putting it a little differently we can say that out of the contribution rate of 10% for retirement benefits, administrative expenses accounted for 1.5%, that is 15% of the contributions.

Lessons for the Caribbean

In the light of the tremendous impact which the Chilean social security reforms have had on the imagination of many policy makers and policy advisers in this part of the world it may be useful to begin this section with a few comments from a wide range of scholars and commentators. Perhaps it is instructive to lead off with a few comments from Robert Myers,[4] a great admirer of the Chilean system:

> *In summary, the new system - both as to its design and to its performance - is excellent..... Further the new system desirably contains significant elements of social adequacy in addition to those of individual equity. However, this is not to say that the program is without problems....*[Myers, 1992]

What are these problems that Myers refers to, and what are his views on the suggestion that the Chilean approach should be adopted even in the United States? Myers refers to five problems:

1. Although the new system has led to improvements in the coverage of workers, there still remains a problem of compliance which will have to be addressed;

---

[4] Myers has served as chairman, Commission on Railroad Retirement Reform, 1988 - 90; executive director, National Commission on Social Security Reform, 1982-1983; deputy commissioner, Social Security Administration, 1981-1982; member, National Commission on Social Security, 1979-1981; chief actuary, Social Security Administration, 1947-1970. He is now professor emeritus at Temple University.

2. There is still some doubt about what will be the eventual level of retirement pensions" - the expectation that the goal of 70% of salary could be delivered on the basis of a 10% contribution rate is open to "considerable question";
3. The flat charge for administering the AFPs is clearly disadvantageous on a cumulative basis to lower income workers.
4. The expectation that the new system will greatly increase private savings is probably without good foundation.

> *So much depends on what happens in the other sectors of the economy that it is impossible to give any accurate answer on the effect of the new system of private saving.*

5. Finally, Myers points to the fact that

> *A considerable amount of government debt will be created in the future for meeting the deficits of the old system and for payment of the bonos (the recognition bonds.)*

Although Myers acknowledges that "the investment of even a small portion of the assets of the AFPs in the private sector will have the desired stimulating effect." He does not advocate such a move by the new system. As far as he is concerned

> *The principal advantage of the new system in the general economic picture is,...., the* ***psychological*** *(emphasis, mine) one of persons feeling that a considerable amount of money that is indexed against inflation is all theirs.*

In these circumstances Myers is firm in his view that the Chilean model has no applicability to the United States. This is mainly because relatively little of the financing of the US system comes from general revenues. Such financing, in his opinion is

> *highly undesirable" and "the necessary funds should be derived in a visible, direct manner from payroll taxes on workers and employers. What must be realized is that " a privatized, individual account system cannot 'guarantee' either the future investment rate of return of the accounts or how much pension an individual unit of account will purchase.*

Far from recommending the Chilean privatization route for the US, Myers reminds his readers that "a social insurance system is flexible and, if financial difficulties arise in the future, appropriate (and probably small) adjustments in contribution rates and/or benefit provisions can easily be made to rectify the situation."

Other commentators have also expressed both praise and reservations about the Chilean reformed system. MIT's Peter Diamond, another guru on social security in the United States commends the Chilean reforms for

> *defending the system from political risk.....Since legislating a benefit formula can lead to a program that is not viable in the long run, there is real appeal in individual accounts as insulation of the pension system from political actions to increase benefits without direct financing. The Chilean system gets high marks on this dimension...*[Diamond, 1995]

However, Diamond is not selling Chile as an example to any one:

> *"it is also important to recognize that it is not easy to imitate Chile - it requires hard work at regulation and political discipline so that such a reform doesn't unravel in either private or public raiding of accumulated funds.....Thus whether to go the Chilean route and how closely to imitate the Chilean details are questions best answered separately on a country-by-country basis."*[ibid.]

This slew of comments on the Chilean reforms will be incomplete without the voice of the region's leading scholar on social security, Carmelo Mesa-Lago. The position taken by Mesa-Lago is not inconsistent with that of the other scholars mentioned. The reforms, in his view, have brought gains and losses to each of the three major participants: workers, employers and the government. Workers have gained from

> *lower payroll contributions, a higher level of benefits (so far), freedom of choice concerning AFPs and retirement plans, the recognition of previous contributions, eligibility for a minimum pension, a sounder pension program with state guarantees, high investment yields and faster and simpler processing of pensions.* [Mesa-Lago, 1994]

They have lost in terms of

> *the decline in coverage (when coverage is measured based on active contributors), the payment of commissions to the AFPs, poor information concerning what percentage of contributions goes to commissions (at least until recently), restrictions against using the accumulated fund until the time of retirement, lack of knowledge on crucial issues and decisions, and the elimination of the employers' contribution.*[ibid.]

This latter point turns out to be the main advantage to the employers and a major cost to the government which now would single-handedly have to provide the required subsidies. The economic risks of the reforms now rest squarely with the state and as far as the society as a whole is concerned

> *There is no evidence that the capitalization system has generated higher national savings.*

Mesa-Lago believes that there are several lessons to be drawn from the Chilean experience. The first is that the cost of maintaining the humane dimension of the system is a very high one. Reference here is to the burden of the recognition bonds and the establishment of minimum pensions. These costs have to be balanced against alternative means of protecting the lower income groups in the society. The second lesson is

> *that the presence of a market and private administrators does not necessarily ensure competition, control evasion and payment delays, and promote other efficiency improvements.*[ibid.]

Finally, the fact that a significant part of the population (the armed forces) is not yet in the same boat as the rest of the workers, maintaining their privileged conditions and benefits, could turn out to be

> *a salient inequality that must be eradicated.* [ibid.]

It is instructive that Mesa-Lago does not anywhere suggest that the Chilean experience amounts to a model for other countries. Peru for a long time has been the only country to date which has adopted the model and this elicited no comment of surprise from Mesa-Lago. More recently Colombia has adopted a variant of the model.

Other Comments

We stated earlier that the international financial institutions are favourably disposed to the Chilean model. Even in this case, however, there is a serious note of caution. An Inter-American Development Bank (IDB) Newsletter had the following to say:

> *Despite (an) impressive list of accomplishments and advantages, the Chilean model is not appropriate in the absence of certain preconditions. A reasonably functioning financial system must offer a diversified basket of financial assets to invest in.....This condition, in turn,requires macroeconomic stability, market-determined interest rates,and proper proper regulation and supervision of both the financial and the pension systems.* [IDB, 1993]

In another document the Bank expressed unambiguous caution in respect of the future of the Chilean system:

> *There is no evidence to suggest that the new system will be able to pay higher pensions than the old one.....the estimates concerning pensions to be paid in future by the capitalization system are based on simulations whose basic assumptions do not necessarily reflect the reality of the entire system.*

Moreover, although the Bank agrees that the radical overhaul of the Chilean system presents a great opportunity for protecting the system against the indiscriminate granting of politically motivated benefits it goes on to say that

> *Nevertheless, a private capitalization system is not entirely immune from this temptation. Through Acknowledgement Bonds, the amendment of rules governing retirement, and the eligibility requirements for minimum pensions, it is possible for a government to achieve political goals and to generate economic costs similar to those of a State-administered pay-as-you-go system.*

For its part, the World Bank is usually more effusive in its praise of the Chilean model. Yet, one of its commentators shares the IDB's concern about the new system's immunity from political influence. Moreover it is acknowledged that

> *A major criticism of the Chilean model centers on its capacity to provide poverty alleviation given the low level of the minimum pension and the 20-year contribution requirement, which maybe unattainable for many workers owing to irregular contribution periods....*[Queisser, 1995]

Chile and Caribbean Social Security Reforms

There is no doubt, as Myers (1992) has indicated, that Chile " fired a shot that was heard around the entire social security world" and that the "shot" is still being heard. However, from the several comments we have reviewed, perhaps the single most telling lesson is that there is nothing about the Chile experience which singles it out as the preferred model for the countries of the Caribbean, or for any other country. It is interesting to note that the praises for the new system were in terms of its *psychological* impact and its *political* advantages. Apart from its focus on the risk of being "raided", the Chilean model has not really addressed the basic problem to which we have already referred - the apparent natural hostility of the economy for social security systems. All commentators have pointed to the vulnerability of the new system to developments in the economy.

As we have seen, when it came to the crux of the matter, one of the leading social security experts in the United States reduced the reform imperative to getting the actuarial balances right. It has also been pointed out that one of the advantages of the Chilean system is in the flexibility that now built in as far as making adjustments are concerned. However, we have also seen that this flexibility has not been attained without a price and without an enduring risk of political influence. It would therefore be wrong to conclude that this flexibility provides the best guarantee of securing the value of the funds accumulated over time.

In this context we at the UWI are making the point that there are really two reform options available to us in the Caribbean. One option essentially addresses the arithmetic of the social security system. By a series of possible adjustments to the present system this approach will deliver the degree of security required if the economic conditions are favourable enough. The other option - the one we are proposing - focuses on the algebra of the social security system. In other words, this second option seeks to come to terms with the many "unknowns" which conspire to threaten the viability of the system. Since

these are essentially related to a combination of economic management and economic influence, the UWI recommendation is for the Caribbean to move in the direction of an economically proactive social security system. Except the social security systems begin to use the potentially considerable economic muscle they possess, and use it in a manner which influences the national economic outcomes, they will never be able to provide the security which workers believe they are presently contributing towards.

In our view, this goes way beyond what Chile has done. And yet, accepting this way of looking at the social security reform imperative is in the nature of taking another small step which could amount to a great leap for mankind.

References

Collins, Joseph and John Lear (1993), "Chile's Free Market Miracle: A Second Look," The Institute for Food and Development Policy, Oakland California.

Diamond, Peter (1995), "Privatization of Social Security: Lessons from Chile," An Address to the Seventh Annual Conference of the National Academy of Social Insurance, Washington.

_____ (1996), "Proposals to Restructure Social Security," *Journal of Economic Perspectives*, Vol. 10 No. 3, pp 67-88.

Edwards, Sebastian (1996), "The Chilean Pension Reform: A Pioneering Program," Delivered at the NBER Conference on Social Security, Cambridge.

Holzmann, Robert (1995), "Pension Reform, Financial Market Development and Endogenous Growth: Preliminary Evidence from Chile?", IMF Research Department Seminar.

Inter-American Development Bank (1993), "Social Security Reform in Latin America," A note by Glenn Westley in *Development Policy*, Newsletter on Policy Research. Washington.

Marcel, Mario and Alberto Arenas (1992), "Social Security Reform in Chile," An Occasional Paper of the IDB, No 5, Washington.

Mesa-Lago, Carmelo (1994), *Changing Social Security in Latin America, Toward Alleviating the Social Costs of Economic Reform*, Lynne Rienner Publishers, Boulder and London.

Myers, Robert J. (1992), "Chile's Social Security Reform, After Ten Years", *Benefits Quarterly*, Third Quarter, pp 41-55.

Rix, Sara E. (1995), "Chile's Experience with the Privatization of Social Security," *Public Policy Institute*, Washington.

Queisser, Monika (1995), "Chile and Beyond: The Second-generation Pension Reforms in Latin America", *International Social Security Review*, Volume 48, No. 3.

CHAPTER 2

THE HARMONIZATION OF SOCIAL SECURITY IN THE CARIBBEAN

WENDELL A. SAMUEL

Introduction

The United Nations Conference on Social Development held in Copenhagen has brought renewed focus on the social dimension of economic relations of which social security is but one element. At the same time, the decision of the CARICOM Heads of Governments to allow graduates of the University of the West Indies and University of the Virgin Islands to work and settle in any territory as a precursor to free movement of labour raises questions about the elaboration of a social policy at the regional level. The limited free movement of labour increases the urgency for the CARICOM countries to implement the reciprocal agreement between the Social Security Schemes to which most of the countries are signatories but is still to be operationalized. Moreover, the eventual free movement of labour requires that the policy makers revisit the basis for the agreement to determine its adequacy in these new circumstances. This paper hopes to make a contribution to the clarification of some of the issues involved in the harmonization of Social Security Schemes in the CARICOM countries.

The harmonization of social security can be interpreted in its strictest form as the centralization of the administration of the social security schemes under a regional administration. At the minimum, it would involve a set of measures adopted by the disparate national administrations to ensure the portability of benefits of migrant workers in the CARICOM region. The outcome which emerges would strike a delicate balance between national preferences and national considerations which exert a tendency for cumulative divergence, and the efficiency gains from centralization which creates pressures for greater harmonization.

The theoretical underpinnings of the harmonization of social security are woven from two different strands of economic literature. The first is the literature on Economic Integration which stresses the microeconomic efficiency gains which may result from the removal of restrictions to the movement of labour as developed by Balassa (1961), Meade (1959), Ohlin (1961) etc. The second, is the literature on Fiscal Federalism which addresses the optimal spatial provision of public goods [Musgrave (1969), Olson (1969) and Oates (1972)]. Both strands of literature require some very strict conditions for centralization to be the optimal solution, hence the real world is more likely to lie between the extremes defined above.

Section I of the paper addresses the theoretical considerations in the harmonization of social security which arise from the economic integration literature. The contribution of the fiscal federalism literature to the understanding of the allocation of governmental functions within an intermediate integration movement is discussed in Section II. In Section III the desirability and feasibility of harmonization of CARICOM social security schemes is discussed with reference to the Social Security Reciprocal Agreement. This section of the paper also enquires whether there is a case for closer harmonization of social security arrangements in the OECS countries given the existence of a *de facto* currency union. The final section consists of some concluding remarks and suggestions for further research.

Internal Market Efficiency and Harmonization

The microeconomic efficiency argument for harmonization is based on the notion that differences in national social security arrangements would create distortions in the internal market of the integration movement and may result in trade diversion or factor movements which are not consistent with the configuration dictated by comparative advantage. In particular, countries with low social security benefits and countries in which social security is financed by general taxation would have a locational advantage over countries with high social security benefits partly financed by employers' contributions. This perverse movement of labour in reaction to differentials in social security arrangements is called social dumping. The argument continues that since the efficient functioning of the internal market is a collective good then social security should be centrally regulated.

Market efficiency requires equality between prices, marginal social values and marginal social costs. Distortions to these relations created by national differences in social security diminish the gains from international trade. On the surface, this argument seems quite convincing but a closer examination suggests that centralization may not be a logical conclusion due to the fact that, from the point of view of the firm, wages and contributions are both components of labour costs. Hence, international comparisons of labour costs must not be based only on any individual component but on wages and other social charges taken together (Balassa (1961), p. 217).

Flexible Exchange Rates

To facilitate the analysis, assume that there is a fully integrated market for goods and services, factors are immobile internationally, social security arrangements differ in terms of their financing methods and/or the level of financing, and exchange rates are flexible. If prices and wages are also flexible and employees consider the employers' contribution as part of their wages, then different levels of contributions across countries do not affect relative wage levels. On the other hand, if contracted wages do not fall, a rise in contributions may affect relative wages in the short run, but this would be corrected by an adjustment in the exchange rate. Even if prices and wages are characterized by downward inflexibility, the contributions would eventually be shifted to the employees as opportunities to do so develop with the passage of time (Balassa (1961), p. 220). Similar conclusions flow from the analysis when contributions are paid by employees. Similarly, the finance of social security by general taxation does not necessarily affect wage cost, but if it does, equilibrium can be restored by exchange rate adjustment.

The implications of the above are: (1) there is no need for exante harmonization of the level and method of finance of social security schemes, except in the case of non-general social security arrangements does a case exist. (2) Balassa (1961), p. 220, concludes since contributions imposed in the past may have already been absorbed in the cost structure of the individual countries, harmonization may in fact disturb the existing cost relations. (3) Social security contributions is but one of the contributory factors to competitiveness of a country and over time, differences in social security arrangements can be offset by changes in the other factors.

The interdependence of the elements of labour costs was illustrated by Petersen (1991), who found that in the European Union there was a tendency for wages for time worked being lower in countries with comparatively high indirect labour costs per working hour. He concluded that, "if wages corrected for differences in productivity and social security arrangements were harmonized up to the level of high benefit countries, the comparative cost advantages of the economically less privileged countries of the Community would disappear" (p. 512).

Fixed Exchange Rates

Under a regime of irrevocably fixed exchange rates, as is likely to exist in a monetary union, locational arbitrage cannot be offset by adjustments in the exchange rate. In this case, any adjustment to restore competitiveness of the country would have to occur via price and wage flexibility. Downward inflexibility of wage contracts, in this case, would require a parallel evolution of unit production costs. This could be achieved with some harmonization of social security. Ohlin et al, (1956) argue that this imposes only a minor restriction on the autonomous decision making of the national social security administrations. In general, irrevocably fixed exchange rates require greater convergence of the real sector.

Free Movement of Factors

Free movement of factors does not unduly complicate the analysis or change the qualitative results significantly. With free movement of labour, it would be necessary to ensure the portability of benefits earned in the individual social security schemes and does not entail any loss of social security rights gained on the basis of past employment. A sufficient condition for this is to entitle migrant workers to benefits from all the social security schemes of the countries in which they have worked, paid contributions and/or had residence according to the respective covered periods [Andel (1967), cited in Petersen (1991)].

However, in a homogenous labour market with large-scale labour movements countries would need to harmonize their redistribution policies. In this context, factor rewards may bear no relation to marginal factor productivity, if migrant workers take account of the present value of future social security benefits in their decision to move. In these circumstances, complicated subsidies may have to be implemented to ensure efficient factor mobility.

Fiscal Federalism and Harmonization

The theory of fiscal federalism addresses the assignment of economic powers between different levels of government [Musgrave (1969), Olson (1969), Oates (1972)]. Centralization is seen to be optimal under a restrictive set of assumptions. Although the economic theory of federalism has some insights

for the distribution of powers within a single nation the theory is overly influenced by the experiences in the United States and may not be quite compatible with the existence of different nations [Pelkman (1982)]. This has led to the development of the concept of subsidiarity in the European context. In the typical European fashion subsidiarity has come to be interpreted as what is politically acceptable at any given time.

Fiscal Equivalence

The literature on fiscal federalism focuses on the identification of jurisdiction in which the boundaries of a set of voters sharing a specific public good exactly coincides with the voters. This "perfect mapping" is called fiscal equivalence. Assuming that national boundaries are given and that other political jurisdictions can be redrawn to secure the most efficient performance of fiscal functions, Musgrave and Musgrave (1980) considers the basic fiscal functions, allocation distribution and stabilization. Allocation theory concludes that social goods should be provided and their cost shared in line with preferences of the residents of the relevant benefit jurisdiction. In addition, since a political process is needed to secure preference revelation, the provision of social goods should be voted on and paid for by residents of that jurisdiction. This leads to the conclusion that there should exist several levels of government roughly corresponding to the optimal size of the jurisdiction for various goods. A similar conclusion is reached by Olson (1969) using a system of optimal coalitions in which people vote with their feet. Thus, for centralization to be optimal for the provision of any social goods, preferences would have to be identical among voters and efficient mechanisms for preference revelation must exist. If social security is viewed as a collective good, its provision by a central administration would only be optimal if preferences in the different jurisdictions are similar.

The assignment of fiscal power depends crucially on the monetary arrangements in the integration movement. In existing federations, monetary policy is assigned to the federal government. Given the need for coordination of monetary and fiscal policy for stabilization, the federal government would need to have at its disposal powerful fiscal instruments and would have to insist that individual states use the instruments under their control in concert with the national policy. Moreover, the substantial links between monetary and fiscal policy via the financing of government deficits make the assignment of the latter, exclusive to one level of government, impossible.

The example of Germany, discussed in Denton (1978) illustrates the difficulty of assignment. The Stabilization Law of 1967, which among other things, made changes designed to strengthen the powers of the Federal Government in Germany to deal with cyclical fluctuations, required that state governments plan their budgets several years in advance in coordination with Federal Government policy. The law also imposed controls over the borrowing powers of the lower levels of government.

Of more relevance to the discussion of social security, is the analysis of distribution since social security has strong interpersonal and intergenerational distribution effects. Musgrave and Musgrave conclude that interpersonal distribution of income must be undertaken at the national (central) level. Unless the differentials are minor, inter-jurisdictional differences will affect the choice of location by both individuals and businesses. Decentralized efforts at redistribution will be self-defeating since the rich will leave and the poor will move to the more egalitarian jurisdictions. The tendency for the rich to congregate and exclude the poor who try to follow, which arises in the allocation problem, is reinforced by decentralized redistribution schemes.

Fiscal distribution effected through progressive income tax and transfers must be uniform within an area in which there is high labour and capital mobility. When this analysis is applied to social security schemes in a multi-country context, it results in social dumping discussed earlier under the efficiency of the internal market.

Subsidiarity

The principle of subsidiarity recognizes that the pure theory of fiscal federalism cannot be applied uncritically in a multi-country context. The theory of fiscal federalism does not deal with situations where there is less than full integration. The basic question answered by fiscal federalism is different from the one which needs to be answered in the intermediate stages of economic integration. Recall that the basic question for fiscal federalism is that, given national (central) government, what functions are more efficient to delegate. In the case of economic integration the question is, given national political dynamics, what functions should be transferred to the centre. The questions surely are

not symmetric if only because in the first case exchange rates are irrevocably fixed and product and labour markets are already integrated.[1]

There are two popular interpretations of the concept of subsidiarity. The liberal view suggests that all decisions should be taken whenever possible by the individual actors within the community. Collective action should only take precedence when the individual cannot make the decision or cannot effectively enforce the implementation of the decision. The Supranational view ascribed to Jacques Delors as quoted in Cox (1994) is as follows:

> "Subsidiarity, because it assumes that society is organized into groups and not broken down into individuals, rests strictly speaking on a dialectic relationship: the smaller unit's right to act is operative to the extent, and only to the extent (this is forgotten very quickly) that it alone can act better than a large unit in achieving the aims being pursued." (p. 136).

This clearly suggests a stronger tendency for centralized action. However Cox (1994) argues that this debate is sterile since one cannot make a priori statements about rights, but that the results would depend on the particular circumstances. In practice, subsidiarity boils down to what is politically feasible at that time. With respect to the Harmonization of Social Security, Petersen (1991) states, "This brief survey of the Commission's attitudes - varying according to the political climate of the day - suggests its profound desire to develop a community platform for decision-making in social security, i.e. harmonization is necessary to ensure the functioning of the internal Market." (p. 508).

However, due to the fact that the national social security systems are highly developed and run along different lines, the harmonization of social security is very low on the list of priorities in the European Union. In addition, because of economic divergences between the members are so wide, for example in the average levels of real personal incomes, inter-personal redistribution of incomes will suffer from benign neglect for some time yet. The diversity in social security arrangements allows the countries to choose to some extent the level of provision of welfare and therefore allowing people to have some choice of moving to countries with different levels of welfare and taxation.

---

[1] The efforts of Quebec to secede from the federal government of Canada, notwithstanding.

Social Security Harmonization in CARICOM

In a passive sense, harmonization of the social security schemes dates back to their inception in the mid-1960's. The schemes were established with technical assistance provided by the International Labour Organization (ILO). Thus, it would be passing strange if the schemes did not reflect some degree of similarity, as in some cases the consultants who provided the technical assistance were the same. Migrant workers were required to become registered contributors to the schemes in the country in which they worked. The independence of national schemes meant that such workers would be disadvantaged if they had to leave that particular country before they had made the minimum number of contributions which would qualify them for benefits under that scheme.

Initiatives to address this situation via a system of reciprocal agreements were first mooted at the Heads of Government meeting of CARIFTA in 1972. They agreed to establish a Working party on Reciprocal Arrangements for Social Security in the Commonwealth Caribbean which would undertake the following:

1. Examine the case for a system of international agreements which would ensure that persons moving between Caribbean countries would not lose the social security rights they had already acquired or were in the process of acquiring in the countries to which they had migrated.

2. Undertake a study of existing social security reciprocal arrangements with a view to determining their applicability to the proposed agreements between the Caribbean countries.

3. Examine the degree of similarity between the existing social security schemes in the Caribbean to determine if they are sufficiently similar to make reciprocal agreements feasible and determine the desirability of such arrangements, the effects (if any) on the mobility of labour, the financial impact on the existing schemes and the necessary administrative arrangements.

A draft convention was produced in 1975, but left some outstanding issues unresolved. These included the formulas for totaling periods for qualification and the apportioning of payments; the effects of the reciprocal agreement on the movement of labour; and the inclusion of short-term benefits. With respect

to the inclusion of short-term benefits, which include sickness, maternity, industrial injury and occupational diseases, concerns were expressed about the ability of the countries to provide the requisite information on a timely basis; the differences in coverage between the different schemes;[2] and the possible delays in payments due to exchange control restrictions.

The draft report was considered at the Heads of Government in 1976 but no action was taken. The agreement remained in a state of limbo until 1982 when it was submitted to a technical meeting of Heads of Social Securities. The recommendations of the Technical Meeting were accepted by the Standing Committee of Ministers responsible for Labour (SCML) and the Heads of Government Conference. In 1985 the SCML requested that the Heads of Social Security Schemes review the draft documents which by this time were in dire need of updating. The Heads of Social Securities examined the draft documents at their 1987 meeting and recommended the following:

1. the principle of reciprocity should be re-endorsed;

2. the establishment of a working party consisting of at most seven members to review and update the draft agreement;

3. meetings of the working party would be convened by the CARICOM Secretariat which would select the members and would also include a representative of the Secretariat and the International Labour Organization (ILO); and

4. the report of the Working Party would be examined at a technical meeting of the Heads of Social Security schemes in time to submit the final report to the SCML meeting in 1989.

The working party was constituted with representatives from Barbados, Dominica, St Kitts-Nevis, St Lucia and Trinidad and Tobago, along with representatives of the CARICOM Secretariat and the ILO.

The revised Draft Convention and Administrative Agreement was prepared in 1990 and included the following elements:

---

[2] Some schemes, like Jamaica did not include all of the short-term benefits.

(a) A reciprocal agreement which was confined to long-term benefits (invalidity, retirement and survivors benefits).

(b) It would ensure that workers who had contributed to social security schemes in more than one of the contracting parties, who did not qualify for long term benefits in the individual schemes but would qualify if his contributions were summed, would receive such benefits with the application of the agreement.

(c) Totalization of qualifying contributions would be restricted to the case described at (ii) above.

(d) Pensions would be remitted by the national competent institution to the beneficiary wherever the person is resident, provided that such residence is in one of the contracting parties.

The revised draft was endorsed by the Heads of Social Security in April 1992 and the Final draft was approved by SCML in 1995 and presented to Intersessional Meeting of the Conference of the Heads of Government for signature in February 1996. The long and torturous journey of the reciprocal agreement is unfortunately not uncommon for CARICOM initiatives given the need for consensus.

However, it is hoped that the implementation of the free movement of skills would bring some greater urgency to the implementation of the CARICOM reciprocal agreement.

Evaluation of the CARICOM Initiative

This section of the paper attempts an evaluation of the CARICOM initiative in light of the discussions in Sections I and II of the paper. In order to do this it may be necessary to determine the extent of diversity/harmonization which currently exists. The next step would be to examine the extent to which the requirements for a fully harmonized system of social security schemes, identified in Section I and II, are satisfied in the CARICOM countries. However, this only addresses the issue of whether or not there should be complete harmonization. The thorny question of how much coordination would be necessary boils down to the degree of political will.

Existing Levels of Harmonization

An examination of the Social Security Schemes in the Caribbean reveals that a significant amount of harmonization already exists. This is hardly surprising, given their origin and the role played by the ILO in their establishment. On the financing side, all of the schemes are financed by pay roll taxes paid by both employees and employers, the total of which ranges from 5 per cent in Jamaica to 12 per cent in Guyana (see Table 2.1), excluding Guyana, Jamaica, St. Vincent and the Grenadines and Trinidad and Tobago from the picture, the total contribution by employers and employees cluster in the range of 8 - 10 per cent, with a small category of workers in Barbados paying about 12 percent. La Foucade (1995) has noted a general reluctance to change rates of contributions and insurable income thresholds. This she attributes to the political sensitivity of the rates, the need for parliamentary approval in the revision of Social Security Acts, and the similarity of the effects of payroll deductions with other taxes on income.

The threshold levels of insurable incomes vary significantly across the countries and can be related to the economic circumstances of the countries, primarily the effects of devaluation in a context where the absolute levels are inflexible as noted above. However, there is also a similar clustering of levels of insurable income, although not as tight as for the rates of contribution, for the countries which have maintained fixed exchange rates.

All of the countries have opted for financing on a part capitalization basis rather than a strict pay-as-you-go mechanism. In all cases separation of finances of the social security from the consolidated fund ensures that all benefits are not financed from general government revenue.

Most of the social security schemes are, relatively speaking fairly young schemes and have not been exposed to full complement of retirement obligations. As a result, most of the schemes have accumulated substantial investment funds. It is critical that these funds be invested prudently so that the schemes can meet their obligations as they mature. The investment infrastructure and policy of the CARICOM schemes show some amount of diversity. The larger schemes have relatively efficient functioning investment committees and have a less narrow range of instruments in which to invest. The investment infrastructure in some of the smaller schemes, on the other hand, is less sophisticated and investment committees where they exist, meet

and make perfunctory decisions on the investment portfolio. The range of assets is extremely narrow, mainly consisting of treasury bills, government bonds, fixed deposits and cash.

The narrow range of instruments in the financial sector has forced many schemes to take up a significant amount of government paper. Even so, the percentage of government paper in the individual portfolios varies significantly from a high of over 75 per cent in Grenada to 2 per cent in Montserrat.

The thinness of the financial markets in all of the countries has prompted some schemes to investment in real estate schemes many of which in some cases has not met with the expected level of success. High delinquency and additional administrative cost associated with the monitoring and collection of payments has prompted the Trinidad and Tobago scheme to reduce its exposure in the area of real estate (La Foucade 1995).

The constraint on the investment portfolio imposed by the thinness of the financial markets is further exacerbated by the regulation in most countries limiting the investment in foreign securities. Only Barbados, Montserrat, Guyana, St. Kitts-Nevis and Trinidad and Tobago permit investment in other countries. However, even in these countries the investment committees have tended to limit their horizons to the domestic economy with only a minor portion of the funds being invested abroad. For example in Guyana only 0.02 percent was invested in foreign assets while 3.8 and 2.1 per cent respectively of the Montserrat and St. Kitts-Nevis schemes was invested abroad (La Foucade 1995). Centralization of the administration of the schemes and the relaxation of the requirement to invest at home would open up greater opportunities for portfolio diversification.

On the benefit side, there is also some amount of harmonization. Taking first of all the long-term set of benefits offered by the social security schemes, i.e. retirement, invalidity and survivorship, the retirement age, the number of qualifying contributions and the maximum benefits are largely similar, except for Jamaica (see Table 2.2). The differentials arise from the administrative practices some of which La Foucade (1995) notes as being antiquated and in need of revision. The similarity provisions for benefits also holds for survivorship. Because the provisions for invalidity tried to incorporate the practices existing in the countries before the inception of the social security schemes there is some amount of variability on this count.

Turning next to the short-term benefits which include unemployment, sickness, maternity, funeral grants, etc., there is significant variability between the countries in these provisions.

Only Barbados provides unemployment benefits and only Jamaica does not provide sickness benefits. The diversity of provisions for sickness and maternity benefits are given in Table 2.3. Small funeral grants are given by a few countries to assist with the burial of a qualifying member of a social security scheme. These short-term benefits account for a small percentage of benefit payments and should be given similar consideration in determination of the level of harmonization of social security schemes.

When the financing arrangements and the provisions for long-term benefits are taken together, there is a significant amount of harmonization between the social security schemes in the CARICOM countries excluding Suriname which came out of a totally different origin. Thus, the level of natural harmonization together with the reciprocal agreement may provide a strong enough base for further coordination.

Mobility of Labour

Harmonization of social security schemes is not terribly important if there is little mobility of labour. However, if there is significant mobility of labour then harmonization may be necessary to avoid distortions. In the case of the Caribbean, in spite of controls on the movement of labour and the necessity of obtaining a work permit before workers can legally work in another territory, there is some movement of labour. Downes (1993) suggests that labour movement has tended to reflect the economic fortunes of the various countries. The influx of workers into Antigua and Barbuda and also Trinidad and Tobago during the oil boom and the exodus of people from Guyana are examples of such movements. However, intra-CARICOM migration is relatively small. The 1990 Census reveals that less than 5 per cent of Caribbean people are living in other Caribbean countries (Guengant 1993). However, the OECS countries have rather high intra-Caribbean migration.

Greater mobility of labour in the Caribbean may require some amount of harmonization of social programmes. However, it is uncertain whether the limited movement of labour contemplated by the Heads of Governments will lead to a substantial increase in labour mobility in the near future. Thus, given

the existing level of labour mobility, full harmonization of social security may not be necessary.

The Exchange Rate Regime

In Section I, it was argued that any difference in social security financing would be offset by exchange rate changes under a flexible exchange rate regime. Under a fixed exchange rate regime such difference can be neutralized by an appropriate devaluation prior to entry into a monetary union in which exchange rates would be irrevocably fixed. At the current time two different types of exchange rate regimes exist in CARICOM. Guyana, Jamaica and Trinidad and Tobago have adopted flexible exchange rate regimes, while the other countries have maintained fixed exchange rates. The official statements emanating from both groups of countries suggest that they are fully committed to their respective regimes for the foreseeable future. Suriname now pursues a floating exchange rate regime after having adjusted the rate from time to time. Although Suriname is a member of the Common Market, the authorities have not given an indication about their position on the single currency.

While differences in social security schemes are not easily offset under fixed exchange rates, the existence of floating exchange rates reduces the need for harmonization. An examination of the of the CARICOM social security schemes reveals that the countries with fixed exchange rates have a significant amount of harmonization. Thus, the significant degree of harmonization between the fixed exchange rate countries and adjustments in the floating exchange rate countries may obviate the need for harmonization. Moreover, when Balssa's (1961) observation that differences in social charges are absorbed into the countries cost structure with the passage of time, the case for complete harmonization is further weakened.

Similarity of Preferences

For full harmonization to be optimal there must be similarity of preferences across the countries. This requires a preference revelation mechanism, which in the context of a federal political configuration results in people voting with their feet. In the case of CARICOM national restrictions on the movement of labour nullifies this as a preference revelation mechanism. Judgment on this issue may have to be postponed until there is greater freedom of movement. Even then, labour movement may still be a preference revelation mechanism

with a lot of noise, since other factors may exert a stronger influence on the movement of labour. However, given the persistence of differentials in social security schemes, these may be a reflection of difference in preferences. In this context it may be necessary to leave room for diversity to reflect differences in personal and national preferences.

Disparities in Economic Development

Petersen (1992) observes that the less developed countries in the European Union have tended to have less generous social security schemes for two reasons: (1) they are unable to afford the levels of benefits available in the more developed countries; and (2) the low levels of benefits may contribute to their competitiveness and assist in the reduction in disparities between the rich and poor countries. In CARICOM, significant disparities in the level of development exist. The level of per capita income ranges between US$500 in Guyana and over US$10,000 in the Bahamas. However, per capita income may not be the most reliable measure of economic diversity since some of the countries with high per capita income have severely underdeveloped economic infrastructure and are highly vulnerably to external economic shocks. Harmonization in this context is likely to impose difficulties on low-income countries and those with less developed economic infrastructure.

The Efficiency of the Internal Market

One strand in the argument for the harmonization of social security hangs on the efficiency of the internal market, which presupposes that there is a significant and fully integrated internal market. Girvan and Samuel (1994), noting that intra-regional trade accounts for approximately 10 per cent of total CARICOM trade argue that given the insignificance of the internal market, production integration should be directed at external markets and competitiveness. The size of the internal CARICOM market is likely to dwindle even further with liberalization of the economies. Moreover, the existence of restrictions on trade in goods and services suggests that the market is not fully integrated. CARICOM (1993) details the incidence of restrictions on intra-regional trade. In this context, the efficiency of the internal market may be a shaky peg on which to hang the harmonization of social security. The external competitiveness of the individual economies may be jeopardized by an upward harmonization of social security benefits.

The OECS Harmonization Initiative

Frustrated by the slow pace of progress of the CARICOM reciprocal agreement, the OECS countries which have had a better track record on the implementation of decisions, moved to develop their own reciprocal agreement. The provisions of the OECS reciprocal agreement are consistent with the CARICOM agreement. In addition, it includes some of the short-term benefits, i.e. sickness and maternity. Evidently the existence of a single currency would have eliminated foreign exchange difficulties and the proximity of the countries would reduce the information difficulties.

All of the OECS countries are signatories to the OECS Social Security Reciprocal Agreement and the associated Administrative Agreement. Instruments of ratification of the Agreements have been deposited by the requisite number of countries to make the Agreement effective. Administrative arrangements were well on the way to begin the implementation of the Reciprocal Agreement before the end of 1996.

The OECS Reciprocal Agreement was signed on June 21, 1991 and was contracted between the then existing members of the OECS.[3] The Convention makes provision for accession to the agreement by unanimous agreement of the members. Accession takes effect three months after the deposit of the instrument of accession with the Director General of the OECS.

The reciprocal agreement applies to the following benefits:

(a) invalidity, old-age and survivor's benefits;

(b) benefits in respect of employment injuries and occupational diseases;

(c) funeral benefits, and;

(d) sickness and maternity benefits.

---

[3] The members of the OECS at that time were Antigua and Barbuda, Dominica, Grenada, St Kitts and Nevis, St Lucia, St Vincent and the Grenadines, Montserrat and the British Virgin Islands.

The respective social security schemes have undertaken to provide all information concerning action taken, local legislation and subsequent amendment and statistical information concerning beneficiaries and benefits. This undertaking seeks to address the information problem identified by the CARICOM working party. They have also undertaken to provide administrative assistance to each other free of cost.

Although, the agreement requires cash payments to be made directly by the scheme on which the obligation falls even if the beneficiary resides in another participating territory, they can arrange bilaterally to have the local schemes pay on their behalf. The convention does not explicitly address the exchange control issue but it implicitly rules out exchange controls on payments between the ECCB member countries and the BVI for social security purposes. The payments mechanism is also not addressed directly, but there would be a need for an efficient payments mechanism in which the Central Bank may have a role to play. Although the provisions for benefits under the various social security schemes are largely similar, some differences exist. An approach to the reduction of these differences could be to declare a stand still on changes in the provision which lead to further disparities and the coordination of future changes which would lead to their erosion. Some of the areas in which differences exist include:

1. The qualifying contributions for the various benefits;

2. the rate of contribution for employer and employees;

3. the age range during which contributions are made by the insured;

4. the structure of benefits, for example the quantum of payments paid to widow(er)s and children under survivors' benefit and the number of children included; and

5. the income base on which contributions are made and benefits are paid, for example the St. Kitts-Nevis scheme levies contributions on income including allowances but benefits are paid only on basic salary.

The existence of a single currency implies that the OECS countries constitute a *de facto* currency union with irrevocably fixed exchange rates. Moreover, the disparities in income between the countries are less than the rest of

CARICOM. These considerations would seem to suggest that there should be greater harmonization among OECS schemes than at the level of the wider CARICOM region.

However, labour mobility among the OECS countries is not significantly greater than in the rest of CARICOM. In addition, the level of intra-OECS trade is approximately 6 per cent which is less than the regional level. Even with fewer restrictions on intra-OECS trade, the size of the sub-regional market limits the relevance of the market efficiency argument. This suggests that considerations about the efficiency of the internal market are of less relevance than for the rest of CARICOM.

The size of the individual schemes also suggests that economies of scale can be reaped by the consolidation of the OECS schemes. While administrative cost may not be reduced significantly due to the need to maintain administrative capabilities in all of the countries, there are a number of common services which can be shared by the schemes. These include accounting, management information systems, etc. One area in which significant economies can be achieved is in the area of investment of the accumulated funds. The existence of eight small funds limits the opportunities which would be available for the investment of a much larger fund. Moreover the individual countries may not be able to provide the personnel to adequately staff investment committees to ensure the most efficient investment of the financial resources of the schemes. A sub-regional approach to investment would be able to harness talent which the individual countries may not be able to command. Alternative approaches to regional investment of social security funds were discussed in Sebastian (1995). He suggested that the establishment of a sub-regional investment fund consisting of the surplus funds of the various schemes may be the most viable option given the difficulties of creating a unified social security administration.

Conclusion

This paper looked at the harmonization of social security schemes in the CARICOM countries using the theoretical insights of fiscal federalism and economic integration theory as a backdrop. It concludes that total harmonization may not be desirable given that the Caribbean countries do not satisfy all of the basic conditions which would make complete harmonization

optimal. These include, a high level of labour mobility; irrevocably fixed exchange rates; small disparities in the economies; and a substantial and fully integrated internal market. However, there already exists significant harmonization of the provisions for financing and the payment of the long-term benefits of the social security schemes as a result of their common origin. This coupled with an efficient reciprocal agreement should provide an adequate level of harmonization given the existing level of labour mobility, diversity of exchange rate regimes, disparities in economic structure and differences in preferences. It also provides a strong base for further coordination in the future. The differences can be further attenuated if there is greater coordination in the updating of largely antiquated administrative procedures.

Section I of the paper discusses the case for harmonization which arises from the literature on economic integration. The literature suggests that complete harmonization would only be necessary if there is significant mobility of labour and irrevocably fixed exchange rates. The contribution of the fiscal federalism literature to the analysis of the division of functions within an integration movement is discussed in Section II. The literature suggests that some amount of diversification may be necessary and that complete harmonization would be optimal only with very restricted assumptions including identical preferences and fiscal jurisdictions. The desirability of harmonization of social security is discussed in Section III. The development of the CARICOM reciprocal agreement is reviewed and the high degree of natural harmonization is noted. The need for closer harmonization in the OECS social security schemes, given the existence of a currency union and small disparities between the economies, is discussed. There is no presumption for complete harmonization due to the low mobility of labour and differences in preferences. However, the size of the schemes suggests that there can be significant economies in administration and investment of accumulated funds if the schemes were centralized.

Although the existing level of labour mobility does not require further harmonization, given the political difficulty of achieving this, initiatives for the free movement of labour would suggest greater harmonization in the future. In addition, the formation of a monetary union with irrevocably fixed exchange rates may also require greater harmonization. This means that as the schemes look towards the future, steps should be taken now to facilitate harmonization in the years to come. The appropriate response would be to

minimize any increase in disparities and to coordinate and update of administrative procedures to increase convergence of social security practices.

References

Andel, N. (1967), "Problems of Harmonization of Social Security Policies in a Common Market," in Shoup C. *Fiscal Harmonization in Common Markets*, New York: Columbia University Press, pp 353 - 84.

Balassa, B. (1961), *The Theory of Economic Integration*. Homewood: Allen & Unwin.

Buchanan, J.M. and C.J. Goetz (1972), "Efficiency Limits of Fiscal Mobility: An Assessment of the Tiebout Model," *Journal of Public Economics*, No. 1, pp 25 - 43.

Cox, A. (1994), "Derogation Subsidiarity and The Single Market", *Journal of Common Market Studies*, No. 32 , pp 127 - 48.

Denton, G. (1978), "Reflections on Fiscal Federalism in the EEC", *Journal of Common Market Studies* No. 16, pp 283 - 301.

Downes, A. (1994), "Labour Market Issues in Caribbean Monetary Union" in T. Farrell and D. Worrell *Monetary Integration in the Caribbean*, Port of Spain, CIS 1994.

Girvan, N. and W. Samuel (1994), *Market, State and Caribbean Integration: Towards A New Paradigm*, Kingston: UWI Press, (forthcoming, Manuscript 1994).

Guengant, J. (1993), "Whither The Caribbean Exodus?: Prospects for the 1990's," *International Journal*, No. 68 pp 336 - 53.

La Foucade, A.D. (1995), *A Review of the Evolution and Performance of Social Security Schemes in the English-Speaking Caribbean*, Port of Spain: Interamerican Conference on Social Security and National Insurance Board.

Meade, J. M. (1953), *Problems of Economic Union*. Chicago: University of Chicago Press.

Musgrave, R. (1969), "Theories of Fiscal Federalism," *Public Finance*, No. 24, pp 521-32.

_____ and P. Musgrave (1980), *Public Finance in Theory and Practice, London:* McGraw-Hill.

Oates, W. (1972), *Fiscal Federalism*. New York: Harcourt Brace.

Ohlin, B. et al. (1956), *Social Aspects of European Economic Cooperation*, Report to the International Labour Office, Geneva: ILO.

Olson, M. (1969), "Strategic Theory and Its Applications to the Principle of Fiscal Equivalence: The Division of Responsibilities Among Different Levels of Government," *American Economic Review*, No. 59 pp 479 - 487.

Organization of Eastern Caribbean States "Convention on Social Security in the Organization of Eastern Caribbean States," Mimeo.

_____, "Administrative Agreement for the Application of the Convention on Social Security in the Organization of Eastem Caribbean States". Mimeo.

Pelkmans, J. (1982), "The Assignment of Public Functions in Economic Integration,,".*Journal of Common Market Studies*, No. 21 pp 97 - 125.

Petersen, H. J. (1991) "Harmonization of Social Security in the EC Revisited," *Journal of Common Market Studies*, No. 5, pp 505 - 526.

Rhodes, M. (1992),"Labour Market Relations in Post-1992 Europe," *Journal of Common Market Studies*, No. 30.

Samuel, W. (1990), "Social Security Schemes in the OECS Countries," *Bulletin for Fiscal Documentation*.

Sebastian, S. (1995), "Mobilizing Capital: Coordinated Investment Management of Social Security Reserves," Paper Presented at the ECCB Meeting with Social Security Schemes, May 1995.

Smith, G. (1994), "Update on Reciprocal Arrangements for Social Security in the Caribbean Community", *New Insight*, pp 26 - 27.

_____, "A Guide to the CARICOM Social Security Agreement", Mimeo.

Thurow, L. C. (1971), "The Income Distribution as a Pure Public Good," *Quarterly Journal Of Economics*, No. 85 pp 327 - 36.

Table 2.1 - Financing of Social Security Schemes in the Caribbean

Country	Age of Insured	Annual Insurable Income EC$	Employer's Contribution %	Employee's Contribution %	Self Employed
Anguilla	16 - 59	36,000	5	5	N.A.
Antigua & Barbuda	16 - 59	54,000	5	Gov't 2 Private 3	8
Bahamas	16 - 59	35,100	5.4	1.7 - 3.4	6.8 - 8.8
Barbados	16 - 64	50,220	8.25	7.5	10
Belize	14 - 65	6,760	6	1	N.A.
British Virgin Island	15 - 65	37,260	4.5	4	8.5
Dominica	14 - 60	60,000	7	3	7
Grenada	16 - 59	30,000	4	4	6.75
Guyana	16 - 59	5,460	7.2	4.8	11.47
Jamaica	18 - 64	250,000	2.5	2.5	5
Montserrat	16 - 59	31,200	4.5	3	N.A.
St. Lucia	16 - 59/64	36,000	5	5	N.A.
St. Kitts-Nevis	16 - 59	70,200	5	5	N.A.
St. Vincent & The Grenadines	16 - 59	31,200	3	2.5	N.A.
Trinidad & Tobago	16 - 59	11,960	5.6	2.8	N.A.

Source: Respective Social Security Schemes
a: The insured determines his/her contribution to the scheme

Table 2.2 - Long-Term Benefits under Social Security Schemes in the Caribbean

Country	Minimum/ Maximum Pension	Qualifying Contributions	Survivorship	Invalidity
Anguilla	EC$ 120/wk - 60%	250 paid or 500 paid/credited	EC$ 27/wk - 60%	50 wks. to qualify EC$ 105 - 30%
Antigua & Barbuda	EC$ 136.50 - 60%	500 paid/credited	EC$32.50 - Spouse 1/2 pension Orphan 2/5 pension Child 1/5 pension	150 pd to qualify EC$1000 - 75%
Bahamas	40 - 60%	150 paid or 750 paid/credited	Spouse 1/2 pension Children 1/10 pension (3)	40 - 60%
Barbados	EC$ 111.38/wk - 60% Non contrib. $ 90.45	150 paid or 500 paid/credited	Spouse: 1/2 pension Children: 1/3 pension (3)	150 pd. to qualify EC$111.38 - 60%
Belize	30 - 60%	150 paid or 500 paid/credited	Spouse 1/5 pension Children EC$ 135/mt - 2/5 pension	150 pd to qualify EC$100 - EC$540
British Virgin Islands	US$ 234/mt - 60%	500 paid/credited 250 pd. (For special)	EC$175.5/mt - Spouse 2/3 pen Children 1/3 pen	EC$234/mt - 60%
Dominica	EC$ 25/wk - 70%	150 paidor 150 paid/credited	Spouse: 2 pension Child EC$30/mt - 1/6 pension	EC$25/wk - 70%
Grenada	EC$ 35/wk - 60%	150 paid or 500 paid/credited	Spouse: 1/2 pension Children: EC$7.50/wk (4)	150 pd. to qualify 30 to 60%
Guyana	G$ 3669/mt - 60%	150 paid or 750 paid/credited	Spouse 1/2 pension Children 175 pension	G$3369/mt - 50%
Jamaica	J$150 - J$ 300/wk	312 with 13 min. Yearly	Spouse: J$150 - J$300/wk Orphan/Special J$ 500/wk	J$150 - J$300/wk
Montserrat	EC$ 173/mt - 60%	150 paid	Spouse:1/2 pension Children: 1/3 pension (3)	150 pd to qualify 50 pd for a grant EC$173/mt - 60%
St. Kitts-Nevis	EC$ 2160/yr - 60%	500 paid	Spouse: EC$90/mt - 1/2 pension Child: EC$30/mt - 1/6 pension	150 pd to qualify 30 - 60%
St. Lucia	EC$ 25/wk - no max	120 paid of 520 paid/credited	Spouse: 3/4 pension Children:1/4 pension	40 - no maximum
St. Vincent & the Grenadines	30 - 60%	500 paid/credited	150 contributions 75% of pen. (Spouse) 25% of pen. (Children)	150 contributions 30 - 60%
Trinidad & Tobago	TT$ 30/wk - 75%	750 paid/credited	---	---

Table 2.3 - Sickness and Maternity Benefits Payable in the Caribbean (1996)

Country	Sickness				Maternity			
	Qualifying Contribution	% Av. Wage	Weeks Duration	Waiting Period (days)	Qualifying Contribution	% Av. Wage	Weeks Duration	Grant Country Currency ($)
Anguilla	26 (8/13)	60	26	3	26 (20/39)	60	13	250
Antigua & Barbuda	26 88/13)	60	26	3	(26/20/39)	60	13	40
Bahamas	40	60	156-240 days	3	50	60	13	250a
Barbados	b	66	312 days	3	26	100	12	500c
Belize	50	80	22	5	50	80	12	100
British Virgin Islands	26 (8/13)	66.67	26	3	39 (20/39)	66.67	13	200
Dominica	13	60	26	4	30	60	12	250
Grenada	13 (8/13)	60	26-52	3	30 (20/30)	60	12	400
Guyana	50	70	26	3	15	60	13 - 26	300
Jamaica	--	--	--	--	26	Min. Wage	8	None
Montserrat	26	60	26	3	30 (20/30)	60	12	400
St. Kitts/ Nevis	26 (8/13)	65	26	None	39 (20/39)	65	13	400
St. Lucia	26	60	26	2	7 months	60	12	200
St. Vincent & The Grenadines	26 (8/13)	65	26	3	30 (20/30)	65	13	200
Trinidad & Tobago	10	66	26-52	3	10	60	13	500

Source: Social Security Schemes
Numbers in bracket under qualifying contributions refers to the number of weeks during the period when contributions should have been paid. For example (8/13) means that the beneficiary must have paid 8 of the last 13 contributions. b: An employed person only has to satisfy the condition of having worked immediately before becoming ill. Self-employed have to pay 30 contributions.

CHAPTER 3

THE EVOLUTION OF PENSIONS SYSTEMS IN BARBADOS: A CRITICAL APPRAISAL

FRANK W. ALLEYNE*

* Frank Alleyne is a Senior Lecturer in the Department of Economics, UWI, Cave Hill Campus and is currently Acting Director of the Institute of Social and Economic Research, UWI, Cave Hill Campus, Barbados.

Introduction

Commencing in 1925 when a few elite workers were granted the concession of a pension after a period of continuous employment, employers have grudgingly conceded to workers payment of a pension as an inalienable right after completion of a specified minimum period of continuous employment. The present collection of public service, parastatal, and private sector pensions schemes is devoid of a unifying policy framework and poses difficult challenges to private sector providers of pensions plans and public sector planners as well.

In Section I we trace the evolution of pensions in the Central Government service, and this sets the stage for an examination of the development of pensions in the statutory bodies which developed at a later stage. The National Insurance and Social Security Act (1966) established the legal framework for a comprehensive national public pension scheme. Section II traces the development of social security pensions analyzing their cost, method of financing, and qualification requirements.

Private sector pensions schemes were introduced later than Central Government schemes. In Section III we discuss the supplemental schemes provided by the private sector examining the conditions which give rise to their demand, methods of financing and management, types of schemes, coverage of the workforce, and the location of private schemes in a system of national pensions.

Section IV examines the nature of the relationship between pensions provided by the Central Government, the Social Security Office, and the private sector, calling attention to the urgent need for a unified policy framework to inform the development of a fully integrated national pension scheme. Inflation and increasing longevity have created difficulties for pensioners in maintaining an "expected" standard of living, and produced near nightmares for the financiers of pensions, and we turn attention to these problems in Section V. Finally we offer some suggestions for reform of the system in order to achieve an integrated national pensions scheme.

Evolution of Public Service Pensions

Collymore (1995)[1] noted that the Superannuation Act of the United Kingdom 1891[2] was the earliest known instance of public sector provision of pensions for its employees. At that time the notion of a pension was elitist since it covered only the most senior officers in the public service. The principles underlying the 1891 United Kingdom legislation were eventually extended to cover the Colonial Service in 1925. Prior to 1925 pensions in the local public service were granted on an "ad hominem" basis requiring the legislature to grant permission to pay a pension to a particular officer. These deficiencies in pension legislation created a cumbersome process which required the legislature to pass specific pieces of legislation to grant pensions to deserving public servants.[3]

The extension of the principles which informed the 1890 UK Legislation to the colonies in 1925, was occasioned primarily by a desire to create uniform conditions of service for British civil servants at home and abroad. The Teachers Pension Act 1925[4] and the Public Employees Pension Act (1937)[5] entitled teachers and civil servants to pensions along the lines established in the 1891 United Kingdom legislation.

Collymore noted that the pension law was a standard instrument throughout the colonial empire, facilitating the transfer of colonial civil servants between colonies. Relocation of colonial servants from one colony to another gave rise to various classes of pensions (mixed service pensions, scheduled service, government service, and other scheduled authorities). Provision was made for the dependents of the colonial civil servant by the Widow and Orphans Pension Act (1928)[6] to take care of the children and spouse of the colonial officer working in overseas environments threatened by devastating diseases.

---

[1] Collymore, Branston.R. Pensions in the Public Service - An Overview. *New Insight*, No.14 Superannuation (War Department) Act, 1890 Laws of the United Kingdom.

[2] CAP 18 Superannuation (War Department) Act, 1890 Laws of the United Kingdom.

[3] The Barnwell Pension Act, 1943; The Hurley Pension Act, 1943: Gittens Gratuity Act, 1943; Laws of Barbados, 1943. Vol XI Part II.

[4] Teachers' Pensions Act; 1925-3. Vol. VII. Part I. Laws of Barbados.

[5] Public Employees Pensions Act, Laws of Barbados, 1937 Vol.1X, Part IV.

[6] Widows and Orphans Pensions Act, 1928-3. CAP 37 Laws of Barbados.

Where these pension arrangements were extended to the local civil servant they were less generous, and discriminated against the middle and lower level public officers. The island was divided into eleven parishes each run by a vestry which provided basic services such as road maintenance and health. These vestries also provided personalized gratuities for employees until the Parochial Employees Pension Act 1944[7] which granted pensionable status to this group of workers. In 1959[8] the vestries were replaced by three Councils (Southern, Northern, and Bridgetown) and local government pension regulations replaced the 1944 Act.

The era of modern public service pensions was ushered in by the enactment of the Pensions Act (1947),[9] which brought several classes of public officers within the provision of a single Act, improved benefits, and reduced the period of service required for receipt of a maximum pension from forty years to thirty three and one-third years.

The dismantling of the British Empire which began after the end of World War II, ushered in an acceleration of pension reform in the British colonies, Barbados being no exception. Commencing in 1947 with the passage of the Pensions Act other important reforms included the Casual Employees Pensions Act (1961)[10] and the Local Government Pensions Regulations (1961)[11]; the Teachers (Secondary School) Pensions Act (1962)[12], and the Widows and Children Pensions Act (1963).[13] This period which is noted for rapid reform of social legislation coincided with the introduction of internal self-government in the colonies. Indigenous administrations tended to be more sympathetic to their employees hence the introduction of more humane and comprehensive pensions legislation compared with the period prior to the 1940's.

---

[7] Parochial Employees Pensions Act, 1944-14. Laws of Barbados, 1943 and 1944.
[8] Local Government Act, 1959. CAP 107 Laws of Barbados. 1971 Vol. III.
[9] Pensions Act, 1947-20 Laws of Barbados 1947 Vol. VI. Part III.
[10] Casual Employees Pensions Act, 1961-44 Laws of Barbados Part II.
[11] CAP 107 Section XVII Laws of Barbados 1961 Vol. III.
[12] Teachers (Secondary School) Pensions Act 1962-47. The Laws of Barbados 1962 Part II.
[13] Widows and Children Pensions Act, 1963 CAP 37 Laws of Barbados.

The Casual Employees Pensions Act

The Casual Employees Pensions Act[14] provided for the grant and payment of pensions and gratuities to persons who had been employed on a casual basis in the public service. The Act defined a casual worker as one who was not holding or acting in an office established by an order under the Civil Establishments Act, or was not a public employee specified in the Public Employees Pensions Act.[15] For the first time casual workers were provided with the security of pensionable employment. The Act specified the minimum period of service required for receipt of a pension, and the age at which a retired officer could begin to receive a pension. Provision was made for premature retirement on medical grounds and award of pension provided that the officer's early retirement was not due to his/her negligence. The Act permitted the retiring officer to opt for a full pension set at the annual rate of one-six-hundredths (1/600) of his pensionable service, or a pension at the rate of three-fourths ($^3/_4$) of maximum pension and a gratuity equal to twelve and one-half (12 ½) times the amount of the reduction in pension. The legislation provided for payment of a gratuity to the estate of an officer who died before retirement, and payment of pensions to dependents. Payment of pensions to surviving dependents was determined by the circumstances of the officers' death.

Pensions Act 1967[16]

The 1967 legislation amended and consolidated laws pertaining to pensions of public officers, and made special provision for officers who retired from the public service other than Central Government, and re-entered the Central Government service. Section VI of the Act addresses the issue of financing and determined that pensions are a charge on the Consolidated Fund. Section VII states that no officer has an absolute right to pension, gratuity or other allowance, and receives such at the discretion of the Governor General. This matter of an officer's right to a pension was subsequently addressed at Sections

---

[14] Casual Employees Pensions Act 1961-44 CAP 20 Third Supplement of the Laws of Barbados.

[15] Public Employees Pension Act, Laws of Barbados, 1937 Vol. IX Part IV.

[16] Pensions Act, CAP 25. Vol.1, Laws of Barbados 1971-86.

103 and 104 of the Constitution of Barbados. Section VIII of the Act sets out the conditions governing the award of a pension, and Section XII fixed the maximum pension at two-thirds ($^2/_3$) of the highest pensionable emolument received by an officer in the course of his service.

Pensions (Transferred Federal Officers) Act[17]

The Transferred Federal Officers Pensions Act (1965) was necessitated by the collapse of the West Indies Federation in 1962, and the subsequent dislocation of federal civil servants. The Act facilitated re-entry into the Barbados public service and protection of benefits of those officers who opted to forgo a gratuity and pension from the Federal Government.

Local Government Taxation (Transfer of Functions) Act[18]

Consequent upon the abolition of Local Government it was necessary to transfer the functions of the Local Government Commissioner to the Minister of Finance. Section VIII of the above legislation provided for the protection of the pension, gratuity, and other allowances granted to officers transferred from the Local Government to the Central Government service. The Act specifically addressed the issue of transferred officers who were not desirous of relinquishing pension entitlements enjoyed in Local Government. It vested the authority to decide the issue in the Governor General.

The National Insurance and Social Security Act[19]

The National Insurance and Social Security Act CAP 47 of the Laws of Barbados established the legal framework for a comprehensive public pensions system commencing in 1966. Section XXI of the Act sets out a range of benefits payable under the social security scheme. Two principal types of benefits are provided for in the legislation, short-term (maternity, employment injury, sickness, unemployment) and long term (old age contributory, invalidity, disablement, survivors, and non-contributory old age). The range of contributory pensions includes old age, disablement, survivors, and invalidity.

---

[17] Pensions (Transferred Federal Officers) Act Vol. II, Laws of Barbados 1971-86.

[18] Local Government Taxation (Transfer of Functions) Act. CAP 108A Vol. III, Laws of Barbados, 1971.

[19] National Insurance and Social Security Act. CAP. 47, Vol. II, Laws of Barbados, 1971.

Old Age Contributory Pension

In order to qualify for a contributory pension an insured person who has attained the age of sixty-five years must have not less than 150 contributions paid to his/her account, and have at least a total of 500 contributions paid or credited to his/her account. The annual rate of pension is 40 percent of the average insurable earnings in the best three consecutive years of the final fifteen years, supplemented by a 1 percent of the total earnings on which contributions were based subsequent to the first 500 contributions paid or credited up to a maximum of 60 percent. The minimum pension is BDS$82.50 (1996). The maximum pension payable is sixty percent of average insurable earnings. At 31st December 1995 the number of Old Age Contributory Pensioners was 13,725, costing the National Insurance Scheme BDS$ 86,044,246.00 during 1995.

Invalidity Benefit

An Invalidity pension is payable to an insured person who cannot work because of sickness when the 312 days of sickness benefit payments have been exhausted. Payment of an invalidity benefit continues for as long as the insured worker is unable to work, but on attaining age sixty-five the invalidity pension is converted into an "old age contributory pension" at a level not lower than the quantum of the invalidity pension. At the end of 1995, there were 1,810 pensioners on the National Insurance register at a cost of BDS$ 10,455,952.00 during 1995.

Survivors Pension

A contributor to the social security scheme who has failed to accumulate at least 500 contributions on reaching age sixty-five is entitled to an "Old Age Contributory Grant " (OACG). The amount of the OACG is a lump sum equal to six weeks average insurable weekly earnings for each fifty contributions actually paid or credited to the insured person's account. The recipient of an OACG can qualify for a Non-Contributory Old Age Pension (NCOAP). The NOACP is payable to persons who have attained the age of sixty-five years but are not eligible for a contributory pension. At the end of December 1995 the number of persons receiving survivors pensions was 1,563, at a cost of BDS$ 4,010,396.00 to the National Insurance Scheme during 1995.

Disablement Benefit

A disablement pension is paid to an insured person who has suffered a loss of faculty of at least thirty percent (30%). In the event of loss of faculty pension is payable for life, but if the impairment is temporary, it is payable for the period of impairment. A total loss of sight or hearing, or both hands normally count as 100 percent disablement. The maximum pension payable is ninety percent (90%) of insurable earnings. At the end of December1995 there were 233 persons receiving disablement pensions.

Non-Contributory Old Age Pensions[20]

Part V of the Non-Contributory Old Age Pensions Act (NCOAP) provides for the payment of non-contributory old age pensions. The Old Age Pensions Act (1938)[21] is the first initiative taken by Government to address the problem of the indigent which was highlighted by the Reverend Francis Godson.[22] The responsibility for paying the NCOAP was placed on the Vestries until the system of local government was introduced. In 1967 when Local Government was abolished[23] that responsibility was transferred to the Interim Local Government Commissioner, and thereafter in 1969 to the Chief Welfare Officer. In 1982 the responsibility for financing the NCOAP was placed on the National Insurance Scheme.

A non-contributory old age pension is payable to persons who have attained the age of 65 years and are not eligible for a contributory pension. To receive the NCOAP, an applicant must satisfy the following conditions:

- Be a citizen of Barbados who has been residing in the island for fifteen years since attaining the age of eighteen years;
- Be a permanent resident must be residing in the island for fifteen years since attaining the age of forty years, or an aggregate of twenty years since attaining the age of eighteen years;

---

[20] The Non-Contributory Old Age Pensions Act, 1938. CAP 48, Part V, Laws of Barbados.

[21] Old Age Pension Amendment Act, 1937-13, Laws of Barbados. 1937, Vol. IX Part IV. [22]

[22] Blackman, Francis. Methodism 2000 Years In Barbados. Methodist Church in Barbados, 1988. p. 62.

[23] Local Government Act, 1967. CAP, 107 Laws of Barbados. 1971, Vol. III.

- Be blind or a deaf mute on becoming eighteen years and earning less than BDS$ 30.00 per week.

Reasons For Disqualification:

- A recipient of a pension in respect of public service in Barbados;
- Inmates of a Government health institution or prison;
- A person in receipt of this pension who is overseas for a period in excess of six months;
- A person in receipt of a pension from another Social Security Scheme.

Persons in receipt of pensions in respect of public service with another Government or with an international organization of which the Government of Barbados is a member.

Until 1982 non-contributory old age pensions were a charge on the Consolidated Fund, when they were transferred to the National Insurance Fund in that year. Pensions are financed by employers and employees each of whom is presently required to pay 2.0 percent of insurable earnings. At the end of 1995, there were 14,312 non-contributory old age pensioners, costing the National Insurance Fund BDS$49,854,607.00 during that year. The number of non-contributory old age pensioners has declined slowly from 16,253 in 1990 to 14,312 at 31st December 1995. In spite of the modest rate of decline in numbers of pensioners, a corresponding reduction in the cost of the NCOAP bill has not occurred because of occasional increases in the pension ceiling.

Reform of Pension Laws

The introduction of social security pensions created anomalies which necessitated modification in existing pensions legislation to eliminate areas of duplication. In 1971, the Casual Employees Pensions Act[24] was amended to provide for the cessation of payment of pensions to persons commencing employment after 1st July 1971. These persons were permitted to work until age sixty-five and receive a gratuity.

---

[24] The Casual Employees Pensions Act, CAP 20, Laws of Barbados, Vol. II, 1971-86.

The provision for Employment Injury through sections 14.1 and 21.2 of the NIS Act provided the rationale for amending all pension laws to discontinue the provision for increases in pensions resulting from retirement because of injury sustained on the job. This was effected through an amendment to the pensions laws in 1972.

Prior to 1975 a public employee was eligible for pension from the Central Government and the National Insurance Scheme. This area of duplication was removed by an amendment to all pension legislation[25] which stipulated that officers/employees who started to work on or after 1st September, 1975 was eligible for pension under the pension legislation for that portion of his salary which exceeded the NIS insurable earnings ceiling or in respect of any period of retirement on pension when the OACP in not being paid.

Section XXI(f) of the National Insurance and Social Security Act (1966) provides for payment of survivors pensions to a surviving spouse and dependent children in cases where the insured deceased was at least fifty years. This provision duplicated the Widows and Orphans Pensions Act 1928.[26] In 1978, the Widows and Orphans Pensions Act was amended to remove this area of duplication.[27] Dependents and spouse of officers entering the public service on or after 1st April 1978 were no longer eligible for benefits under the 1928 legislation.

Compulsory Retirement Age

The 1975 amendments[28] improved the conditions of service for public officers by providing that for purposes of computing an officer's pensionable service a break in service should be disregarded provided that the last stint of service before retirement is of five years duration. The Act facilitated early retirement while protecting an officer's pension by providing that any person who left the public service on or after 30th November, 1966 with ten or more years of pensionable service before reaching the age at which pension was paid may have his eligibility for pension stored until the age of fifty-five.

---

[25] Pensions (Miscellaneous Provisions) Act, 1975. Laws of Barbados.

[26] The Widows and Orphans Pensions Act, 1928-3. CAP. 37, Laws of Barbados.

[27] Widows and Children Pensions (Amendment) Act, 1978-6. CAP. 37 Barbados Acts, 1978.

[28] Pensions (Miscellaneous Provisions) Act, 1975. The Laws of Barbados, 1975.

The 1985 pension amendments[29] in addition to providing for compulsory retirement at age 65, varied the scale for computing pensions to the disadvantage of officers from 1/600 for every month of pensionable service to 1/60 for every year of pensionable service, thereby extending the period of employment for maximum pension from 33 1/3 to 40 years. This provision pertaining to the scale for computing pensions was reversed in 1990[30] and returned to the pre 1985 status.

Statutory Boards

The vast majority of approximately fifty statutory boards came into existence after the 1950's. Collymore[31] notes that a variety of pension schemes applied to these institutions, and several had no schemes in place prior to 1990. An investigation of the provision of retirement benefits for retiring employees of statutory boards in 1988 discovered that non-teaching staff in secondary schools had lost their right to pension under the Public Employees Pension Act or the Casual Employees Pension Act[32] in respect of any service after the Education Act was proclaimed in 1983. Arising out of that examination, amendments[33] to the Public Employees Pension Act[34] and the Casual Employees Pensions Act restored the rights to pension of officers disadvantaged by the 1983 Education Act. In 1990 government mandated all Boards to provide appropriate arrangements for retirement benefits for their employees.[35]

Private (Supplemental) Pensions Schemes

The Income Tax Act[36] provides for the regulation of businesses providing retirement pension plans. Section VII of the Act determines personal allowances

---

29 Pensions (Miscellaneous Provisions) Act. 1985, Barbados Acts, 1985.
30 Pensions (Miscellaneous Provisions) Act. 1990, Laws of Barbados.
31 Collymore, p. 12.
32 Casual Employees Pensions Act. CAP. 20, Laws of Barbados. Vol. II. 1971-86.
33 Pensions (Miscellaneous Provisions) Act, 1989.
34 Public Employees Act, Laws of Barbados. 1937. Vol. IX. Part IV.
35 Collymore. p. 12.
36 Income Tax Act, CAP. 73, Laws of Barbados. Vol. III. Section XIX.

against taxes payable with respect to premiums paid into registered retirement plans, and Section XIX specifies how the assessable income of a company shall be determined. The sole concern of the Act is with ensuring that appropriate amounts of taxes are paid. The earliest record of registration of plans with the Department of Inland Revenue is 1951. At the end of 1995, some 360 plans were registered with the Department.

Private pension schemes supplement the National Insurance and Public Service pension schemes by meeting the unmet segment of market demand which State sponsored schemes deem actuarially imprudent to incorporate into their arrangements. The areas of greatest demand for supplemental pension schemes are the self-employed and employed supervisory and management personnel in the private sector. Persons earning in excess of the insurable earnings ceiling under the National Insurance Scheme are most likely to demand private pension plans which enable them to attain a higher income level in retirement.

Types of Supplemental Pensions Plans

Supplemental pension plans marketed in Barbados can be classified under two broad categories. These are the Defined Contribution/Money Purchase Plan; and the Defined Benefit plan. Under the Money Purchase Plan both the employer and employee contribution is fixed by the company purchasing the plan. The employer's percentage is matched by that of the employee. The pension benefit to be received by the contributor is not fixed in advance. The quantum of retirement benefits depends upon the pool of funds contributed by employees and employers, and income generated from the investment of funds. The retiree's pension is quantified at the time of retirement.

The supplier provides investment and administrative services to the buyer and determines the specific types of investment selected within the broad parameters established by the purchaser. The fund is structured in a manner to enable employers to project the cost of providing the pension benefit which is usually a fixed percentage of payroll. The drawback of this model for the retiree is his inability to know in advance what the level of his retirement pension will be.

Defined Benefit Plan

In the case of the "defined benefit plan" the employee's level of benefit is fixed and a specified benefit is fixed for each year. The employer's cost varies in this plan depending on:

- the size and age composition of membership;
- investment returns;
- the National Insurance earnings ceiling;
- the mortality rate of the membership.

The "defined benefit plan" is reviewed every three years. The trend is toward purchase of the "defined benefit plan" because the purchaser knows in advance the precise level of the benefit. The drawback of this scheme for the employer occurs when the insured worker retires early thereby requiring the employer to pay the additional cost of the NIS portion of the pension.

Main Types of Defined Benefit Plans

The private sector provides personalized pension plans, specially designed to suit the needs of their clients. The principal types of plans marketed are the: Life and Five Year Certain Pension; Life and Ten Year Certain Pension; Life Pension With No Certain Term Guarantees; Contingent Beneficiary Option.

The "Life and Five Year Certain Pension" provides for monthly payment beginning on retirement and continuing for 60 months at least. In the event of death before receipt of 60 contributions the balance is payable to a beneficiary. The "life and ten year certain pension" provides for a smaller pension than under the "five year certain term", but provision is made for payments to a beneficiary if the pensioner dies within 10 years of commencement of receipt of pension. The "life Pension with no Term Certain Guarantees" provides for larger monthly payments than the five and ten year models, but provision is made for the duration of the lifetime of the pensioner only. Under the contingent beneficiary option, provision is made for a lifelong retirement pension for the pensioner and named beneficiary contingent on his/her surviving the pensioner.

The retiree's preference of plan is greatly influenced by his certain knowledge of the level of benefit provided in retirement, and hence the "defined benefit plan' has gained ascendancy over the "defined contribution plan". In a

comprehensive assessment of the merits of both plans, we need to consider the different levels of cost associated with a particular level of benefit; burdens of the regulatory environment on suppliers; responsiveness of plans to the financial needs of younger or older workers; and the ease and cost of administration.

At the end of 1995 there were about 10,000 persons covered by private pension plans. The main suppliers of supplemental pension plans in Barbados are the Barbados Mutual Life Assurance, Colonial Life Insurance, Life of Barbados, Caribbean Home Insurance, and Maufacturers' Life whose portfolio has been managed by the Life of Barbados since it ceased writing new business in Barbados at the end of 1991. The Barbados Mutual Life dominates the market accounting for about 65 percent of plans in force at the end of 1995. At 31st December 1995 the value of Mutual Life segregated pension funds stood at $262 million.[37] The Mutual Life attracted the business of 140 companies and provided management services for all of them except eight. Their plans provided benefits for approximately 5,100 employees and 700 pensioners.

Financing of Supplemental Pension Plans

The most important element in pension funding is the investment return on the pension fund. A pension fund has to be substantial in order to provide such diversification of assets as would provide adequate security. In April, 1969 the Mutual Life Society established two registered Unit Trusts in Barbados, namely, the Barbados Mutual (Bonds) Fund, and the Barbados Mutual (Equity) Fund. The Unit Trusts are referred to as the Segregated Funds, because the assets are held apart from the Society's General Life Fund.

Pension fund suppliers offer investment management and administration services to companies, groups, and individuals interested in purchasing pension plans. In the case of the Mutual Life purchasers are offered investment in either or both of the two Unit Trusts in proportions chosen by them. Administration services include design of plans, computerized record keeping, regular monthly billing, payment of pensions and other benefits, and optional provision of actuarial advice.

---

[37] The Mutual, Annual Report 1995, Segregated Pension Funds - Barbados. p. 4.

Financing Issues

Central Government and social security pensions are financed on a pay-as-you-go basis. The essence of pay-as-you-go systems is the financing of current pensions expenditure out of current revenue. This method of operation renders a scheme vulnerable to adverse developments in any one of many unstable social and economic factors. Table 3.1 shows that Central Government expenditure incurred on pensions ranged between 4.4 percent and 6.0 percent of recurrent expenditure during 1974 - 1995.

Government's ability to restrain its pension expenditure after 1980 was assisted by its decision to transfer the financing of Non-Contributory old Age Pensions (NCOAP) to the National Insurance Scheme (NIS) after 1981. While reducing the financial burden of the NCOAP on the Consolidated Fund, the switch in source of financing transferred a substantial cost to the NIS Fund. The formula devised for implementing for financing the NCOAP after 1981 was a 4.0 percent levy on insurable earnings shared equally by employers and employees. Occasionally the proceeds from the levy proved inadequate to defray the cost of the NCOAP and was subsidized by the National Insurance Fund. The cost of pensions to Central Government was reduced substantially through a series of legislative actions designed to remove areas of duplication consequent upon the introduction of the Social Security Scheme in 1966. By design, as well as through fortuitous circumstances the State has avoided a crisis in financing its unfunded pensions bill.

Social Security Pensions

Because the NIS benefits are financed on a pay-as-you-go basis whereby current revenues are used to pay current benefits in the early years of the scheme benefits expenditures were low compared to revenue. Prior to Government's decision to transfer the NCOAP from the Consolidated Fund to the NIS Fund the portion of NIS benefits allocated to pensions increased gradually between 1974 and 1982 from 13.5 percent to 43.4 percent in 1981. Between 1981 and 1982 the NIS pensions expenditure grew by 172.2 percent, due mainly to the transfer of the NCOAP to the NIS Fund.

After 1982 the pensions share of NIS benefits expenditure grew rapidly from 43.4 percent in 1981 to 108.9 percent of Contribution Revenue in 1993. In

order to meet its liabilities the NIS was forced to utilize investment income to subsidize the cost of benefits in 1993. In addition to financing the NCOAP, the financing costs of the NIS scheme have been increased through the slow reduction in the number of non-contributory old age pensioners, increases in longevity which exceeded projections, and non-compliance by substantial numbers of self-employed persons and employers.

In order to increase the revenue of the NIS to meet benefits expenditure the insurable earnings ceiling was increased from BDS.$212.50 per month 1967 to $3100.00 in October 1991. The current insurable earnings ceiling is BDS.$3100 per month. Increases in the earnings ceiling provide temporary relief in meeting liabilities but increases the level of liabilities which the PAYG system is required to fund in future years. The critical financing issue is the ability of the system to pay expected benefits to future generations of retirees.

Investment Income

Table 3.5 shows that during 1991 - 1995 investment income grew slowly, 1993 being the exception. The distribution of the NIS investments shows a concentration in Government paper reflecting the existence of narrow financial and capital markets and Government's financing requirements.

Dependency Burden

Table 3.3 shows that the ratio of pensioners to employed persons increased from 25.6 in 1975 to 29.6 in 1994. The implications for a pay-as-you-go system are ominous, because as the pensions bill increases a declining portion of the population will be required to generate the required revenue. The pensions bill is expected to increase over time because retirees are living longer, and increases in minimum pensions occur at least twice in every decade.

Assuming that no adjustments in the minimum pension takes place the prognosis is that either the insurable earnings ceiling will be raised to generate a higher level of contribution revenue, or other devices such as tightening of eligibility criteria, and stricter enforcement of regulations pertaining to qualification criteria for the NCOAP will be implemented. The continued rise in the dependency burden erodes the potential for earning investment income as pensions expenditure claims exceed total contribution revenue. A critical

issue which confronts policy makers is the long term viability of the current model.

Reform of the Pensions System

The case for reform of the existing pensions system rests on two substantial grounds. The analysis has identified the inability of the present model to meet its obligations at some time in the future, and secondly the piecemeal structure of the current system. A plethora of legislation provides the legal framework for public service pensions. Since all public servants are paid from the same source and are covered by some form of pensions programme, it is appropriate to repeal the existing Acts pertaining to pensions and replace them by a standardized, comprehensive pensions law which ensures that all public service workers are provided with similar pensions conditions.

The tidying up operation should seek to address the articulation of a comprehensive national pensions policy which attempts to integrate public service, social security, and private pensions planning. The current legislation addresses integration of public service and social security pensions by providing that workers entering the public service after 1st July, 1975 will be eligible for pensions only on that portion of salary which exceeds the NIS insurable earnings ceiling.

Integration of the national pensions framework should attempt to lay a coherent foundation for planning at all levels including private pensions schemes. At present suppliers of private pensions schemes do not have access to national policy guidelines pertaining to pensions. Private sector providers of pensions plans determine the ceiling of their schemes by fixing it at about 2/3 of the insured person's pre-retirement salary when combined with the NIS retirement pension. Private plans are therefore additive in relation to the NIS pension. The methodology adopted by private suppliers in computing the target retirement pension is to take a percentage of an insured person's annual salary, which is then reduced by some factor of the NIS pension for each year of service. For example, where a person works for thirty-three years, the NIS plan is reduced by one-third.

Integration of private and public sector pensions planning should address the issues of establishing ceilings, protection of pensions value, and development and regulation of private pensions schemes. The fixing of NIS insurable

earnings ceilings is critical to orderly development of the market for supplemental pensions schemes, because the NIS ceiling is employed as the base line of planning by the suppliers of private plans. Since 1967 no clearly defined principles have informed the setting and adjustment of the insurable earnings ceiling, specifically with respect to the level and timing of adjustment. In the past the matter of adjustment and timing appears to be informed by political expediency. This modus operandi has created an environment which is inimical to effective management and orderly planning.

Reform of the pensions system may incorporate a modified aspect of the United Kingdom (1960)[38] reforms and develop a two-tiered national pension scheme which is comprised of a "Minimum Earnings Related Pension" provided by the NIS and a supplemental pension provided by private suppliers. The NIS pension ceiling could be targeted at covering the middle income worker. Workers desirous of planning for a higher retirement pension should be encouraged to purchase additional retirement insurance from the private market.

With respect to the adjustment of the NIS insurable earnings ceiling the central issue pertains to protection of the value of pensions. The critical issue is not indexation *per se* but indexation to what. The literature discusses indexation employing wages or prices as the basis for adjustment.[39] This paper argues in support of using the wage index because wages are employed as the basis for determining insurable earnings ceilings and contribution rates and not price levels. In principle, some band could be fixed within which the real value of pensions could be allowed to vary.

In order to eliminate the *ad hoc* nature of adjustments in pension entitlements and contributions rates, a law should be passed requiring a mandatory actuarial review prior to any change in the level of entitlements, or contribution rates. The review findings should quantify the costs of the proposed pensions adjustments, and specify measures to raise the required revenue to ensure continued viability of the scheme if such action is necessary. The law should

---

[38] Goodman, John. Social Security in the United Kingdom: Contracting Out of the System. American Enterprise Institute, Washington, 1981.

[39] Kaplan, Robert. S. Indexing Social Security. American Enterprise for Policy Research. Washington D.C. 1977.

stipulate that the review findings be made public and be disseminated as widely as possible.

CAP. 47 of the Laws of Barbados (1971) provides for a mandatory actuarial review of the National Insurance Scheme every three years. This law needs to be changed to provide for a more frequent review of the performance of the Scheme. The record shows that by the time an actuarial review is completed and the report laid in Parliament the recommendations no longer relate to the current situation. The provision pertaining to actuarial review of the Scheme would have been adequate in its early years, but in light of the rapid growth in benefits expenditure with consequential pressure on contribution revenue and investment income, provision needs to be made for ongoing actuarial review of the Scheme.

In addition to adopting a "Minimum Pensions" provision as one tier in the NIS model, we may consider "contracting out" as one means of reducing demand on the NIS for liberalization of pension entitlements. Employing this method, part of the benefit is taken out of social security and provided by a private plan instead, provided the benefit is equivalent. "Contracting out" has the potential to stimulate private sector pension planning, retain resources in the private sector, reduce public expenditures on pensions, offer employees greater flexibility in designing a benefit package and create an environment where workers are encouraged to take responsibility for the planning of their retirement benefits.

Development of a national pensions policy places the onus on the State to address the issue of appropriate mechanisms for development of private sector pension plans. At present, the suppliers of private plans are required to register with the Department of Inland Revenue and apply to the Commissioner of that Department for approval so that they can benefit from the relevant tax concessions under the Income Tax Act. The relationship between the providers and the Department of Inland Revenue is primarily concerned with regulation for tax purposes, and fails to address the issue of developing the market for private pension plans. Matters such as investment planning, reserves management and actuarial advice which are central to pension planning are not the concern of the Department. The reform programme should provide for the inclusion of these roles in the remit of the overseeing public sector agency in order to pay adequate attention to developmental policy issues.

Conclusion

During the last three decades substantial progress has been made in enhancing the content of pensions systems and extending coverage to the pensionable population. Passage of the 1947 Public Officers' Pension Act, the National Insurance and Social Security Act (1966); government's decision in 1990 that all public officers be provided with pension arrangements, and the emergence of private sector suppliers of pension plans constitute significant landmarks in the evolution of pensions systems in Barbados.

The substantial advances recorded create an agenda for further refinement and development. Extensions in coverage of the population, and increasing longevity have combined to put pressure on the pay-as-you-go system of financing pensions. These financing difficulties which surfaced in the early 1990's emphasize the necessity to search for an appropriate pensions model which engenders confidence in the working population that they will receive pensions in retirement.

Emergence of private sector providers of pensions plans underlines the need for articulation by the State of a national pensions policy which provides a coherent framework for integrating private and public sector pensions planning. Finally a rationalization of the several pieces of public sector pensions laws is required to provide a single unified law governing provision of public officers pensions.

References

International Social Security Association. (1987), "Conjugating Public and Private: The Case of Pensions," *Studies and Research*, No. 24, Geneva.

Feraud, Lucien. (1975), "Complementary Pensions: A Comparative Analysis," *Studies and Research*, No. 7. International Social Security Association, Geneva.

International Social Security Association. "Complementary Pension Or Complementary Pension Schemes," *Studies and Research*, No.3, Geneva, 1973.

Mesa-Lago, C. (1984), *Changing Social Security In Latin America*, Lynne Rienner, London.

Ferrara, Peter, J. (1985), "Reform Proposals," in P.J. Ferrara (ed.) *Social Security: Prospects for Real Reform*, Cato Institute.

Kaplan R. S. (1977), *Indexing Social Security*, American Enterprises for Policy Research. Washington, D.C. 1977.

_____. (1976), "Financial Crisis in the Social Security System," American Enterprise Institute for Policy Research, Washington, D.C.

Thullen, P. (1985), "The Financing of Social Pensions: Principles; Current Issues and Trends" in Carmen Mesa-Lago (ed.) *The Crisis Of Social Security and Health Care*, Latin American Monograph and Document Series, No.9.

Morgn Victor, E. (1984), "Choice In Pensions," Institute of Economic Affairs, London.

International Social Security Association, Intemational Social Security Review, Vol.49, 2/96. "Social Security In The 1990's: The Imperatives Of Change" pp 5 -15, and " "Expanding Role Of Private Pensions" pp 33 -48. Geneva, 1996.

APPENDIX

Table 3.1
Pensions Expressed as a Percentage of Recurrent Expenditure (1975/76 - 1994/95)

Year	Recurrent Expenditure ($Millions)	Pensions Expenditure ($Millions)	Pensions as a % of Recurrent Expenditure
1975-76	174,405	8,049	4.6
1976-77	212,332	11,748	5.5
1977-78	240,241	12,873	5.4
1978-79	264,060	14,686	5.6
1979-80	314,586	16,695	5.3
1980-81	494,982	19,727	4.0
1981-82	450,203	22,290	5.0
1982-83	577,164	26,298	4.6
1983-84	587,252	29,861	5.1
1984-85	559,810	33,942	6.1
1985-86	626,326	35,490	5.7
1986-87	627,211	40,376	6.4
1987-88	848,063	42,287	5.0
1988-89	880,930	48,119	5.5
1989-90	951,708	52,269	5.5
1990-91	957,268	54,646	5.7
1991-92	921,460	63,414	6.9
1992-93	941,061	67,000	7.1
1993-94	954,137	64,318	6.7
1994-95	990,220	64,000	6.5

Source:Auditor General's Report, Government of Barbados. 1976 - 1995
Estimates of Revenue and Expenditure, 1974 - 1995

Table 3.2
Pensions Expressed as a Percentage of Contribution Revenue (1974 - 1995)

Year	Pensions Expenditure ($000)	Contribution Revenue ($000)	Pensions as % of Contributions
1974	1,836	13,609	13.5
1975	3,371	14,225	23.7
1976	4,357	15,863	27.5
1977	5,293	18,320	28.9
1978	7,027	24,458	28.7
1979	8,328	31,382	26.5
1980	11,471	34,057	33.7
1981	17,932	41,287	43.4
1982	48,117	67,573	71.2
1983	57,479	83,006	69.2
1984	68,243	91,916	74.2
1985	72,843	99,615	68.5
1986	86,125	105,685	81.5
1987	93,098	115,765	80.4
1988	97,198	122,113	79.6
1989	108,288	139,941	78.5
1990	116,510	133,866	87.0
1991	132,581	142,600	93.0
1992	135,378	134,529	100.6
1993	137,798	126,591	108.9
1994	142,930	160,234	84.5
1995	150,365	182,572	82.4

Source: Economic and Financial Statistics. Central Bank Barbados, Dec. 1995
National Insurance Board Annual Reports, 1974 - 1984 and 1988 - 1995.

Table 3.3 - Dependency Ratios (1975 - 1991)

Year	Dependent Population as % of Active Workforce
1975	23.6
1976	23.6
1977	27.4
1978	26.9
1979	24.5
1980	25.7
1981	26.3
1982	28.9
1983	29.7
1984	31.4
1985	31.7
1986	31.2
1987	30.9
1988	30.4
1989	30.0
1990	29.5
1991	31.1
1992	32.5
1993	33.1
1994	29.6

Source: Annual Statistical Digest. Central Bank of Barbados, 1977-1995
National Insurance Board. Annual Reports, 1968-1984 and 1988 - 1995

Table 3.4
Investment Income (1967 - 1995)

Year	Income ($m)	Average Yield	Net Return
1967	0.25	--	--
1968	0.25	4.96	-3.44
1969	0.65	6.35	2.45
1970	1.13	6.96	--0.64
1971	1.67	7.09	0.01
1972	1.97	7.23	--3.68
1973	2.76	6.93	--12.77
1974	4.64	--	
1975	5.69	--	--
1976	5.73	--	--
1977	6.28	--	--
1978	6.63	--	--
1979	9.09	6.66	-6.4
1980	11.3	6.97	-7.43
1981	11.7	6.14	-8.46
1982	19.9	10.05	-0.25
1983	28.3	12.22	6.92
1984	22.4	7.87	3.27
1985	28.3	7.72	3.83
1986	22.4	6.14	4.80
1987	25.5	7.03	3.67
1988	22.4	6.20	1.43
1989	27.7	5.80	-0.47
1990	25.6	6.70	3.59
1991	26.4	7.91	1.51
1992	32.4	8.70	2.45
1993	50.9	6.60	2.80
1994	43.3	7.10	6.10
1995	49.0	7.60	5.70

Source: Actuarial Reports, National Insurance Scheme of Barbados.
1972, 1977, 1979, 1982, 1985, 1988, 1990, 1996
National Insurance Board Reports. 1994, 1995

Table 3.5
Pensioners as Percentage of Labour Force (1988 - 1995)

Year	Labour Force (000)	Insured Population as % of Labour Force	Pensioners as % of Labour Force	Pensioners as % of Labour Force
1988	121.4	79.6	25.0	32.0
1989	122.0	74.2	25.4	34.0
1990	123.9	73.1	25.1	34.0
1991	122.5	77.9	25.6	33.0
1992	124.8	70.6	25.1	36.0
1993	124.3	69.8	25.4	36.0
1994	131.1	70.9	24.1	34.0
1995	136.7	69.3	23.2	33.0

Source: Eighth Actuarial Review of the National Insurance Scheme, December 1993.
National Insurance Board Annual Report. 1994, 1995.

Table 3.6
Proportion of Labour Force Covered by Pension Program (1988 - 1995)

Year	Old Age Contributory	Non-Contributory	Survivors	Invalidity	Disablement
1988	9.1	9.1	0.01	0.01	0.01
1989	9.5	9.5	0.01	0.01	0.01
1990	9.8	9.8	0.01	0.01	0.01
1991	9.7	10.3	0.01	0.01	0.01
1992	9.8	10.3	0.01	0.01	0.01
1993	9.9	12.1	0.01	0.01	0.02
1994	9.9	11.2	0.01	0.01	0.02
1995	10.0	10.5	0.01	0.01	0.02

Source: Eighth Actuarial Review of the National Insurance Scheme, December 1993
National Insurance Board Annual Report. 1994, 1995.

CHAPTER 4

PENSION ARRANGEMENTS IN TRINIDAD AND TOBAGO

PENELOPE FORDE*

* The author is Chief Economist, Research Department, Central Bank of Trinidad and Tobago. The views expressed are those of the author and not necessarily those of the Central Bank of Trinidad and Tobago. This paper is an updated version of one chapter in an unpublished monograph. The monograph completed by the author in 1990 is entitled *The Insurance Industry in Trinidad and Tobago*, Research Department, Central Bank of Trinidad & Tobago, mimeo.

Introduction

Within recent times, the universal provision of pensions of one form or another has come to be considered a norm in both industrialised as well as developing countries. While this not entirely new in Trinidad and Tobago, it has important macroeconomic implications in respect of savings, institutional investment and tax policy. This paper is concerned with the nature and operations of pension funds in Trinidad and Tobago and how they impact on the wider macroeconomy.

The paper is divided into five sections, the first of which is definitional and conceptual in nature. The second section examines the current characteristics of the Trinidad and Tobago system of pensions and places this into perspective with particular reference to pension legislation. Section III considers the operating aspects of private pensions (occupational pensions) with special emphasis on the structure of their assets and investment strategy. Section IV is devoted to a discussion on the provision of pensions for the public sector employees; however there is no discussion of pensions which are provided by the National Insurance Board as this is described elsewhere in this book. Section V concludes with a miscellany of outstanding issues and an outlook for future areas of research.

Some Definitional and Conceptual Issues

Following Asimakopulos and Weldon (1968; 1970), pensions may be defined as payments made to individuals either because they have reached a certain age and retired from the labour force or from a particular job, or simply because they have reached a certain age.[1]

A "pure private pension plan" is one where pensions are paid out of the sums accumulated on behalf of individuals as a result of contributions made over their working lives. A "pure government pension plan" is one where the

[1] This definition of a pension is based on one view of the function of a pension that is to enjoy retirement rather than to endure old age. Other functions of pensions are - morale booster, tax protection, deferred salary or compulsory employee saving. It is this last function which has become more common in Trinidad and Tobago.

government uses its taxing power to transfer the command over goods from those who are of working age to those who are retired. The essence of a private pension plan is the payment of pensions out of past savings, while transfers between groups form the basis for a government pension plan. The current pension arrangements in existence in Trinidad and Tobago have elements of 'pure private' and 'pure government' plans and hence represent a mixed system.

Pension plans can be contributory or non contributory, self administered or insured (e.g. under deposit administration contracts), funded or a pay-as-you-go (PAYG) system. Under a PAYG system (non-funded), current contributions from wage earners provide pensions for previous workers in the labour force. With funded pension schemes, reserves are set aside to meet the expected future retirement benefits, for which contributions are made during the working life of the members. Most private plans tend to be funded, while public pensions tend to be a mixture of fully funded and partly funded plans.

Private pension plans can be of the contributory or non-contributory variety, but in general employees contribute towards their pension benefits.[2] Private pension plans are sometimes called occupational pension plans because they are closely associated with an individual's occupational status. Similarly pension plans can be self administered (by trustees) or under deposit administration with an insurance company, and some occupational schemes fall within this category. At present the current arrangements in Trinidad and Tobago consist of private or occupational pension plans - self administered and insured plans - and the public pension system which is by and large of the PAYG variety. Pensions are also available under the National Insurance System (NIS) and non-contributory old age pension (OAP) system, but these two latter systems will not be discussed in the paper.

The provision of pensions raises some interesting issues for labour, insurance companies and financial markets. In the case of labour, pensions may be seen as an incentive for long-term employment, an aid to recruitment and

---

[2] Odle (1974) noted that pension schemes in the petroleum sector were non contributory for top management. This system may have changed somewhat within recent times, but only a proper analysis of individual pension plans will reveal this. See Kotlikoff and Smith (1983) for their detailed analysis of pensions in the American economy.

good industrial relations. However beyond a certain retirement age, pensions can be a disincentive if an individual is able and willing to continue his employment. With respect to the insurance industry, the existence of employer-sponsored pension schemes may affect the micro distribution between group pensions, annuities and even the purchase of life insurance. In Trinidad and Tobago, there is a small private market in annuities, whose growth in the last decade may have been fueled by tax considerations. However for many companies whose employee base is fairly small, it may be more efficient to provide individual annuities than group pensions. Given the size of pension funds, the managers of these funds are important actors in financial markets, because of their investment decisions. Finally, pensions may affect the overall savings rate because benefits accrued are illiquid and individuals cannot borrow against these funds.[3] Thus individuals may increase their total savings more than they may otherwise would have done. In the discussion which follows some of these issues will be highlighted where they are relevant to the discussion.

Trends in Occupational Pension Funds in Trinidad and Tobago

At the end of 1992 there were 216 registered pension plans, 71 of which were self-administered. The total assets of 57 of the self-administered plans amounted to TT$3,755.3 million, 9 per cent of which were locally invested.[4] This compares with assets of TT$84.5 million in 1971 for 19 self-administered plans out of a total of 63 registered plans. Growth in the registration of pension funds has been steady and consistent during the 1970s, 1980s and early 1990s.

Table 4.1 indicates that the number of registered occupational pension plans increased from 63 in 1971 to 216 in 1992. Between 1971 and 1973 there were 35 plans registered, but these reflected the backlog of plans which were

---

[3] This may have been true until fairly recently. However several mechanisms have been proposed whereby it may be possible to access pension funds long before retirement. See the discussion in the next section and footnote 14 below.

[4] In compliance with the requirements of the Insurance Act 1980, the trustees of all pension fund plans are required to submit annual audited accounts to the Supervisor of Insurance. However few of these returns are submitted on time to be included in the aggregate accounts and this has resulted in an almost two year lag in current information on the insurance industry. As of writing (March 1996) the latest data available relate to the year 1992.

registered on the basis of the 1966 Insurance Act. Since then there has been a steady increase in new plans registered with peaks in 1976 and 1981. More than one half of all plans registered are insured plans that are administered by insurance companies under deposit administration contracts, while 75 plans are self-administered. These plans are administered primarily by "commercial bank" trustees.

Table 4.1 - Pension Plans Registered, Selected Years

Year	PENSION FUND PLANS REGISTERED				Plans Amended
	of which				
	Total	Insured[1]	Self Administered	Plans Cancelled	
1971	63	44	19	na	na
1972	76	53	23	na	na
1973	98	75	23	na	na
1974	103	70	33	2	17
1975	110	76	34	--	7
1976	123	84	39	--	3
1978	136	96	40	2	4
1980	144	102	42	--	2
1981	154	10	47	2	5
1983	165	115	50	2	1
1984	171	118	53	--	12[2]
1986	181	124	57	8	15
1987	191	132	59	11	29
1988	199	140	59	2	21
1990	211	145	66	3	19
1992	216	142	71	3	na

Source: Annual Reports, Supervisor of Insurance

1 Insured plans i.e. those which are administered by an insurer under a deposit administration contract.

2 Two changed from insured to self administered.

In an analysis of the US pension system, Wise (1985) suggests that pension coverage go hand in hand with union representation, large establishment size and other economic compensation. Although similar data are not available for Trinidad and Tobago, the same general factors appear to be at work in the economy. Time series data are not available on the number of workers employed in the private and public sector who are covered by pensions. In general however most public sector employees are covered by the various public sector plans which are discussed in Section IV below. With respect to the private sector, no data are available on the number of employees with pension coverage. The lack of information in this area needs to be filled by a micro study along the lines of Kotlikoff and Smith (1983).

Table 4.2 details the number of occupational pension fund plans by industrial origin as at the end of 1973 and 1988. The Petroleum, Finance and Distribution sectors accounted for just over one half of all self administered plans in both 1973 and 1988; the Manufacturing, Finance and Distribution sectors account for about 55 per cent of all insured plans for the two selected years. Data on union membership are unavailable so that the correlation between the two variables cannot be made. The evidence suggests, however, that pension coverage has been determined primarily by the structure of the economy i.e. dominance of Petroleum, Distribution and Finance sectors.[5] This evidence supports Odle (1974) who also found that schemes in the Manufacturing and Distribution sectors dominated all others. Odle noted that the growth of pension funds in Trinidad and Tobago was a post war phenomenon, since of all the plans registered in 1971, only one had commenced operations before 1939. In Table 4.3 given below, the data prior to 1971 are reproduced from Odle (1974) and the series is then updated. The large number of plans registered in the 1970's reflects the growing strength of trade unions in negotiating benefits for their workers.

Most private pension plans are administered under deposit administration contracts with insurance companies. There appears to be no relationship between industrial sector and choice of method of pension schemes. However, of the self-administered schemes, over 90 per cent of them are bank trusteed. One reason for the dominance of insured plans is that when employment in a

[5] Although thirty-three plans are classified as belonging to manufacturing sector very many of these plans are related to the petroleum and energy based sectors.

Table 4.2 - Pension Plans Registered: By Industrial Origin, 1973 and 1988

Sector	Self Administered		Insured	
	1973	1988	1973	1988
Agriculture	--	--	4	3
Petroleum	7	15	9	11
Manufacturing	--	4	25	33
Electricity and Water	2	3	2	
Construction	--	--	2	3
Transport, Storage and Communication	2	10	4	19
Distribution	4	7	12	19
Finance	7	15	4	24
Hotels and Guest Houses	--	1	1	--
Education and Community Services	--	2	6	2
Personal Services	--	1	5	16
N.E.S	--	2	2	10
TOTAL	22	59	75	140

Source: Based on data from the Annual Reports, Supervisor of Insurance.
Note: In some sectors there are multi-employer schemes so that a large proportion of total contributions relate to a small number of firms

Table 4.3 - Date of Commencement of All Pension Fund Plans Registered as at December 31, 1990

Year	NUMBER OF PENSION SCHEMES		
	Registered	Cancelled	Mergers
Pre 1939	1	--	--
1940 - 1950	12	na	na
1951 - 1960	27	na	na
1961 - 1965	25	na	na
1966 - 1971	88	na	na
1972 - 1979	79	4	--
1980 - 1990	81	32	3

Source: Odle (1974) and based on data from Annual Reports, Supervisor of Insurance.

company is relatively small it may be preferable to have the plans managed under contracts, rather than by individual or corporate trustees.

The Legislative Framework

Prior to the 1966 Insurance Act, pension plans were not governed by any particular law. Amendments to the Income Tax Ordinance Chapter 33 No. 1. (Ordinance No. 25 of 1941, Sections 4 (ii), 5 and 6) gave employers relief from taxation of contributions to Provident Funds and pension schemes. Most pension funds or schemes were approved by the Governor in Council and once approved, there was no statutory right or power to inspect the books or supervise funds in existence.[6] Under the 1966 Insurance Act *all* pension plans, for which a fund is established under trust, had to be registered with the Office of the Supervisor of Insurance (OSI). Provisions were introduced whereby trustees of all plans were required to submit revenue accounts. For those plans which were self-administered, the trustees had to prepare an annual balance sheet for submission. In the case of insured plans, that is, those under deposit administration contracts, the balance sheets would naturally form part of the insurance company's balance sheet.

Investment ratios were stipulated for the investment of these funds in the same manner as the statutory funds of life insurance companies. The local asset ratio was set at 60 per cent in 1971 and in 1976 increased to 80 per cent. Finally the Act provided for actuarial investigations of each plan from time to time. Under the present legislation, the Insurance Act 1980, these investigations must be undertaken every three years.

Legislation in the United States and the United Kingdom established minimum standards for pensions which originate in the private sector.[7] These standards

---

[6] See Government of Trinidad and Tobago (GOTT), Report of the Committee Appointed by Government to Consider and to Recommend Provisions for the Approval of Private Superannuation Schemes (1961).

[7] In the United States the Employee Retirement Security Act (ERISA) was enacted in 1974. In the United Kingdom, the Social Security Acts of 1985 and 1986 introduced a significant number of changes to pension schemes as well as controls on them. In the wake of the death of Robert Maxwell and the problems with the pensions of the newspaper group, a Committee under the chairmanship of Lord Goode examined pension laws in the UK and recommended certain revisions. Details of these recommendations have not been available for inclusion in this paper.

relate to pension participation, vesting, portability and minimum retirement ages. In Trinidad and Tobago, except for the public sector plans, the laws are silent on minimum standards and are concerned instead with regular reporting and the actuarial soundness of plans. In respect of pension participation, most private plans tend to specify a minimum age as well as a service requirement.

Vested pension benefits are defined as benefits to which the worker has a legal claim based on past work experience. If the worker chooses to leave the firm before he or she attains normal or early retirement age, the pension plan sponsor is legally obligated to pay a benefit to the worker. In the UK and US, by law, employers must "vest" their workers after some maximum period of time. 'Cliff Vesting' - vesting after ten years of service, but no vesting prior to ten years - is typical in the US. Data on vesting pattems are not readily available for Trinidad and Tobago. However, on the basis of Section 28(1) (1) of the Income Tax Act (Chap. 75:01), one can infer that vesting usually occurs after five years. Refund of contribution to a plan is payable on withdrawal before five years or for any other reason. In the post 1983 period, as the economy experienced a period of declining income, many individuals have been able to obtain refunds even after five years have elapsed. In this regard individuals have been able to justify to the tax authorities the need for the refunds on a case by case basis.

Pension portability can be defined as the ability of a terminating employee to transfer the value of his/her pension credits to another employer's pension plan. In Trinidad and Tobago, pension portability is not a common occurrence in the private sector and indeed rarely occurs between the public and private sector. In the case of the public sector which operates on a PAYG system, portability to the private sector is clearly difficult to achieve.

The Assets and Liabilities of Occupational Pension Funds

The Insurance Act 1980 requires that only trustees of self administered pension plans submit balance sheets, because balance sheet data on insured plans will generally form part of the operations of life insurance companies. Table 4.4 therefore shows the distribution of assets for self-administered pension plans for selected years.[8] Local assets dominate total assets, averaging

[8] These data related to approximately one half of the self-administered plans.

around 90 per cent of the total assets in the post 1975 period and this is in keeping with the thrust of the provisions of the 1966 Insurance Act which set a limit on the local assets ratios of pension funds. Between 1971 and 1975 government securities accounted for about one third of total assets, mortgage loans 3.7 per cent, equities 2.7 per cent and foreign securities 37 per cent.

Table 4.4 - Pension Fund Plans: Self Administered - Total Assets for Selected Years /TT$000/

Year	Total Assets	TT Gov't Securities	Mortgage Loans	TT Company Equities	Other Local Assets	Foreing Assets
1967	39.7	N.A.	N.A.	N.A.	N.A.	N.A.
1970	69.6	24.6	2.6	1.9	14.5	26.0
1972	97.4	56.0	3.5	4.7	19.5	13.7
1975	148.6	46.5	15.6	13.0	58.3	15.2
1977	277.6	86.2	51.8	44.7	65.1	29.8
1980	550.9	88.1	158.5	82.7	176.1	45.5
1983	972.4	71.8	301.3	241.5	298.6	59.2
1985	1,135.0	105.0	314.4	181.3	513.9	20.4
1986	1,353.3	135.9	352.9	186.3	661.8	16.3
1987	1,653.5	190.7	397.1	190.6	845.5	29.6
1988	1,680.5	214.6	346.2	153.6	736.4	22.0
1989	1,646.7	308.3	288.4	151.1	891.7	7.2
1990	2,034.5	591.0	275.2	229.6	928.6	1.2
1991	2,867.8	989.3	321.7	316.4	1,201.3	39.1
1992	3,755.3	1,083.7	390.1	319.4	1,740.0	222.1

Source: Annual Reports, Supervisor of Insurance

Between 1980 and 1984, however, government securities declined in importance relative to mortgage loans and equities. The shift in the composition reflected one aspect of the boom in economic activity in the 1970's, which was fuelled by the two oil shocks. This had generated increased incomes and as a consequence an increase in the demand for housing. However at the onset of a severe recession which began around 1983, this had a significant impact on the stock market and real estate. Thus by 1984 investments in these areas were being reduced and investment in government securities rebounded, as the central government increasingly sought financing from the domestic market. In contrast real estate and foreign assets were relatively unimportant in the portfolios of pension funds. The rise in importance of equities reflected the increased availability of this type of instrument during the late 1970's and early 1980's. The collapse of the stock market in the 1980's meant however that this type of investment lost its attractiveness for the institutional investors. Between 1985 and 1992 there has been a switch in the composition of the portfolios of pension funds as fixed deposits now account for almost half of total assets. This has occurred against the background of falling values in the real estate market, given the slowdown in economic activity, and the limited investment opportunities available. The preference for fixed deposits suggested a greater bias towards income certainty.

It is interesting to compare the investment behaviour of pension funds in Trinidad and Tobago with their counterparts in the developed economies. Davis (1988) presents comparable data on holdings of monetary assets, fixed interest bearing assets, and the holdings of real assets for five highly industrialised economies. In respect of self-administered pension funds, comparable data are assembled in Table 4.5 for Trinidad and Tobago. The evidence suggests that pension fund managers have been fairly conservative and invest in fixed-interest bearing assets with a relatively safe rate of return, rather than in the holdings of real assets.

Section 185 of the Insurance Act 1980 requires that each registered plan be submitted for actuarial valuation every three years. However, each year different plans are investigated, so that an aggregate analysis of the discrepancy between the market value of assets and liabilities is difficult to assess at any one time. Any meaningful assessment can be made only at a point in time - for example, during 1988, actuarial valuations of 46 registered pension plans were completed and 27 of these plans held assets greater than their liabilities. When Odle examined a subset of plans for the year 1969, he found that for

Table 4.5 - Characteristics of the Portfolios of Self Administered Pension Plans for Selected Years

	As a Proportion of Total Assets		
	1970	1980	1985
A. Marketable Securities[1]			
U.K.	0.85	0.79	0.86
U.S.	0.90	0.86	0.87
Canada	0.77	0.73	0.9
Japan	0.26	0.62	0.64
Germany	0.23	0.34	0.44
Trinidad and Tobago	0.38	0.31	0.25
B. Real Assets[2]			
U.K.	0.61	0.70	0.74
U.S.	0.45	0.41	0.44
Canada	0.23	0.20	0.27
Japan	0.36	-0.15	0.19
Germany	0.17	0.18	0.19
Trinidad and Tobago	0.02	0.15	0.16
C. Capital Uncertain Assets[3]			
U.K.	0.93	-0.94	0.94
U.S.	0.90	0.82	0.85
Canada	0.76	0.70	0.76
Japan	0.50	0.67	0.67
Germany	0.36	0.42	0.51
Trinidad and Tobago	0.38	0.31	0.21
D. Fixed Interest Bearing Assets			
U.K.	0.32	0.24	0.20
U.S.	0.51	0.43	0.42
Canada	0.65	0.63	0.56
Japan	0.14	0.52	0.48
Germany	0.69	0.76	0.79
Trinidad and Tobago	0.39	0.44	0.37
E. Bonds			
U.K.	0.32	0.24	0.20
U.S.	0.45	0.41	0.41
Canada	0.53	0.50	0.49
Japan	0.14	0.52	0.42
Germany	0.19	0.24	0.32
Trinidad and Tobago	0.35	0.16	0.09

Source: Davis (1988).
Note: Categories overlap so that they do not add up.

1 Equities, bonds and market paper.
2 Equities and property.
3 Bonds, mortgages (Canada, U.S., Germany) and other loans (Germany).

only four of the 16 schemes were assets greater than liabilities. Odle suggested that the shortfall was due to the shortfall in holdings rather than fluctuations in market value. However as regular valuations were mandated under the Insurance Act, this ensured that plans were examined regularly to determine their solvency and action taken to follow the recommendations of the actuaries.

The liabilities of pension plans are the reserves which are set aside to meet future commitments, for which contributions are made over the lifetime of a worker. Benefits can be given in the form of superannuations, gratuities or death grants. By law, actuarial valuations must be carried out every three years to determine the solvency of the plans. However changes in membership of a plan as well as changes in the number of pensioners in the intervaluation period can have an effect on the pension funds. Table 6 details data on self-administered pension funds as well as on other types of funds. The size of accumulated funds for self-administered pension funds grew from TT$61.5 million in 1970 to TT$2,189 million in 1990, compared with insured funds which increased from TT$10.6 million to TT$539 million over the same period. Although there are more insured plans than self-administered, the actual size of the funds of the latter are larger than the former. In his study Odle found that even within the self-administered schemes, some were more important than others. Thus at the end of 1990, some twelve plans accounted for 75 per cent of the total funds.

A few life insurance companies are involved in group pensions; the data show that in terms of size, these accounts are not as significant as the two main categories. The existence of different employer-sponsored schemes has ensured that the market in annuities is very small. As already noted, in some companies given the small size of the employed staff annuity type arrangements are more appropriate. During the boom period of the mid-1970's and early eighties however, because of high marginal tax rates of 70 per cent many individuals used annuities as tax shelters. Despite tax reform introduced in 1988, the fact that premiums for annuities and occupational pension plans are now tax deductible has allowed for continued growth in this area. However there is not enough data nor research available to suggest whether individuals are diversifying their savings portfolios among different saving instruments.

Table 4.6 - Pension Funds: Value of Funds for Different Types of Pension Funds for Selected Years /TT$000/

Year	Group Pensions	Insured Plans	Self Administered Plans	Annuity
1970	4,436	10,618	61,569	N.A.
1971	4,268	15,722	82,712	233
1972	4,939	19,939	95,044	221
1973	4,962	25,369	102,480	240
1974	5,067	29,429	106,931	494
1975	8,504	37,347	147,944	654
1976	9,361	45,144	224,021	1,048
1977	9,971	58,779	275,705	1,883
1978	15,259	63,857	325,323	1,948
1979	23,684	69,936	278,518	3,727
1980	41,142	95,368	538,851	2,950
1981	47,811	96,402	517,689	1,869
1982	39,928	118,865	706,704	1,472
1983	46,467	134,362	935,003	N.A.
1984	62,748	207,833	836,861	7,425
1985	75,728	279,034	863,348	6,641
1986	161,378	447,300	1,509,203	16,544
1987	185,978	365,102	1,615,019	7,740
1988	276,179	423,181	1,766,054	11,822
1989	329,386	513,171	1,691,176	13,837
1990	473,365	539,019	2,189,490	14,660
1991	475,918	780,200	3,360,671	20,076
1992	526,818	859,961	3,661,967	18,195

Source: Annual Reports, Supervisor of Insurance.

The Provision of Pensions for Public Service Employees

> *"The legislative basis of pension arrangements for public officers and employees of Statutory Authorities are long established. The cornerstone is set out in the Pensions Act Chapter 23.52 (formerly Pensions Ordinance Chp. 9 No. 6) and first came into effect on August 1, 1934. The arrangements started within the context of the colonial system and has remained intact."*[9]

As was discussed earlier, what distinguishes occupational pension plans and public pensions is that the latter tend to be partially funded systems. In Trinidad and Tobago, most of the public sector plans are non-contributory and non-funded PAYG schemes.[10] Odle identifies several reasons, why the public sector pensions are usually non-contributory and un-funded. One reason is that the public sector is permanent and there are no 'risks' attached to the honouring of its commitments to retired members. A second reason is that the government has unlimited powers of taxation and so has the capacity to finance itself. In addition any funds collected would be invested largely in government bonds given the 'thinness' of the local securities market. However if a government operates a PAYG system in which public pensions are financed out of general revenues, this could occur at an embarrassing financial time. It is perhaps this important factor which justifies why governments should aim at the funding of pension plans in the public sector. Nevertheless the cost of funding pensions especially in respect of past service would be extremely prohibitive at this point in time. The straitened state of the government finances in the post 1986 period suggests that if a funded scheme were in existence, there would have been less pressures on the government for fiscal adjustment of the type that was introduced.[11]

---

[9] See GOTT. Final Report of the Pensions Review Committee, 1982.

[10] There are three exceptions to this: the Water and Sewerage Authority (WASA), the Industrial Development Corporation (IDC) and the Port Authority of Trinidad and Tobago. It must be noted that the IDC has been merged with another entity and no longer exists. As at the time of writing the author is unsure of the status of that pension plan.

[11] As a cost cutting measure, the government introduced proposals which would allow monthly paid employees under 60 years who were willing, to take early retirement i.e. Voluntary Termination of Employment Plan (VTEP). However, since the plan has been introduced certain key areas in the public service were not allowed to make use of VTEP. The plan would

In Trinidad and Tobago there are three basic categories of pensions for public officers. There are non-contributory pensions for pensionable establishment posts in the public service; contributory pensions (albeit nominal contributions) primarily for members of the Protective Services, Diplomats and for non pensionable officers; and the contributory Provident Funds which has since been superseded by an agreement with the National Union of Government and Federated Workers (NUGFW). Parliamentarians also make a nominal contribution for their pensions which accrue when they complete ten years service as a Member of Parliament (See Act 44 of 1976).

Table 4.7 attempts to summarise the benefits provided to most public officers under the various Pension Ordinances. For example an average public officer with ten years' service or more has a right to a pension, with the privilege of retirement from age 55 and onwards, with an immediate pension which is not actuarially reduced. The rate of accrual of pension benefits is l/50th of pensionable emoluments for each year of pensionable service, with the maximum pension benefits set at 2/3 of final pensionable emoluments, with full benefits earned after 33-1/3 years of service. On paper the public service pensions always appeared attractive, primarily because they were non-contributory with a high accrual rate. Pension benefits were portable within the public service and when officers were transferred to some state enterprises and similar bodies, in most instances they transferred their length of service and pension benefits with them.

Table 4.8 provides an estimate of the current costs of providing public service pensions. As is evident these costs have averaged well under 5 per cent of current expenditure over the 1970-1985 period, despite approximately *five* increases in the nominal amount in the twenty-two year period to 1988. In 1990 public pensions approached 8 per cent of current expenditure for the first time, in large part because expenditure on pensions and gratuities grew sharply in light of the VTEP Plan.

---

allow them to receive eligible benefits in cash and bonds. The target date of 1.11.88 was set but after much discussion and criticism was subsequently abandoned to allow the government enough time to present a second set of proposals. The evidence suggested however that most public sector workers who retired in the period 1988-1990 did not opt for VTEP, but had earned early retirement on the basis of 33 1/3 years of service.

Table 4.7 - Summary Characteristics of Public Sector Pension Provisions as at December 31, 1990

Group of Officers	Legislation	Rate of Accrual of Pension Benefits
Civil Service[1] Assisted Secondary School Teachers[1] Teachers[1] Statutory Authorities[1] Municipal Corporations[1] Prison Service[1]	Chp. 23:52 Chp. 39:03 Chp. 39:02 Chp. 23:53 Chp. 25:05 Chp. 13:02	1/50th pensionable emoluments for each year of pensionable service; the maximum pension is 2/3 of officer's final pensionable emoluments. Full pension benefits are earned after 33 1/3 years of service.[4]
Police Service[2] Fire Service[2]	Chp. 15:01 Chp. 35:50	1/40th pensionable salary for each year of pensionable service; the maximum pension is 85 percent of pensionable emoluments.[5]
Defence Force[3]	Act No. 7 of 1962	1/40th pensionable salary for each year of pensionable service; the maximum pension is 66 2/3 percent of pensionable salary.[6]

Source: Final Report of the Pensions Review Committee, 1982.

Notes:

(a) The compulsory age for retirement is 60 years; however in the Police and Fire Services, Second Division officers have a compulsory retirement age of 55 years; in the Defence Force this varies according to rank.

(b) For all public officers (except the Police Service, Fire Service and Defence Force) the minimum qualifying length of service for a pension is 10 years.

1 Non-contributory.

2 1 1/4 percent of salary.

3 5 1/2 percent of basic pay.

4 Where the officer has held the appointment for at least three years, a pension is based on the officer's final pensionable emoluments. In other instances computation is based on the officer's average pensionable emoluments over the last three years of service.
An officer may elect to have 25 percent of pension commuted in the form of a gratuity which would be payable along with a reduced pension (equal to one half of the final pensionable emoluments or final average pensionable emoluments). This is only possible where the officer has a maximum 33 1/2 years of service. Gratuity is calculated as 12 1/2 times one quarter of the reduced pension.

5 Police officers who enter before 1.1.73 and Second Division Fire Officers (18.3.74) may qualify for a maximum pension of 92 1/2 percent.
The principle regarding the acceptance of a reduced pension and a gratuity operates in the same manner as that for other public officers.
A lump sum of 3 1/2 times the annual pension is also earned - in addition to pension, rather than a commutation of any part of the income stream.

Table 4.8 - Central Government: Pension and Gratuity Payments, 1966 - 1993

Year	Pensions and Gratuities TT$M	Current Expenditure TT$M	Pensions and Gratuities as Per Cent of Current Expenditure %
1966	7.5	203.6	3.6
1967	9.3	216.6	4.2
1968	10.6	232.4	4.5
1969	12.0	254.8	4.7
1970	11.9	280.4	4.2
1971	13.7	348.0	3.9
1972	18.2	418.4	4.3
1973	19.8	399.2	4.9
1974	20.8	670.8	3.1
1975	31.1	847.6	3.6
1976	38.7	1,065.8	3.6
1977	42.2	1,277.8	3.3
1978	58.1	1,611.2	3.6
1979	67.2	2,504.6	2.6
1980	76.5	3,074.8	2.4
1981	100.5	3,493.8	2.8
1982	142.8	5,893.5	2.4
1983	186.1	6,242.9	2.9
1984	207.0	6,297.1	3.2
1985	240.9	6,077.9	3.9
1986	263.1	5,636.3	4.7
1987	289.1	5,629.0	5.1
1988	330.3	5,543.0	5.9
1989	404.4	5,202.9	7.7
1990	450.1	5,563.8	8.0
1991	391.9	6,102.6	6.4
1992	373.2	6,443.1	5.7
1993	392.6	6,450.1	6.0

Source: Review of Fiscal Measures, Ministry of Finance.
Annual Reports and Annual Economic Survey, Central Bank.

Other Issues

The previous sections contained a broad outline of the trends in pension arrangements in Trinidad and Tobago. There are several other issues which are related to insurance and pension funds which can also be explored. Some of these issues are: ageing and its impact on pensions, portability of pensions, pension reform, and the impact of Aids on pensions benefits. In this section however the focus is on ageing, legislative reform and the impact of pensions on savings.

Ageing and Its Impact on Pension

While there have been changes in the structure and composition of the population between the 1911 and 1990 censuses, the one constant feature has been its youthfulness. The median age at the 1990 census was 24.2 years compared with 21.7 years (1946), 18.4 years (1960), 18 years (1970) and 21.2 years (1980). Increased emigration in the 1950's as well as increased birth rates in the 1950's had an impact on these population trends.[12] Table 9 details population distribution by age and sex at four census periods - 1960-1990. Although the population is relatively young, the proportion of persons 60 years and over has increased from 6.03 per cent in 1960 to 9 per cent in 1990. This factor is more noticeable when one looks at the age dependency ratios.[13] These ratios fell from 87 persons per100 persons of working age in the1960 and 1970 censuses to 66 persons per 100 persons of working age in the 1990 census. The high ratios in the 1960 and 1970 census were a reflection of the very young population. In 1980, the ratio of 68 persons for Trinidad and Tobago compares with 48.1 (Canada), 56.3 (United Kingdom), 47.9 (West Germany), 48.4 (Japan) and 51.3 (USA). The aging population in most European countries will have a major impact on the provision of economic services in these economies. Population aging is further compounded for countries with near zero birth rates - stationary populations. For these countries, the financing of

---

[12] In the U.S., those persons born between 1946 and 1964 are usually termed the 'baby boom' generation. See Moen (1988) for example for a discussion of these issues. As this age cohort grows older it will make a major impact on pension behaviour and the care of the elderly.

[13] The age dependency ratio measures the extent to which the youthful population (under 15) and the old age population (over 65) depend on the support of the working age population..

health and social services into the future implies a heavy burden on those within the age group 15 - 59 who are of working age. While these are not problems which are critical to Trinidad and Tobago at this time, the experiences of the major industrialized nations may provide useful lessons for the future. A recent IMF study has focussed on these issues for some major OECD countries and has outlined suggestions for reform of these systems. (See Ageing Population and the Fiscal Consequences of Public Pension Schemes SM 96/11.)

Table 4.9 - Population Census: Age and Sex, Percentage Shares 1960, 1970, 1980 and 1990
/Per Cent/

Age Group	1960		1970		1980		1990	
	Male	Female	Male	Female	Male	Female	Male	Female
Under 15	42.9	41.9	42.8	41.4	34.6	33.9	33.8	33.1
15-59	51.7	51.5	51.0	51.5	57.2	57.1	58.0	57.6
60-64	1.9	2.0	2.3	2.2	2.6	2.4	2.4	2.5
65	3.5	4.6	3.9	4.9	6.9	6.6	5.7	6.8
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Social Indicators Report, Central Statistical Office

Another feature of the demographic structure is the increase in the life expectancy at birth (See Table 4.10). In 1980 life expectancy at birth was 66.88 years (males) and 71.62 years (females) compared with 52.98 years (males) and 56.03 years (females) in 1946. The improvement in life expectancy and the impact of the Trinidad and Tobago baby boom generation suggests that by the year 2010 the bulge in the population may well be at the cohort 50 years and over. This result may however be tempered by the increased outmigration in the late 1980's.

A third feature of the population and labour force data is the fall in the labour force participation rates for persons 65 years and over. Since 1973 there has been a steady decline in this ratio especially for males. The fall in the ratio for males from 42 per cent in 1972 to 26 per cent in 1984 has occurred in spite of the rise in female participation rates, and the relative constancy of overall participation rates, especially in the 1977-1983 period. The decline in the rates may be attributed to increased pension coverage, (introduction of Old

Age Pensions and National Insurance Benefits) self employment or changes in economic structure. The reasons for the fall in participation rates are however deserving of independent study but, it should be noted that the provision of NIS benefits in the post 1972 period may have acted a stimulus to the fall.

Table 4.10 - Life Expectancy at Birth for Selected Years

Year	Male	Female
1901	36.73	38.75
1911	38.97	40.95
1921	37.59	40.11
1931	44.51	46.95
1946	52.98	56.03
1951	56.31	58.45
1960	62.15	66.33
1970	65.73	68.77
1980	66.88	71.62

Source: Social Indicators Report, Central Statistical Office.

Pension Funds and Savings

Insurance companies and pension funds affect economic activity in two main ways - as a provider of indemnification and as an institutional investor. As institutional investors insurance companies have an impact upon overall savings in the economy. Given the growth in occupational pension schemes, what impact, if any, do any of these schemes have on an individual's savings behaviour? The evidence from the developed countries is conflicting at best. Cagan (1965) for example finds that non-pension saving is independent of pension savings. However Schoeplin (1970) found evidence of the substitutability between pensions and other retirement savings. Munnell (1976) and Feldstein (1978) reinforce this, arguing that Cagan's results are explained by an induced retirement effect. That is, if an individual is compelled to join a

retirement scheme, he may be induced to retire at an earlier age than he had otherwise intended. Because his labour-leisure choice is distorted, he is forced to save more during working years and this could account for the complementarity between pension saving and other saving. For the UK, Green (1981) finds that on the basis of cross section data and the life cycle hypothesis, pension and other savings are complements rather than substitutes (in agreement with Cagan and others).

In the case of Trinidad and Tobago as far as this author understands there has been no empirical study on the effect of pensions and savings. Preliminary evidence seems to suggest that pension coverage may not have increased the overall savings rates. Certainly the introduction of NIS had little effect directly on overall savings. Indirectly however, to the extent that individuals had access to NIS funds for mortgages, then residential capital formation increased. These conclusions need however to be bolstered by additional research.

In the late 1970s as inflation placed more individuals into higher tax brackets, some of them used personal annuities as a form of tax avoidance. The tax laws at that time, however, allowed only one pension deduction. Thus this type of plan was beneficial to those in the upper income bracket. In the late 1980's the lower marginal tax rates and falling incomes however have reduced the attractiveness of this type of tax shelter. Since 1990, following on the tax reform measures of 1988 and 1989, it is possible for individuals to make deductions for pensions plans and personal annuities. This can therefore serve as a stimulus to the growth of individual annuities. Pension savings have an advantage over most other forms of savings primarily because of the tax benefits enjoyed. However, this is balanced by the illiquid nature of this type of savings as well as the fact that individuals cannot borrow against their future pension benefits.[14] It is this latter factor which distinguishes 'pensions' and other savings instruments. Pensions can be classified as the most illiquid type of saving relative to bonds, equities and even credit union shares. In the United States, individual retirement accounts (IRAs) have received favourable

[14] In the 1991-1992 period there has been a move to allow the withdrawal of contributions from approved pension plans for the purpose of purchasing a first home. As at the time of writing the Income Tax (Amendment) Bill, 1992 was out for public comment, with detailed guidelines to be followed for these withdrawals.

tax treatment and attracted commensurately large sums of money. No such system exists in Trinidad and Tobago; however favourable tax treatment for this type of savings, may pave the way for increased national savings.[15]

Legislative Reform

Pension plans operate in Trinidad and Tobago under a legislative framework set up in the early 1980's. At the time that the Insurance Act 1980 was set up, this framework was generally suited to the local economic conditions and prevailing economic philosophy of the time. Several major changes have affected the economy over the past 16 years and insurance companies now do business in a completely different environment. For example there has been a movement towards complete financial liberalization, with financial sector reform and the establishment of a floating exchange rate regime. In addition, the establishment of open market operations and the government's ability to issue in the domestic economy, securities denominated in a currency other than TT dollars, has added an extra dimension to the financial system.

With the repeal of the Exchange Control Act, 1970 pension plans as institutional investors are now somewhat constrained by the provisions of the Insurance Act to maintain a local asset ratio of 80 per cent.[16] The constraint is particularly binding as 'local' is defined in a fairly tight manner as the framers of the legislation recognised at the time that there would have been a paucity of long term investments in the local economy. However given the changes in the financial environment, the definition of local may no longer be relevant as the institutional investors seek greater portfolio choice and diversification. In this regard there is some justification for amendments to be made to the 1980 Act to allow for a relaxation of the definition of 'local' or a change in the composition of the local assets ratio or a combination of both. Prudence suggests that any alteration in the ratio should be done in stages while investors should be legally constrained to certain types of securities.

---

[15] A number of new savings instruments came into being in the post 1992/1993 period, introduced by the Unit Trust Corporation, one commercial bank and other institutions. More detailed study of the characteristics of these instruments will be needed before firm conclusions can be made.

[16] The Insurance Act defines local assets as follows: an asset which originates in Trinidad and Tobago, is denominated in Trinidad and Tobago dollars, and is physically held in Trinidad and Tobago.

Conclusion

This paper has provided a brief overview of pension arrangements in Trinidad and Tobago. The discussion has ranged from a focus on the legislative framework to the investment decisions of pension funds. Several aspects of pension arrangements still remain to be explored - portability of plans, mean income of pension recipients of private plans and pension reform. Several of these issues however may be better developed within the framework of a micro or cross section study of pension plans.

References

Asimakopulos, A. and J.C. Weldon, "On the Theory of Government Pension Plans", Canadian Journal of Economics, Vol. I, No. 4, November 1968, pp. 699-717.

_____, "On Private Plans in the Theory of Pensions", Canadian Journal of Economics, Vol. III, No. 2, May 1970, pp. 223-237.

Cagan, Phillip, "The Effect of Pension Plans on Aggregate Saving: Evidence from a Sample Survey", NBER, NY, 1965.

Davis, E.P., "Financial Market Activity of Life Insurance Companies and Pension Funds", BIS Economic Papers, January 1988.

Feldstein, Martin, S., "Do Private Pensions Increase National Saving?" Journal of Public Economics, Vol.10 December 1978 pp.277-293.

Government of Trinidad and Tobago (GOTT), Final Report of the Cabinet Appointed Pensions Review Committee, October 7, 1982.

Green, F., "The Effect of Occupational Pension Schemes on Saving in the United Kingdom: A Test of the Life Cycle Hypothesis", Economic Journal, Vol. 91, March 1981, pp. 136-144.

Kotlikoff, Laurence and Daniel Smith, Pensions in the American Economy, NBER, Univeristy of Chicago Press, 1983.

Moen, R., "Past and Current Trends in Retirement: American Men from 1860 to 1980", Federal Reserve Bank of Atlanta, Economic Review, Vol LXXIII, No. 4, July-August 1988, pp. 16-27.

Munnell, Alicia, "Private Pensions and Saving: New Evidence", Journal of Political Economy, Vol. 84, Mo. 5, October 1976, pp. 1013-1032.

Odle, Maurice, Pension Funds in Labour Surplus Economies, ISER, 1974.

Schoeplein, R.N., "The Effect of Pension Plans on Other Retirement Saving", Journal of Finance, Vol. 25, June 1970.

Wise, David (ed), *Pensions,* Labour and Individual Choice, University of Chicago, University of Chigago Press, 1985.

CHAPTER 5

Social Protection and Poverty in the Commonwealth Caribbean

Ralph Henry

Introduction

This paper reviews the evolution of social protection in Commonwealth Caribbean countries against the structure of their economies that have generated high levels of poverty for much of their modern history. The quantitative evidence on poverty is limited to the latter years of the 20th century, but the historical record is replete with an account of the hardships that have been the lot of large sections of the population from time to time. There have been recent studies on poverty, utilising a broadly similar methodology in Trinidad and Tobago, St. Lucia, St. Vincent and the Grenadines, Belize and Jamaica. Some of the more pointed references will be directed at those countries. Fortuitously, the selection is broadly representative of Caribbean conditions at first blush. In the two larger countries, the World Bank has been the umbrella under which the poverty assessments have been conducted. In the case of the other countries, the Caribbean Development Bank financed studies which were conducted by Kairi Consultants Ltd. Over the period 1994-96, the results of which were publicised in a forum hosted by the Economic Commission for Latin America and the Caribbean (ECLAC) in October 1996.

An explicit assumption of this paper is that recent economic difficulties, triggered by a mix of internal economic policy initiatives and of the vagaries of trade, have created a sea change in fiscal policy in the region. This, in turn, has reduced, and will continue to reduce social protection in the Commonwealth Caribbean. There is need for Governments to recognise the futility of current policies and to move quickly to establish systems that are sustainable, and provide adequate protection in an environment in which the rate of change is likely to accelerate, thereby increasing vulnerability for many workers. As they seek to protect their citizens, there is need to ensure that the procedures put in place, would not undermine labour commitment and competitiveness of economies that have to be active participants in the international economy, given their small size.

Definition of Social Security

Social security remains an amorphous concept, subject to varying definitions and interpretations. The ILO has been the primary agency in the international system, charged with monitoring the evolution of social security systems across the world. The ILO (1984) defines social protection in terms of the

implementation of public measures against economic and social distress deriving from the stoppage or drastic reduction in earnings. A more complete context for the examination of poverty and the social security issue is provided by Dreze and Sen (1991). They view social security as the use of social means 'to prevent deprivation, and vulnerability to deprivation' (Dreze and Sen, 1991, p. 5). Poverty or deprivation relates not so much to income, but rather to a failure in capabilities and functionings. In this regard, then, the basic problem of social security is protection against 'widespread, persistent deprivation' and the 'fragility of individual security' (Dreze and Sen 1991, p. 10).

They argue further for maintaining a distinction between entitlement promotion and entitlement protection. The latter relates to the prevention of a decline in the capabilities and functionings or in living standards, and the other to the more ambitious objective of enhancing the level of protection and of capability expansion, which are not necessarily convergent with increases in income and in economic growth. Rather, the expansion of capabilities like:

> *...the ability to live long and to avoid preventable mortality has typically gone hand in hand with the development of public support in the domains of health, employment, education, and even food in some important cases* (Dreze and Sen, 1991, 9. 11).

While the expansion of capabilities is not always associated with growth in income, it is frequently a function of the relative importance of growth-mediated security strategies and support-led security strategies of the State. Governments differ in the emphasis that they accord to these strategies: in other words, a poorer country may have systems that provide better protection to the poor, than a country that is richer in terms of per capita income. Moreover, governments that have pursued strategies of redistribution with growth are more likely to provide protection for the poor, than governments that are wedded to the philosophy of 'grow first and redistribute later'. Clearly then, this larger perspective on social security takes us much beyond the confines normally set in the discussion of provident funds and national insurance systems.

In the final analysis, a social security system is premised on the provision of elements of a social safety net. Such issues as the width, and the composition of the base of a scheme, the cost of administering it, the robustness of

investments supporting it, where it is funded by contributions from prospective beneficiaries, and the adequacy of the benefits, all hang on the efficacy of the safety mechanism defined by the social security programme in its various elements. Odle (1974) and La Foucade (1995) have focused on the narrower definition of social security in their examination of the formal programmes that have been set up in the Commonwealth Caribbean by way of social insurance. For present purposes, we adopt the wider definition that includes social assistance and measures to address the needs of the poor and other vulnerable groups, irrespective of existing or previous employment status.

Three criteria may be set for a social safety net in a market economy. Firstly, it must provide transfer income or consumable resources adequate to cover a deficiency of income that threatens a household or an individual with starvation and destitution. Secondly, the social safety net should provide the household with capacities for sustained participation in income generation in the medium to longer run, provided the members are of age, are possessed of the strength for, and are deemed, within the cultural norms, to be adequate to the task of, active participation in the market-place.

In some households, deficiency of educational attainment or of training would require compensatory investments in the present, to starve off poverty in the future. On the other hand, an elderly couple would have little interest in participation, or should be spared of the need to participate in order to access income and should be protected any way. A third requirement for the safety net is that it should ensure that the systems to address the two other imperatives are themselves stable, and provide protection against fragility and vulnerability. But as has been shown by Espina (1996) and Esping-Andersen (1990), a range of historical and institutional factors have influenced the models of social protection that have evolved in the more developed countries.

Esping-Andersen (1990) suggests that there are, at least three factors that have contributed to the nature of the welfare state evident in the industrialised North Atlantic countries:

1. the nature of class mobilization;

2. class-political coalition structures; and

3. the historical legacy of regime institutionalisation.

While these factors are undoubtedly important in the Caribbean context, resources do not permit of more than a cursory examination of their effects. This paper will examine the evolution of social protection in the Commonwealth Caribbean paying closer attention to the degree to which it has been effective in protecting citizens from poverty.

Historical Background

The Colonial Phase:

Formal social security in the Commonwealth Caribbean had its beginnings in the last century with the establishment by the first generation of emancipated slaves of Friendly Societies as a form of protection against certain risks and/ or to deal with life crises that could befall the household. Immediately following emancipation, informal social protection was the only recourse available to the household, as the newly freed Africans developed social networks outside the plantation system. The Friendly Society offered a formalised structure within which to routinise protection. As an institution, it had had its origins in the first half of the eighteenth century in industrialising Britain, and had as one of its objectives, the muting of the effects of the Poor Laws. It was adapted to the conditions in the Caribbean, initially by the missionaries to the region, who played a key role in social development in the post-emancipation era, especially in the field of education.

From its earliest stage, formal social security in the Commonwealth Caribbean was influenced by developments outside the region. As colonies of Britain, the dependencies seldom developed programmes to achieve objectives beyond what was considered appropriate in the mother country. Indeed, they usually lagged behind. Outside of the Friendly Societies that the emerging proletariat subscribed to, there was, in some communities, relief for the poor organised by the vestries of the denominational groups that became active in the post-emancipation period. Their approach reflected the paternalism of 19th century Britain, which was the main source of inspiration. The emerging middle class in Britain, by the mid 19th century, established a tradition of charity, and this had an impact on the colonies. Their concern was some advance on the earlier period given the punitive treatment meted out to the poor whose condition was deemed a consequence of their moral turpitude.

The conduit to the colonies was through the ministrations of the denominations which came to the Caribbean proselytising among the freed Africans. The unfortunate who could not subscribe to, or fell outside the provisions of the Friendly Societies, had to depend on informal charity. In some countries, the Friendly Societies either developed into building societies, or provided a model for their development. Jamaica is an example of this trend and is the country in which the building society movement took on the largest presence. Building Societies have mobilised substantial savings among the poor for housing, and even up to the present has continued to play a major development role in that country. Another institution that closely resembled the Friendly Society, and in many cases functioned like it, was the Secret Order. According to Wells and Wells (1953), the Orders were branches of similar institutions in Britain and the United States, and attracted a clientele that was usually of higher income than the poor who, instead, gravitated to the Friendly Society. The criteria for entry were more demanding, but the purposes served were largely similar: assistance in distress, illness, and provision for burial.

Meanwhile, intent at the official level in the Caribbean was anything but benign. Colonial officialdom wasted no time on the emancipation of the slaves, importing wholly the same legislative provisions for dealing with those who fared badly in the throes of the industrial revolution in Britain. Some of the punitive legislation that applied to 'incorrigible rogues, and vagabonds', and others not favoured by circumstance in the British setting, was immediately adopted as the first form of social control over the recently freed Africans. Indeed, such legislation existed in the law books in some Caribbean countries, even into the last half of the 20th century, and dates back to August and September 1838, having been enacted within the first few months of formal emancipation on August 1, 1838. In the case of Trinidad, the vagrancy law was promulgated on September 14, 1838.

The next major advance in the structure of formal social security came almost a century later and originated with the adoption of recommendations of the Moyne Commission. The Commission recognised that the level of poverty experienced in some parts of the Commonwealth Caribbean dictated a greater intervention on the part of the State. The riots that had erupted in most of the region were sparked off by industrial relations conflict, but the destitution among significant sections of the population in the respective countries provided the powderkeg for the social conflagration of the late 1930s, with eruptions in most of the countries. The Moyne Commission was appointed to investigate

the factors that led to such a massive ground swell of anti-colonial sentiment across the Region.

Following the publication of the Moyne Commission Report, many of the countries introduced or upgraded the provisions for Old Age Pensions, and provided for official systems of 'Poor Relief'. More particularly, measures were instituted to permit greater devolution of authority from the Colonial Office to the island legislatures, which were thenceforth to be elected under universal adult suffrage. The Commission detailed a number of measures to be adopted in the field of social welfare. Full-fledged agencies or departments to give effect to the recommendations were established in the governmental structure. Also instituted were labour departments with the responsibility to mediate over conflicts between employers and the unions representing their workers. Along with the improvement of the institutions for industrial relations and for worker protection, provisions for workmen's compensation in respect of work related disabilities were also introduced.

The Post-Colonial Phase:

The arrival of independence in the 1960s marked another and more advanced phase. Accession as full members to the international institutions required that these countries introduce legislative provisions to comply with the tenets of the organisations that they joined. As dependencies of Britain during the colonial period, the countries had had a relationship with the International Labour Organisation when it was formed. When they became full members, the organisation was able to play a greater role in their development, and in assisting them to observe internationally accepted standards in the field of labour and industrial relations. It was to play a key role in the establishment of National Insurance systems in the region. Technical assistance was provided to the new members, with bilateral or multilateral financial support from other sources. Jamaica was the first to introduce a national insurance system, and was followed by the other countries as they gained their independence in the 1960s and 1970s.

Poor Relief Ethos:

With the arrival of self-government and then of independence, three distinctive traditions have influenced the evolution of the social security system in the Region. Firstly, there has been the poor relief ethos, a product of the Poor

Law philosophy of 18th and 19th century Britain which finally found official recognition in the Caribbean towards the end of the 1930s and early 1940s. A prominent feature in the measures that constituted the official response was that the poor should receive none but the bear necessities of life, a quality caricatured by Charles Dickens in his description of the ethical principles of the work house in the Britain in the last century.

Elements of that tradition have persisted. There has been very little inclination on the part of the Commonwealth Caribbean Governments to institute any automatic adjustment mechanism to protect persons, who receive social or public assistance, from the ravages of economic change and from inflation. The boom years in Trinidad and Tobago were the one occasion when there was a significant departure from that trend, as the Government instituted a range of provisions for persons receiving public assistance and old age pensions. There were food stamp entitlements, and free passes for the aged on the public transport system.

Civil Society Security and Development

Parallel with the involvement of the State, and in many cases, predating it, have been the NGOs, some of which were involved in provision of succour to the poor. The period of the Great Depression was particularly significant in the emergence of these institutions in the Commonwealth Caribbean. Other insttitutions emerged as more specialised agencies focusing on physical and other disabilities and were often established as part of an international network, and thus had an impetus from an external source. They were usually structured in such a way as to mirror their external benefactor and to benefit from overseas financial flows which were the only, or the main source of support. As they became part of the domestic institutional structure, in time, they would benefit from subventions from the Government of the country. In a few cases, the Government became the main support.

Another variant of civil society response in the evolution of the social security/ safety net have been the agencies with a clear development focus. These have been much fewer in number. An outstanding case has been Jamaica Welfare, established just before the Second World War. While it set itself the task of mobilising assistance for the poor, it was clear to its founders that the most secure basis for the elimination of poverty and for reducing vulnerability

was the development of the capacities of the poor themselves. Jamaica Welfare was used as a model for other agencies being developed in the Commonwealth Caribbean at the same time (Girvan 1993).

The arrival of self-government, and then full political independence led to a view that the State was the main, or even the only, axis of development. Thus, the thrust for the development of the poor was channeled, to the extent that it was identified specifically, through such agencies as Ministries of Planning, and Community Development Departments. Moreover, as the new structures were agencies of the State, governing political parties had a ready-made platform for influence, and for mobilising votes at election time. There was no real wish to encourage a genuine independence in development agencies established by the people themselves.

Indeed, in some countries the emergence of independent NGOs, often with outside funding, was often the source of political tension. Some governments would actively attempt to thwart the work of such organisations (Henry and Mondesire, 1997). This was guaranteed to lead to these agencies developing hostile postures to the government, and/or becoming the base for oppositional politics. Yet, there exist some that have been outstanding successes as development institutions. Among these are BEST in Belize, Projects Promotion in St. Vincent and the Grenadines, and the National Research Development Foundation (NRDF) in St. Lucia. All have a rich record in mobilising the poor with their own resources, and for their own development, in addition to their being able to parley resources from external sources.

Another important agency for development has been the credit unions and the cooperative sector generally, which emerged in the 1940s. These institutions may not always have been seen, nor would have regarded themselves, as involved in social security, and in safety net issues. However, from their sheer presence in poorer communities, they contributed to the development of financial and other capabilities among the lower income groups in Caribbean society. The credit unions could be seen as the filial descendant of the Friendly Society of the last century. The basis of mobilisation was often the same - the community - but in the context of the evolving Caribbean, now includes the work place.

There have been outstanding examples in this genre as well. The Fishermen's Cooperatives in Belize have transformed the fishing industry of that country,

and improved the livelihood for many poorer villages especially in the north of that country. The credit unions of Dominica provide the primary banking institutions. While not as central in the monetary sector as in Dominica, credit unions have been very successful among lower income groups in Belize, Trinidad and Tobago, and St. Vincent and the Grenadines. The success rate has not been as good in the other areas, especially in agriculture and fishing on which many of the poor are still reliant in the Commonwealth Caribbean, in the latter years of the 20th century. The Northern Fishermen's Cooperative of Belize has been the major exception, in that regard.

National Insurance/Provident Funds

The Third tradition in the evolution of the safety net derives from the ILO inspired social security programmes that the countries instituted, usually immediately following their independence. These have all been anchored on the employment situation of the prospective beneficiaries in *pay as you go* schemes. By the end of the 1970s, most countries had either national provident fund or social insurance provisions in place. The range of protection provided has remained limited: old age, disability, and survivorship, sickness/maternity and employment injuries tend to be the main areas for protection. While most countries require the registration of the self-employed, the nature of benefits varies. Only one country, Barbados, makes provision for unemployment. Table 5.1 which is adapted from La Foucade (1995) shows the level of coverage provided by the various countries.

In her review of broad performance indicators on the social security schemes in the Commonwealth Caribbean, La Foucade concluded that total expenditure had begun to outstrip contribution income by the end of the 1980s, and anticipated 'a cloudy financial future for schemes' (La Foucade, 1995, p.68). In spite of the incontrovertible evidence, the countries had failed to implement actuarial recommendations, a problem she attributed to:

1. the unsuitability of the recommendations;

2. political inertia;

3. disagreement of administrators with the recommendations; and

4. technical and human resource constraints in implementation of the recommendations.

La Foucade (1995) focused on the internal efficiency of the programmes, and formed the view that they had become unsustainable in the realities of the 1980s. It should be noted that at the best of times, the programmes provided only a limited degree of protection. Meanwhile, in respect of the compensatory or complementary mechanisms, there were deficiencies in their capacity to reach the poor, whether by way of poverty alleviation or by poverty reduction measures (Henry and Mondesire, 1997).

Table 5.1 - Introduction of National Insurance Benefits in the Commonwealth Caribbean

Country	OADS	Sickness/ Maternity	Employment Injury	Unemploy ment	Self-Employed	Voluntary Coverage	Medical
Antigua-Barbuda	1973	1973	–	–	–	–	1978
Bahamas	(1956) 1974	(1972) 1974	(1943) 1978	–	1984		1984
Barbados	(1973) X	(1966) X	(1916) X	(1982) 1982	1974	1984	–
Belize	(1979) 1981	(1979) X	(1981) X	–		X	–
Dominica	(1970) 1976	(1975) 1976	(1937) X	–	1989	X	–
Grenada	(1969) 1983	(1983) 1983	–	–	(1983) 1988	(1983) 1988	–
Guyana	(1944) 1969	(1969) 1979	(1916) 1970	–	(1969) 1971	X	1969
Jamaica	(1958) 1966	(1979)* 1979	(1937) 1970	–	–	–	–
St. Lucia	(1970) 1979	(1978) 1979	(1964) 1979	–	–	–	–
St. Vincent & the Grenadines	(1970) 1987	(1986) 1987	(1939) X	–	–	–	–
Trinidad & Tobago	(1939) 1972	(1971) 1973	(1926)	–	–	X	–

OADS: Old Age, disability, survivors'.
(): First Law
*: Maternity for domestic servants only
X: Coverage provided but year of introduction unknown
Source: La Foucade (1995)

The latest phase in the evolution of social security in the Commonwealth Caribbean came in the 1980s. Larger countries succumbed to balance of payments and fiscal crises, and had no other recourse but to seek the assistance of the International Financial Institutions (IFIs). This was the period when the conservative philosophies of Thatcher in the United Kingdom and Reagan in the United States created a new mood in the North Atlantic. The Governments in the industrial countries sought to correct for the problems in their macoeconomy which were no longer responsive to the time-worn measures of macroeconomic stabilisation. High unemployment and high inflation coexisted, confounding the theory built around the Phillips Curve on the trade-off between inflation and unemployment. Thatcher and Reagan were prepared, in their respective countries, to reverse policies of previous administrations, and to adopt market-driven strategies and to reduce the role of the State. The influence of their thinking spread quickly among the industrial countries, and not least to the IFIs, in which they determined the resource base through their financial contributions.

For whatever the reason, social insurance, conceived and developed for a different environment, and with a limited remit of the 1960s and 1970s, is now unlikely to provide protection against poverty for a large section of the vulnerable community because of the more difficult economic situation faced by these countries in the years ahead. Indeed, social insurance programmes have started to mature at the time when Caribbean economy has been experiencing relatively slow growth at best, and declining and negative rates in some cases. If social security is partially a function of the generation of current income on the one hand, and of the prevailing social ethos on transfers and on the developmental support for the less fortunate, on the other hand, the Commonwealth Caribbean, with weakly developed social security systems, seems destined to an absolute parsimony in the treatment of the poor.

Poverty and Economic Strategy

Since the early 1950s, the Commonwealth Caribbean has been engaged in the formulation of economic strategy aimed at the transformation of their economies. The region had revolted against the conditions in which it found itself, after a century of individual freedom following Emancipation in 1838. Poverty was endemic in the structure of plantation economy that the Caribbean then was, and in some respects, still is, according to the characterisation

developed by Best (1968). While much had changed over the period, Caribbean people under the colonial yoke in the 1930s were convinced of the need to take their freedom to a new level if they were to transform their material condition.

Lewis (1950) had dared to juxtapose the word 'industrialisation" next to the British West Indies. Lewis (1939) had earlier identified a persistent unemployment problem in the Commonwealth Caribbean which was exacerbated by the Great Depression. He envisaged a solution in his celebrated article on the industrialisation of the British West Indies in 1950. He recommended the adoption of labour intensive light manufacturing with foreign capital and capitalist providing the inputs of technology and markets in the first instance.

Since the region was deemed to be too small to provide adequate market size for much of a diversified production, external markets had to be found. Foreign capitalists were expected to provide this in a virtuous cycle of their delivering capital, technology, markets and the "tricks of the trade" altogether. The large reservoir of labour that could not be absorbed in agriculture, could be put to productive effort in activities in which the Caribbean was thought to have a comparative advantage. To a more limited degree, the Tourism Sector was expected to play a similar role. In both respects, the necessary requirement was the provision of the infrastructure by the Government (Federal), and the creation of the appropriate institutional infrastructure of incentive legislation and departments to administer it.

For at least the next thirty years, the countries became engaged, albeit severally for the most part, in an attempt at the restructuring of their economies according to some notion of an internal capacity to identify the direction in which there was a possibility for growth and transformation. Over the period, these countries embarked firstly on a limited version of export-led growth, which was quickly corrupted into import substituting industrialisation, at the domestic or national level, and then after the start of regional economic integration, at the regional level.

The prescription outlined by Lewis (1950) was never really followed. Thus, he was to note that while Hong Kong had proved, by 1958, the viability of the strategy that he had proposed for the Caribbean, the region continued to flounder (Lewis, 1958). Some amount of manufacturing was established, but

did not deliver employment on the scale initially envisaged and this was to lead to the caricaturing of the strategy of "industrialisation by invitation" among radical thinkers at the time. By the mid 1970s, the IFIs had arrived and became active in macroeconomic policy formulation in some of the countries of the Region, starting with Jamaica, which succumbed to acute fiscal and balance of payment problems, partly exacerbated by the oil crisis. Others were to follow - Guyana, Trinidad and Tobago, and Barbados, i.e. all of the so-called MDCs or more developed countries of CARICOM, but also some of the LDCs, occasionally. As part of the conditionality arrangements, the Governments were required to undertake a major shift in strategies of development that had been pursued.

Yet by the late 1980s, Caribbean economists could all but agreed that the region was a sure case of *'development in suspense'* (Beckford and Girvan, 1989, and Worrell, 1989). The mix of policies that have been pursued, whether on the advice of the IFIs, or on the basis of home-grown models, had not demonstrated success *a la* East Asia. The closing stage of the 1990s finds the Commonwealth Caribbean at a level transformation, and with a rate of growth that fully replicate the verdict on the 1980s: slow or faltering growth, lack of transformation, vulnerability to terms of trade in respect of a limited range of exports, high unemployment and increasing poverty as the primary characteristics of current reality, with few exceptions.

Access to foreign exchange earnings is still dependent on the performance of the primary sector - oil, bauxite, sugar, and bananas - or on export-oriented light manufacturing or assembly operations and tourism. The prices of commodity exports have continued to suffer a real decline. Light manufacturing in recent years has been particularly sensitive to any slight movement in comparative wages internationally, or to the march of the technological revolution that has made low wage labour intensive production increasingly an irrelevance. In more recent times, there has been a preoccupation with the establishment of Export Processing Zones as the mechanism for attracting labour intensive manufacturing and assembly operations. This has consigned these countries to the production in the commoditised manufactures (Kaplinsky, 1993).

Meanwhile, the North American Free Trade Area (NAFTA) has allowed Mexico to displace them in some of the manufacturing activities in which they were previously engaged, or alternatively, lower wage costs in the export processing

operations in the Dominican Republic and in other newer locations like El Salvador, Honduras and Guatemala, have put paid to the idea of their being competitive in labour intensive production for export markets. Countries at greater distance from the main markets have been absorbing their transport cost disadvantage through lower wages, with the result that competition around the wage rate has become increasingly acute among those that seek to utilise their large supply of cheap labour: Bangladesh, Vietnam, and Nepal are immediate examples of lower wages in competitive export locations.[1]

Tourism and information processing have been the sectors that are being promoted to the extent that there remains any semblance of industrial policy. Even their tourism product has less appeal in the absence of characteristics that can differentiate it from sun, sea, and sand that are on offer in countless other locations (Poon, 1990). Information-processing has been largely of lower level data-entry activity, rather of the skill and knowledge-based activities which might have attracted higher returns if the work-force were better equipped in terms of training and education.

In other words, having accepted the conditionalities of the IFIs, the underlying strategy of market friendly approaches restricts the Commonwealth Caribbean to seeking to exploit static comparative advantage rather than their seeking to create competitive advantage by developing capacities to exploit particular niches. The strategy relegates them to standard commoditised manufacturing and to sun, sea, and sand or mass market tourism.

As Lall (1995) has shown in respect of industrial development in Africa, the structural adjustment model *a la* World Bank carries certain assumptions of questionable relevance to the conditions faced by late developers. The new economic theology requires the countries to open up their economies to international trade as quickly as possible, and to allow border prices to determine the viability of their production system. It is assumed that government intervention beyond the provision of infrastructure and education is likely to be distorting and productive of inefficiency. There is no allowance made for economies of scale, imperfections of information flows in the market for

[1] The competition around sweated labour has finally brought a reaction from the Government of the United States of America, but it is too early to anticipate the degree to which this will reduce the super-exploitation of labour in some poorer countries.

technology, the problems of learning by doing in development of technological capabilities, at the firm and country levels, and for the role of institutions in the realisation of externalities to key agents (Lall, 1995).

Jamaica has had the longest experience among the Commonwealth Caribbean with structural adjustment and stabilisation. In one of the more in-depth review of the performance of the country since the 1970s, Robinson (1994) concludes that:

> *.....adjustment process has so far yielded a structure which leaves the economy as vulnerable to external shocks and world prices as it has always been. The dependence on traditional exports and tourism has hardly been dented by a competitive manufacturing sector while the pursuit of policies which lean towards free trade has undermined domestic food production and the stability of rural communities* (Robinson, 1994, p. 110).

The costs have been enormous and Robinson (1994) asserts that by any criteria, the quality of life for the vast majority of Jamaicans has declined absolutely. The Jamaican experience is not flattering to the programmes of the IFIs.

Mechanics of Adjustment

The mechanics of adjustment *a la* World Bank for small open and undiversified economies are likely to be harrowing given the limited degrees of freedom consequent on a narrow export base. The decline in one sector alone can have an immediate depressing effect on the economy and this has surely been the experience of Trinidad and Tobago as a result of the collapse of oil prices. A comparable tendency is evident in respect of the Windward Islands which have been dependent on banana exports for a substantial share of their foreign exchange earnings. In the case of St. Lucia, the difficulty has been compounded by the fall in competitiveness of the export-oriented Manufacturing sector, because of more attractive wage rates in other parts of the Caribbean.

Seers (1964) emphasised the distortions inherent in a booming sector. The effects of decline are even more devastating. The shift out of a major export sector in Caribbean-type economies has always been attended by upheaval.

The story of sugar provides many lessons on the problem of transformation and adjustment. Lewis (1939) illustrated the effect of adjustment of the sugar economy:

> *"For two centuries, the islands were a scene of great prosperity, but in the nineteenth century that prosperity vanished; the islands faded into obscurity and ceased to be a turbulent concern of European politics"* (Lewis, 1939, p. 11).

It could be argued that Emancipation and the decades that followed it, were all part of an adjustment of the sugar economy that is not fully completed, in some of the countries (witness the difficulties that the post-independence Governments of Trinidad and Tobago and St. Kitts have experienced in the conversion of sugar lands to alternative uses). It might well be that small-scale economies structured like those in the Commonwealth Caribbean have severe difficulty in shifting their export base. It is inherently problematic moving from one export specialty to another as, for example, it has taken almost a century with sugar, and the cost to generations of workers has been excessive.

Protective policies and other forms of Government intervention seem unavoidable, given the social costs that need to be internalised in such situations of market failure. Given the large role now performed by the IFIs in the policy-making of Caribbean Governments, there are certain initiatives that are effectively ruled out. Infant industry arguments in favour of protection are no longer thought to be admissible even in the short run. Adjustment, therefore, in these small economies invariably means the collapse of whole sectors, and in the absence of the institutional framework to restore the workers losing their jobs to new activities, poverty and unemployment follow naturally in the wake.

Most of the countries have had to adopt structural adjustment programmes with or without the IFIs. In the cases of self-imposed"medicine", there is usually the notion that the adoption of the standard model is likely to win approval and to facilitate a soft landing if the IFIs needed to be invited to undertake a full programme of stabilisation and adjustment in the respective countries. Thus, where they have taken the medicine themselves, the result is that there is very little difference between home grown programmes and those dictated from outside. Barbados is the one country which might have developed an

independent adjustment model and has sought to be very selective in the niches to be targeted in the resuscitation of the economy.

In the final analysis, since boom and bust cannot be avoided, once the structure of Caribbean economy remains essentially anchored in one or two exports, it is the quality of the institutional base created, and therefore the timeliness and efficacy of the hands-on management of the policy-makers that determine the success of adjustment, which will have to be dictated by other than market forces alone. Total dependence on the market guarantees greater vulnerability and collapse into poverty of large sections of the workforce in Caribbean-type economies. In other words, the mechanics of a successful adjustment are fraught with market failure.

The recent experience of bananas is illustrative of the difficulties of relying solely on market indicators in the economic reorganisation of such an important export industry in a small country. In the case of the Windward Islands, in spite of the fact that the writing has been on the wall for some considerable period of time, the countries are not well prepared to deal with the crisis they now face. In the liberalising environment of the 1990s, new activities to replace banana production and to earn foreign exchange have to be export-ready almost from the very beginning.

Thus, a large number of banana farmers in the Windward Islands need to diversify into alternative crops, but there are few farming activities that are as amenable to the small scale production systems to which they have been accustomed and which can generate income on a level and with a regularity that was possible with a perennial like bananas. In spite of the efforts at diversification in some cases, there are few crops that can fully compensate for the role performed by the Banana Industry in the second half of the 20th century.

The retraining necessary, the development of new or the reorganisation of cultivation practices, the establishment of new credit arrangements appropriate to a different agronomy, are all issues that have scarcely been broached, let alone provided with the resources adequate for a rapid transition to a new dispensation. This would have required a conscious industrial policy formulation, to downsize the banana industry and encourage marginal farmers into alternative activities, even in the face of buoyant demand conditions in the

early 1990s. The result of failure or absence of industrial policy is that there has been a rapid spread of poverty to rural areas of these countries.

Neither the domestic market, now opened up more directly to imports, or the new export agricultural activities provide any protection to the marginal banana farmers. Usually, they are too small to enjoy economies of scale in a new activity, and too limited in training to be small and efficient in what are deemed to be *exotica* by domestic standards, but which are regular commodities in international trade in agriculture e.g. cut flowers, pineapples, and mangoes, to quote three examples of the recommended replacement export crops.

Concerted public policy would have been required, to create a major shift out of bananas to other crops in the face of temporarily buoyant demand for bananas in the early 1990s (a result partly of currency alignment between the EC dollar pegged to the US dollar which depreciated against the British pound in which banana exports were realised). No less an intervention with effective industrial policy was required to manage the boom in the oil exports in Trinidad and Tobago in the 1970s. Indeed, the so-called OPEC disease emphasises that it is not the fact of intervention that matters but rather the quality of intervention, in addressing the underlying fundamentals of economies that are undiversified. Failure to create the institutional base for adjustment exposes the labour force to structural poverty when an export sector collapses.

Poverty Profile

Table 5.2 presents information on poverty for a number of countries. The Region has had high levels of unemployment since the 1940s, a factor which Lewis (1950) had sought to address. There is also high underemployment, partly reflected in the emergence of a large informal sector. The estimates of poverty are all above 20 percent, and in some cases, over 30 percent. While there may not exist the grinding poverty recorded in some parts of the developing world - they score in the middle range or higher on the Human Development Index - large segments of Caribbean communities experience severe hardship.

In all cases, weakness in the export sector has been an important factor precipitating the crisis faced by the country, although injudicious macroeconomic policies have also been a factor. In the cases of St. Lucia

and St. Vincent and the Grenadines, the crisis in the Banana Industry has had an immediate impact on the farming sector of those countries. Even the limited protection currently available is likely to be lost under the rules of the World Trade Organisation (WTO), which other banana producing countries in Central America are seeking to invoke against the EC.

In the case of St. Lucia, in particular, after a very strong performance in export processing operations, competitive wages elsewhere in the circum-Caribbean (e.g. the Dominican Republic) and the advent of NAFTA have impacted negatively with the closure and migration of some of the operations to other locations. Thus, two of its important exchange earning sectors have suffered reverses at the same time. The spread of poverty seems to be the likely sequel, exacerbated by high and continuing unemployment and underemployment.

Table 5.2 - Welfare Measures in Selected Commonwealth Caribbean Countries

Country	Poverty Level (%)	Human Development Index (1993)	Unemployment Level (%)
Belize	35	0.754	13.8 (April 1996)
Guyana	43	0.633	N.A.
Jamaica	34	0.702	16.0 (Average for 1996)
St. Lucia	25	0.733	15.2 (mid year 1995)
St. Vincent & the Grenadines	38	0.738	N.A.
Trinidad and Tobago	21	0.872	15.9 (1996 IV)

Sources: World Bank; Kairi Consultants Limited (1996); UNDP (1996)

Social Security for a Small Scale Economy

An efficient system of social security in the Commonwealth Caribbean in the short to medium term has to take account of the structural realities of the

economies of the region. To protect the population from vulnerability, there are three factors that must be addressed. The first relates to the structure of the economy within an international economy committed to more open systems of trade, and in which the rules could hardly be influenced by countries that are such small players in the international market place. The second has to do with the demographic transition of the Region and as the period of high fertility is followed by maturing of the baby-boomers of the post World War II period, and given growing life expectancy, the older age cohorts expand as a proportion of the population. The third factor relates to the critical importance of using the resources of the contributors in a way most conducive to the development of the economy such that there would be the maximum level of sustained economic activity deriving from the mobilisation of the resources even from among the poor themselves.

Commonwealth Caribbean economies in a liberalised world economic system have to be constantly in an adjustment mode. Their largest sectors are likely to be small players in the international economic system. As small countries, they are unlikely to have the range of industries that afford them an easy passage from one "sunrise" activity to another as the structure of demand and competitive supply changes the terrain that they face. The less diversified they are, the more acute is the problem. In such circumstances, social security has to be far more encompassing than the traditional focus on social insurance, and even on social assistance. It has to fulfill developmental objectives as well, directly and indirectly, a feature that was recognised by Odle (1974), and figures prominently in his conclusions and recommendations on probable directions for social security in the Commonwealth Caribbean.

In the present conjuncture of Caribbean Economy, and for the foreseeable future, employment insecurity and fragility are the likely condition of a large percentage of the work force. Much depends on their capabilities in their being able to be quickly reabsorbed into productive employment, including effective own-account employment, when unemployment threatens. The capacity to adapt which can come from training and a sound educational preparation is critical to survival. However, the institutionalisation of training and retraining of workers has yet to be formalised in programmes in the Commonwealth Caribbean, let alone to be linked to the formal social security system. There are facilities to train entry-level participants, but little by way of the formal reorientation of workers who need to be reintegrated into the production system.

In the case of Barbados, the one country with unemployment insurance, there are provisions to have workers access training and retraining in the event of unemployment. But it remains the exception on both counts - in respect of social protection in the face of unemployment, and programmes of training for reintegration into full employment. There is need for the development of a training system that equips the workforce for a high degree of flexibility, a feature that is still very embryonic in the training system of the region.

There is also need for a supporting social infrastructure that allows workers to utilise periods of unemployment for acquiring new skills and training for their reentry into paid productive employment. This infrastructure has to include social protection that keeps the human capital intact, by the provision of transfers to keep workers out of destitution and in good health, while they are being prepared for alternative employment. In other words, there is need for an articulation of social protection, with labour force upgrading and provision of credit for micro-enterprises and informal sector participation. On the other hand, those who are unable to contribute to the output of goods and services in the formal economy still need to be supported as a last resort, by some form of social assistance, adequate to cover their basic needs, but without such programmes contributing to problems of moral hazard.

The process of ageing is now clearly evident in the populations of the Commonwealth Caribbean. High (though declining) rates of fertility are still a characteristic of some of the countries of the region, notably in Belize, St. Lucia, Guyana and St. Vincent and the Grenadines. On the other hand, the implications for population growth have been considerably tempered by the continuing high rates of emigration that have been a feature of the population dynamics of the Region since the Second World War. The general decline in the rate of population growth heralds a slowing in the potential labour force, which, as has happened elsewhere, has implications for any social security programme built on the pay as you go model. The prospective beneficiaries are due to become larger relative to the numbers in the workforce, thereby increasing the costs of social security relative to the inflows from contribution income. Policy measures have to accommodate to that reality to ensure sustainability in the coverage of social security.

Finally, there is need to recognise that insurance schemes can mobilise large sums that could be put to use for development purposes. Odle (1974) noted that the failure to raise contribution levels frittered away the opportunity of

adjusting benefits in line with inflation and, more importantly, of creating a large fund of savings that could be used for development purposes. He recommended more progressivity in the contribution structure and flatter rates on the benefit size, having regard to the fact that in 'labour surplus economies, those in regular employment are a relatively privileged minority...' (Odle, 1974 p. 126). By 1995, La Focade could conclude that the schemes had a number of deficiencies including some level of under-funding. There is clearly a case of Government failure here.

The comparative experience of Singapore establishes the validity of the thesis of Odle (1974). The Central Provident Fund of Singapore has been the primary source of domestic savings in the economic transformation of Singapore from a small third world country into a rich modern society, well equipped to adjust to the vagaries of international trade. This large pool was an important catalyst to expansion through the multiplier effect on employment growth with the stimulus that was given through the housing for the work force. Thus, the high savings contributed to high employment generation, principally in construction activity - housing and infrastructural - and to the general development of the country. The coverage of the Fund is wide (over 80%), and the level of contribution is one of the highest in the world (40% of employees' wage, shared equally between the employer and the worker). According to the Economist (1996), some three-quarters of the worker's individual account is available to pay for property, life insurance, certain education fees, and other approved asset enhancement schemes like unit trusts. There is need for the Commonwealth Caribbean to emulate that model. Many of its current problems would have been effectively resolved if it had followed such an approach sooner.

Prospects

Statutory pension plans have been a focus of attention in the structural adjustment programmes that have been instituted in a number of countries. The fact that such pension arrangements constitute a type of payroll tax invites immediate attention. Indeed, they are deemed to work negatively against employment creation and, therefore, to be generally distorting to the operations of the labour market. A number of pension plans have run up against the problem of under-funding. Most schemes have been pay-as-you-go types: each age cohort pays into the pool a certain percent of current wages which is used to fund the pension of the present cohort of retirees. These resources

are invested and the earnings from the investment, in addition to the subscription from the present cohort of workers, are expected to meet the payments due to the retired.

In recent years, a number of such schemes have run into difficulty. Existing levels and the interest earned on the investments have been inadequate to cover claims. Pension payment obligations have threatened to overtake current worker contribution. La Foucade (1995) found that total expenditure was increasing more quickly than contribution income in most of the Commonwealth Caribbean countries. In the case of Mexico, it was projected that the pension system would become unsustainable by 2002 (Martinez *et al.*, 1996). In a number of countries, the ageing of the population due to the increase in life expectancy, and to the fall in the birth rate, has been the underlying factor responsible for the emergence of actuarial deficits. Even in respect of the richer developed countries, Espina (1996) concludes that pension schemes and social protection generally, cannot avoid downgrading because of:

1. the arrival at retirement age of the largest cohort in history;

2. the emergence of the NICs with competitive advantage based on minimal labour costs;

3. the deregulation of labour markets in the advanced countries, and the reduction of social contributions in order to lower real wages and to make the work force more competitive by international standards.

The standard recommendation that has emerged is the replacement of pay-as-you-go arrangements by fully funded schemes through which each contributor would receive pension benefits more directly related to his/her own unique contribution history.

Under the new system, each worker has an individual account, and the benefits at retirement would be a function of the number of years worked, and the real rate of return on the investments made by the savings under this account. Finally, instead of the State taking responsibility for the management of the portfolio, private sector institutions, mainly insurance companies, are contracted to manage the investment. Pension reforms with such characteristics have been instituted in a few Latin American countries in recent years: Chile, 1981, Argentina, 1994, Colombia, 1994, and Mexico, 1995/96.

The post-apartheid Government of South Africa is contemplating the privatisation of State Pension funds.

In the light of the emergence of actuarial deficits in countries of the Commonwealth Caribbean, the privatisation model is likely to be recommended for national pension programmes. But as Guhan (1994) has emphasised, structural adjustment 'accentuates the need for social security and does not basically alter the types of protection required' (Guhan, 1994, p. 40). As noted earlier, the Caribbean type economy has been susceptible to great difficulty in adjustment, given its very specialised export orientation. With the informalisation and growing precariousness of work that result from structural adjustment, funded programmes for the protection of workers are likely to cover a decreasing share of the work force and to create a major division between an aristocracy of workers and the rest, whose condition of employment prevents their acquiring adequate protection. In the circumstances, there is likely to be a larger group of persons who would need protection strictly of a transfer nature, following the end of their working careers, let alone those who, for whatever reason, had no labour force involvement.

In the context of the dominant ideology within which public policy is cast, there is likely to be less protection for the poor and the vulnerable, at the same time that economy is subject to greater fluctuations in fortunes and generates higher levels of structural poverty. Although there is a need for a higher level of social assistance, the philosophy that guided social assistance programmes derived from the Poor Law traditions of the last century. Moreover, the interventions necessary to improve the capabilities of the vulnerable workers, and to prepare them for reintegration into productive employment, following the collapse of particular sectors, has never been a clear policy objective in the Caribbean context. In other words, the existing ethos may well be institutionalising an incapacity to deal with poverty at the same time that economic processes are geared to increase poverty. The studies by Kairi (1996) confirmed a lack of coordination at the official level in treating with the various dimensions of poverty: the structure of the interventions were hardly tailored to reduce poverty.

According to Esping-Andersen (1990), historical factors have been very influential in the determination of the nature of welfare-statism that has developed in the industrialised North Atlantic, and can be typified around three models: socialist, conservative, and liberal represented respectively by Sweden, Germany, and the United States. These countries differ less in their

demography, than in their institutional features relating to social stratification, social rights, working life, and the evolution of employment. In other words, welfare and "workfare" are not unrelated.

The issue for Caribbean policy-makers is whether these can be so organised that poverty is contained, and as large a share of the resources of the society are utilised for transforming its structure such that these small economies become capable of adjusting to the changes in the internal economy with a minimum of social and economic vulnerability. This concern has not been addressed in the existing policy-framework, which makes poverty the inevitable result for important sections of the population of Commonwealth Caribbean countries.

References

Beckford, G, and Girvan, N., "Introduction," in Beckford, G. And Girvan N., eds., *Development in Suspense: Selected Papers and Proceedings of the First Conference of Caribbean Economists,* Friedrick Etbert Stifung, Kingston Jamaica, 1989.

Dreze, Jean, and Sen, Amartya, "Public Action for Social Security: Foundations and Strategy," in Ahamad, E., Dreze, J., Hills. J., and Sen, A., eds., *Social Security in Developing Countries,* Clarendon Press, Oxford, 1991.

Henry, R. And Mondesire, A., "Poverty Alleviation and Reduction Programmes: the Commonwealth Caribbean Experience" in Girvan, N., ed. *Poverty, Empowerment and Social Development in the Caribbean,* Canoe Press, Kingston.

Kaplinsky, R., "Export Processing Zones in the Dominican Republic: Transforming Manufactures into Commodities," *World Development,* Vol. 21, No. 11, 1993.

Lall, S., "Structural Adjustment and African Industry," *World Development,* Vol. 23, No. 12, 1995.

Odle, M.A., *Pension Funds in Labour Surplus Economies: An Analysis of the Developmental Role of Pension Plans in the Caribbean,* ISER, UWI, Mona, Jamaica 1974.

Wells, A.F., and Wells, D., *Friendly Societies in the West Indies: A Report on a Survey on a Despatch from the Secretary of State for the Colonies to the West Indian Governors,* Her Majesty's Stationery Office, London, 1953.

Poon, A., "Flexible Specialisation and Small Size: the Case of Caribbean Tourism," *World Development,*Vol, 18, No. 1, 1990.

Worrell, D., "Comparative Experience of CARICOM Countries," in Beckford, G. And Girvan N., eds, *Development in Suspense: Selected Papers and Proceedings of the First Conference of Caribbean Economists,* Friedrick Etbert Stifung, Kingston, Jamaica, 1989.

Economist, "Fiscal Providence, Singapore-style," *Economist,* p. 38, January 13th - 19th 1996.

World Bank. *Poverty Reduction and Human Resource Development in the Caribbean, Report No. 15342 LAC,* World Bank, Caribbean Division, Washington, 1996.

Kairi Consultants Limited, "Final Report on the Consultancy: Poverty Assessments and Training - Belize, St. Lucia and St. Vincent and the Grenadines", Caribbean Development Bank, Barbados, January 1997.

La Foucade, A.D. *A Review of the Evolution and Performance of Social Security Schemes in the English Speaking Caribbean,* Port of Spain: Inter American Conference on Social Security and the National Insurance Board, 1995.

CHAPTER 6

SOCIAL INSURANCE AND POVERTY ALLEVIATION IN A DEVELOPING COUNTRY: THE CASE OF TRINIDAD AND TOBAGO

JULIET MELVILLE[1]

[1] This paper benefited from the helpful comments and suggestions by Cecilia Melville.

Introduction

Since the entry of Trinidad and Tobago into a structural adjustment programme with the IMF in 1988, rhetoric about concern for the most disadvantage groups in the society has figured prominently in official circles. A number of policy initiatives has been started to protect these vulnerable groups. Nevertheless, the evidence to date suggests that poverty has worsened through the 1980s. This paper takes a critical look at the formal social insurance system in Trinidad and Tobago with the aim of determining its effectiveness in providing a measure of income security (in the wake of falling real incomes and deterioration living standards) and in tackling the wider issue of poverty. In order to be able to make a judgement about the efficacy of the social insurance scheme in combating poverty, one needs to know who are the poor and where they are located. On the basis of this, and given the scope of the insurance scheme, then some conclusions can be reached as to the role of the social insurance scheme in the fight against poverty.

The next section briefly reviews the rationale for social security. This is followed by an assessment of the poverty situation in Trinidad and Tobago. The state sponsored National Insurance Scheme (NIS) is then examined in Section 4, while Section 5 critically evaluates the NIS as a mechanism for poverty alleviation. Some concluding remarks are made in the final section.

Rationale for Social Security

Poverty is one social problem that has proven intractable in the face of efforts to eradicate it. Across time and space, there has always been segments of a society that have failed to attain a standard of living that is considered the norm for that particular society. Persons who are unable to attain this level of existence are regarded as 'poor' and enjoy some minimum level of welfare. By and large, societies have failed in their efforts to eradicate poverty and this is evident in that poverty remains one of the most (if not the most) pressing concerns of the 1990s. All societies (though with varying degree of interest and vigour) have focused attention on raising the level of welfare of persons falling below the poverty line. The systems which have evolved to safeguard welfare have been altered, adapted, modified and transformed in response to the changing character of the society. So whereas, in traditional societies. one's welfare revolved around the family and the immediate community, and

social wellbeing was based on mutual obligations and reciprocity, in today's modern, urbanised societies a set of formal mechanisms at the state level has developed to meet these needs. In fact modernisation and urbanisation have been culpable in the disruption and disappearance of tradition safety nets.

The mechanisms and institutions developed by modern society to take care of those less fortunate members who lack the capacity or are unable to provide for themselves are embodied in the society's social security system. Social security has been described as the "collective approaches a society has evolved to protect its members against economic risks" and measures to promote greater economic security. This all-encompassing view of social security includes within its purview" public action at the household, community, and state levels to reduce deprivation and vulnerability". Social security is intended to supplement the personal efforts of the individual to ensure access to certain basic goods and services critical to day to day living.

The literature points to a twin role for social security: preventing deprivation and preventing vulnerability to deprivation. According to the International Labour Organization, the goal of social security is "to provide individuals and families with the assurance that their standard of living will not be totally eroded when they are faced with temporary or permanent loss of income" and "to bridge the gap between affluence and need". Burgess and Stone (1991) see the goal of social security as the prevention by social means of very low standards of living irrespective of whether they are the result of chronic deprivation or temporary adversity (p. 43).

Ahmad, Dreze and Sen (1991) make a useful distinction between protective and promotional social security. Protective social security is concerned with 'forestalling a decline in living standards in general an basic conditions in particular'. This is aimed at preventing the individual and his/her family from crossing the threshold into poverty. The standard of living can be eroded because of temporary or permanent loss of income and reduced access to certain goods and services. Promotional social security is preoccupied with "enhancing the normal living conditions and dealing with regular and often persistent deprivation". Promotional social security is thus oriented to those who are considered to be chronically poor, and its immediate objective is to lift individuals out of poverty.

Modern social security measures are predominantly concerned with safeguarding or replacing earned income. For most people the ability to engage in remunerative employment for others or for oneself is the major, if not the only, source of income and therefore is a critical determinant of one's welfare given the predominance of market transactions. The biggest threat to a person's wellbeing comes from interruptions to one's working life which result in the loss of income. Sharp declines in income from work can have a profound impact on living standards of workers and their families (UNDP, 1995). Cockburn (1980) observed that with the increasing use of money wage, when wages are interrupted through sickness or accident, old age or invalidity, the means of livelihood disappear. In traditional societies, the victims of social accidents could look to the protection of the extended family and the village community. In modern society, social security measures have introduced to meet those problems of insecurity and to give protection against risks which impair or destroy the income of individuals and their ability to support their family. The introduction of social security at the national level is closely linked to the emergence of the modern sector. In the case of many developing countries, the establishment of social security schemes was intended to benefit the colonial administrators (Midgley, 1984).

Social security has invariably entailed protecting workers and their families from loss of earnings associated with unemployment or incapacity to work due to sickness, disability, or old age. This form of protection is embodied in the various social insurance schemes around the world. Social insurance falls under the class of protective social security. This is not specifically aimed at the poor, but according to McGreevy (1990) is "aimed at protecting modern sector workers and their families" and tends to exclude the needs of the really poor.

Social assistance is another element of social security measures employed to safeguard vulnerable groups. Social assistance is specifically aimed at the needy in the society. This usually entails direct income transfers to such groups, possibly through public work programmes targeted to the poor and the provision of social services by the state. Social assistance attempts to treat with chronic deprivation and persistent low levels of living. Programmes are designed to lift recipients up to some community determined minimum standard of living. In many countries social assistance is regarded in a less positive light than social insurance, the former often being regarded as handouts unrelated to the efforts of the individuals. Social assistance is normally financed

from central government revenues and recipients are subjected to a means test. In some countries, social assistance is used to supplement inadequate social insurance benefits.

For many developing countries, social security measures at the state level have tended to be preoccupied with the preventive role and have focused on protecting those members of the society engaged in paid employment in the formal sector through social insurance schemes. Attempts to address the needs of the chronically poor have been pursued through direct means such as income transfers, asset redistribution and the provision of certain basic goods and services by the state, and indirectly through attempts to promote rapid economic growth. Given the limited resources of most developing countries, with the exception of the provision of social services, the social assistance element of social security has tended to be very modest and ad hoc. In Trinidad and Tobago, both social insurance (in the form of the National Insurance Scheme [NIS]) and social assistance (consisting of the payment of an Old Ago Pension and Public Assistance) form part of the social safety net. The present analysis is concerned with evaluating the effectiveness of the NIS in alleviating the hardship of the poor.

The next section reviews the poverty situation in Trinidad and Tobago and examines the salient characteristics of the poor and the implications of these for measures to alleviate poverty.

Poverty in Trinidad and Tobago

Most recent studies on poverty in Trinidad and Tobago indicate that there is substantial number of households subsisting below the poverty line. Based on 1988 Central Statistical Office's (CSO) Household Budgetary Survey, Henry and Melville (1989)[2] found just over 18 percent of the sample households fell below the poverty line in 1988. This study was updated to 1992 and corresponding poverty rate was 22.5 percent.[3] Teekens[4] using the same

---

[2] The poverty line used in this study was drawn on every austere assumptions and ignored accommodation cost in the basked of goods costed.

[3] Social Agenda Policy Group, Building National Consensus on Social Policy: Trinidad and Tobago. Report of the Pilot Mission on Socio-economic Reform of the Inter-American Development Bank. Oct. 1993.

[4] Teekens (1989) included cost of accommodation and used household expenditure in defining the poor.

data set calculated a poverty rate of 14.8 percent for 1988. Subsequent studies by the Restructuring Support Unit of the Ministry of Planning and the World Bank estimated the absolute poverty level in 1992 at 32 percent and 21 percent respectively. The two latter studies were based on information collected from a Survey of Living Conditions (SLC) in 1992.

Table 6.1 - Incidence of Poverty in Trinidad and Tobago

Poverty	Henry & Melville		Teekens[1] (1988)	SLC[1] (1992)	Worldbank[1] (1992)
	(1988)	(1992)			
Poverty Line[2] (Monthly)	--	--	$220.00	$674.82	$202.00
Poverty Rate %	18.54	22.54	14.80	32.50	21.00
Urban Rate	18.90	19.04	13.50	37.30	24.00
Rural Rate	18.20	25.10	15.60	28.80	20.00
Male	--	21.00	13.60	28.50	18.40
Female	--	29.20	18.50	43.30	31.30

Notes: [1] Results reported for absolute poverty line.
[2] Henry and Melville (1988) attempted to take household size into account by calculating different poverty lines for different size household.. Instead of a single poverty line eight different cut off points were defined corresponding to one to eight or more persons households

Source: Henry R., J. Mellville. Poverty Revisited: Trinidad and Tobago in late 1980s. 1989
Teekens, R. Poverty Data from Two Family Budgetary Surveys in Trinidad and Tobago. 1989
Restructuring Support Unit. Trinidad and Tobago Survey of living Conditions: A Profile of Poverty In Trinidad and Tobago, 1992. Port of Spain: Ministry of Planning and Development, 1994.
World Bank. Trinidad and Tobago Poverty and Unemployment in an Oil Based Economy. 1995.

The information available indicates that the poverty situation in Trinidad and Tobago has deteriorated since the early 1980's. Both Henry and Melville (1989) and Teekens (1989) found evidence which showed that between 1981/82 and 1988 poverty had increased amongst all households and all categories of workers.

Table 6.2 - Selected Economic Indicators for Trinidad and Tobago (1980 - 1994)

Year	Real GDP Constant 1985 (TT$Mn)	Real Growth Rate (%)	Real per Capita GDP Constant 1985 ($TT)	Unemployment Rate (%)	Inflation Rate (%)
1980	20,291	--	19,221	9.9	17.5
1981	21,480	5.9	19,213	10.4	14.3
1982	22,298	3.8	19,256	9.9	11.4
1983	19,998	-10.3	17,269	11.1	16.7
1984	18,848	-5.8	16,082	13.4	13.3
1985	18,071	-4.1	15,237	15.6	7.7
1986	17,487	-3.3	14,577	17.2	7.7
1987	16,681	-4.6	13,650	22.2	10.8
1988	16,027	-3.9	12,915	22.0	7.8
1989	15,895	-0.8	12,595	22.0	11.4
1990	16,134	1.5	12,576	20.8	11.0
1991	16,637	3.1	13,264	18.5	3.8
1992	16,288	-2.1	12,824	19.6	6.5
1993	16,016	-1.7	12,493	19.2	10.8
1994	16,651	3.9	12,855	18.4	8.8

Source: Melville, C. Measuring the Social Impact of Adjustment: The Trinidad and Tobago Experience, MSc. Thesis, UWI, St. Augustine, 1996.

The greatest deterioration was recorded for the unemployed, own account workers and paid government employees. The later studies suggest that poverty has continued to rise.

Table 6.3 - Distribution of Poverty in Trinidad and Tobago

Location	Poverty Incidence						Unemployment Rate	
	Teekens 1988		World Bank 1992		SLC 1992		1988	1992
	% Poor	% of Total	% Poor	% of Total	% Poor	% of Total	%	%
Port of Spain	12.1	4.1	13.4	2.6	30.3	2.6	21.6	21.8
San Fernando	5.9	1.1	22.0	2.1	33.3	2.1	26.3	16.8
St. George	14.4	29.6	25.0[1]	23.5	38.5[1]	43.5	28.2	19.8
Caroni	11.2	12.4	5.9	4.2	24.2	4.2	21.0	18.0
Nariva/Mayaro	27.8	5.6	22.3	2.9	54.3	2.9	6.5	20.2
St. Andrew/ St. David	17.2	6.4	31.6	7.4	46.3	7.4	18.0	27.3
Victoria	19.3	25.4	24.4	19.0	59.0	19.0	22.3	16.0
St. Patrick	13.4	12.4	25.6[2]	15.2	31.0[2]	15.2	25.8	23.5
Tobago	11.8	3.0	17.5	3.1	32.5	3.1	25.6	20.9
Total	**14.8**	**100**	**21.2**	**100**	**32.5**	**100**	**22.3**	**19.6**

Notes: [1] Includes the Borough of Arima.
[2] Includes the Borough of St. Patrick

Source: Central Statistical Office, CSSP: Teekens (op. cit): Restructuring Support Unit. Trinidad and Tobago Survey of Living Conditions: A Profile of Poverty in Trinidad and Tobago, 1992. Port of Spain, Ministry of Planning and Development 1994 World Bank. Trinidad and Tobago Poverty and Unemployment in an Oil Based Economy, 1995.

The growth of poverty in Trinidad and Tobago in the late 1980s and early 1990s was no doubt closely associated with the dramatic contraction of the economy as a result of tumbling oil prices, and the subsequent attempts by government to stabilize the economy. According to Table 6.2, from 1983-1993 there was a secular decline in real GDP and real per capita GDP, and unemployment rate leapt above 10 percent reaching 22 percent in 1987.

Despite the differences in methodology, the findings of the various studies are robust with respect to the identity of the poor. The rate of poverty is marginally higher in the urban areas, but the number of poor is relatively divided between the rural and the urban areas. The highest incidence of poverty was found consistently exhibited the lowest rates of poverty. These global figures do not reveal the true extent of deprivation experienced by rural communities. As

Rampersad (1993) observed the rural population is inadequately serviced by public facilities which are inferior in the rural areas. Table 6.3 reveals that the biggest concentration of the poor is found in the county of St. George, and this is not surprising since this county has the highest population density.

The overall poverty rate is highest among households whose heads are unemployed, and those who work in the informal sector.[5] (Refer to Table 6.4). Households headed by old age pensioners and other retirees are likewise highly vulnerable to poverty. The unemployed figured prominently among the poor, accounting for 26 percent of all poor households. The amount of poor households in paid employment is quite significant as well. Based on the World Bank figures, almost 65 percent of the heads of all poor households had jobs, so even those with jobs have found living precarious. According to the World Bank Study, 27 percent of the heads of poor households worked in the private formal sector, 16 percent work in the informal sector and 22 percent worked in the public sector. A job in the formal sector does not necessarily guarantee an adequate level of income to escape poverty. The deterioration of the living standards of those in paid employment is due to a number of factors, not least of which is the absolute fall in income. This combined with the devaluation of the Trinidad and Tobago dollar and the removal of price controls have eroded real incomes. The introduction of user charges for some publicly provided service, removal of the book and uniform grants and the reduced scope of the school feeding programmes could only have aggravated the situation of poor households.

The employed poor can be found in craftwork or in other low paying elementary jobs. Agricultural Workers, Craftsmen, Plant and Elementary Works, and Service Workers have been identified as high-risk groups. Teekens' analysis revealed a surge in the poverty rate among agricultural workers between 1981 and 1988, from 2.1 percent to 25.3 percent and among construction workers from 2.3 percent to 17.1 percent (See Table 6.5).

Poverty among female-headed household appears intractable. According to Table 6.6, all categories of female-headed households are at greater risk than their male counterparts. The SLC found that 42 percent of male-headed single parent households lived in a state of poverty, compared with 50 percent of the

[5] The informal sector is defined to include unpaid workers, learners, apprentices, own account workers and small-scale employers.

female-headed single parent households. Overall, the poverty rate among female-headed household was 43 percent compared to 27 percent for male-headed households.

Table 6.4 - The Incidence of Poverty by Employment Status of Head of Household

Employment Status	Teekens 1988	SLC 1992	World Bank 1992	Teekens 1988	SLC 1992	World Bank 1992
	Incidence of Poverty			% of Poor Households		
Paid Empl. Gov't.	5.3	23	15	11.4	21.5	22.2
Paid Empl. Non-Gov't.	14.5	31.5	22.5	17.1	24.4	26.8
Own Account	20.6	34.1	23.8	20.5	14.6	15.8
Employer	--	.4	9.7	--	.04	1.0
Unemployed	33.6	46.2	28.3	19.4	12.6	25.6
Retired/OAP	14.1	40.9	--	14.8	15.7	--
Unclassified	22	46.4	18.3	16.7	11.0	1.1
Never worked	--	--	26.8	--	--	7.5

Source: Same as Table 7.3

Table 6.5 - Average Monthly per Capita Expenditure and Incidence of Poverty by Sector of Activity of Head of Household

Sector	Average Monthly per Capita Expenditure (1981 TT$)		Poverty Rate (%)	
	1981	1988	1981	1988
Agricultural	480	267	2.1	25.3
Manufacturing, Mining	666	457	1.7	5.4
Construction	607	301	2.3	17.1
Trade & Transport	763	437	3.1	10.4
Community, Social	809	478	2.3	6.6
No Industry	633	317	7.3	21.5
Not Classified	810	--	--	--

Source: Teekens (op. cit)

Among the female-headed households poverty is most severe among the single parent and the extended family households. These two household types make up more than 70 percent of the poor female-headed households. This is largely a reflection of the matrifocal nature of many households in the county. Poverty is more intense among single parent female heads who retired (75 percent), work in the informal sector (71 percent) or are unemployed (54 percent). (Refer to Table 7.7).

The incidence of poverty among male headed households is highest for the single parent male, but these households only constitute 6 percent of all poor male-headed households. The majority of poor male-headed households are of the nuclear (57.5 percent) and extended family (25 percent) types. Extreme poverty is prevalent among male single parent heads that are unemployed (75 percent) or are self-employed (60 percent).

Households with children seem very susceptible to poverty, particularly if these are female-headed, one-parent households, and if there are large numbers of children present. Poverty appears related to the number of children in the household. Households without children and those with only adult members fare the best.

Table 6.6 - Poverty Profile by Sex and Composition of Household

Composition	Male					
	Monthly per capita H/hold Expenditure	% Poor	% of Poor	Monthly per capita H/hold Expenditure	% Poor	% of Poor
Total		27.1	63.4	984.3	43.3	36.6
Single Person	1,588.1	28.6	11.8	13.2	49.2	18.7
Nuclear						
Head & Spouse	1,298.9	34.6	12.2	1.087.3	50	2.3
Head, Spouse & Children	1,169.4	23.7	45.3	1,041.1	29.7	6.4
Single Parent						
Head & Child	912.7	27.8	1.7	935.9	41.8	10.5
Head & Children	1,298.6	41.9	4.4	985.4	50	17.0
Extended & Children	923.7	29.1	24.7	866.2	41.8	45.0

Source: Restructuring Support Unit. Trinidad and Tobago Survey of Living Conditions: A Profile of Poverty in Trinidad and Tobago 1992 Port of Spain: Ministry of Planning and Development, 1994.

Table 6.7 - Poverty by Employment Status of Male and Female Single Parent Heads (SLC) - 1992

Employment Status	Male	Female
Paid Employee (Gov't)	18.8	40
Paid Employee (Private)	31.3	48
Own Account Worker	60	71.4
Employer	--	--
Unemployed	75	53.8
Retired without job	37.5	75
Not Classified	--	31

Source: Restructuring Support Unit (op. cit).

Social Security in Trinidad and Tobago

The National Insurance Scheme

The National Insurance Scheme (NIS) run by the National Insurance Board (NIB) is at the centre of social security system in Trinidad and Tobago. This is a compulsory system of state sponsored social insurance covering the employed labour force, and is intended to provide financial relief in the event a person becomes incapable of work and loses earnings due to illness, disability, pregnancy or old age.[6] The scheme thus provides for the payment of a benefit in the event of any disruption in earnings due to short term separation from the job (ill health, and child birth) and longer term, more permanent separation (retirement, permanent disability or death due to work related accidents). The NIS is financed by contributions of employees and the employers, with the former contributing one third of the total and the latter two thirds. Weekly or monthly deductions are made from employees' wages.

[6] This scheme provides insurance benefits for sickness and invalidity, maternity, employment injury and associated medical expenses, death related to employment injury, retirement, and a survivors and funeral grant.

The NIS covers persons between the *'age of 16-65 in insurable employment who must have made a minimum amount of contribution to the scheme in the period immediately preceding the benefit period'*.[7] In a few cases the benefits are extended to the immediate family (eg. Death Benefit). The scheme does not extend to self employed, nor to persons engaged in seasonal or informal employoment. Based on 1994 labour force data, some 22.1 percent of the labour force was excluded from the NIS. At the same time, the evidence indicates that self-employment[8] and informal sector employment are on the increase. The unemployed are also excluded from the scheme, this means another 17.8 percent of the labour force is not covered by the NIS. Some 40 percent of the labour force was not covered by the NIS in 1994.

Together with the already restricted coverage of the labour force, there are factors at work which are further eroding the reach of the system. Figures compiled by NIB showed that in 1993/94 the NIS covered only 58 percent of the eligible employer population. The data reveal a consistent decline in the coverage of the employer population by the NIS, despite a growth in the absolute number of employers. In 1983/84 the NIS covered 80 percent of all employers. A similar downward trend in the coverage of employed persons is apparent. Over 1989/90 - 1993/94 the ratio of active insured persons to the employed labour force fell from 69 percent to 58 percent. This represented an absolute decline in the numbers insured from 257.1 thousand to 239.1 thousand persons.

The NIS is heavily skewed in favour of pensioners and they are the main beneficiaries of the scheme. For the 1993/94 financial year, payments to pensioners accounted for 66 percent of the total value of benefits paid (Table 6.8). The retirement pension and grant together not only constituted the largest item in the NIS expenditure, but these were also the fastest growing components over the ten year period to 1993/94. Since the pension benefits are tied to earnings, McGreevy (1990) has argued that these tend to be skewed toward those with the higher incomes during their working lives.

---

[7] Only Employment Injury Benefit and the Funeral Grant do not have contribution requirement.

Table 6.8 - National Insurance Benefit Payments (Selected Years)

Year	Short-Term Benefits			Long-Term Benefits			Survivors	EIB Benefit	Total
	Sickness	Maternity	Funeral	Retirement Grant	Pension	Invalidity			
1983/84	7.53	8.36	0.86	0.93	56.75	7.19	10.76	7.62	100
1987/88	3.53	4.53	0.75	6.54	60.06	7.74	11.65	5.20	100
1990/91	2.83	3.44	1.23	7.04	60.81	7.83	12.36	4.46	100
1991/92	2.65	3.89	1.32	7.77	59.17	7.98	12.26	4.96	100
1992/93	2.46	4.00	1.51	7.50	61.00	7.24	12.04	4.25	100
1993/94	2.44	3.31	1.56	9.06	57.44	7.99	13.85	4.37	100

Source: National Insurance Board, Statistical Performance of the National Insurance System July 1983 - June 1994, Jan. 1995

Low benefit payments may make the limited coverage and scope of the NIS a mute point. NIS contributions and benefit payments appear totally out of line with average incomes in the country. In 1981 contribution income was 2.5 percent of the aggregate wage bill. This has remained unchanged since 1980. The maximum monthly contribution is only TT$25.80. The very low contribution levels no doubt impair the NIB's ability to make realistic benefit payments. Figures compiled by the NIB show that the real value of its benefits has eroded overtime.

The level of benefits raises questions about whether these can be regarded as a meaningful source of income replacement. Comparing pension benefits with the poverty line it becomes clear that only for retirees is the higher earning classes (Class V and above), would replacement income exceed the poverty line calculated by the World Bank in 1992 at $202 per month. On the basis of the poverty line calculated by the SL ($674.82/month) pensioners in all categories would fall below the poverty line. The current level of old age pension provided by the state at a rate of $425 per month is greater than the maximum payable under the NIB.

The short-term benefits (employment injury, sickness and maternity) appear a bit more generous, as those in earning class IV and above, receive payments

which exceed the World Bank's threshold income. Clearly, for the lower income groups the NIS fails in its function of providing some measure of income security in the advent of disruption in earnings.

Table 6.9 - Contribution and Benefit Payments by Earning Class

Weekly Earnings	Earning Class	Contribution (Weekly)	Pension/ Invalidity (Monthly)	Injury (Monthly)	Sickness/ Maternity (Monthly)
<50.00	I	$1.10	$130	$117	$104
$50.00-64.99	II	1.60	130	165	149
65.00-84.99	II	2.10	130	217	195
85.00-109.99	IV	2.75	169	282	253
110.00-139.99	V	3.50	204	360	325
140.00-179.00	VI	4.50	248	463	416
180.00-229.99	VII	5.75	313	593	533
230.00+	VIII	6.45	338	663	598

Source: NIB Guide to National Insurance Benefits

The provision for medical expenses appears even more out of sync with actual medical expenses. The benefit provided to meet medical expenses is a tiny fraction of the actual cost of procuring the various services. The benefit for a visit to a specialist is only about 25 percent the actual cost, while that for a visit to a general practitioner is approximately 20 percent of the actual cost. The maximum $100 provided for drugs appear woefully inadequate given the current cost of medicine. The level of medical benefits is of particular concern given the attempts by government to introduce user charges for publicly funded health services and the rapidly escalating cost of both public and private medical services, and the absence of any policy towards ensuring that the needy continue to have access to these services.

Table 6.10 - Rates of Payment of Medical Expenses

Type of Expenditure	Rate per visit $	Actual Cost $
General Practitioner	10	50
Specialist	25	100
Psychiatrist Initial consultation Follow up	 30 25	
Drugs	<100	300*
Private Hospital	50[1]	
Operations Minor Intermediate Major	400	1305.31**

Note: *indicates 1990 per capita drug expenditure
**is the average amount of claims submitted under group medical plan.
[1] Includes cost of investigations, drugs and X-rays
Source: NIB National Insurance Employment Injury Benefit Booklet.
The Coopers and Lybrand Consulting Group, Government of Trinidad and Tobago NHIS Project: Statistical Research Report 1993.

Overall, the levels of benefits paid by the NIS run the risk of becoming totally irrelevant to the participants in the scheme, and moreso for the poor. The NIS's benefits are not indexed to the cost of living, and benefits have tended to lag behind the rising cost of living. La Foucade (1995) attributes the low levels of nominal payments and limited coverage to the low levels of contribution income and the small percentage of contribution income collected (p.5). The NIS contributions are also not tied to increases in income and the NIS faces a number of short-term and long-term challenges which could further threaten the viability of the system. La Foucade (*op cit*) discusses the impending threat of actuarial imbalance. The NIS strategic plan points to the late payment of contributions by a large number of employers, declining employment levels, high administrative cost, and the inefficient use of contribution income to generate returns, among other factors.

Social Insurance as a Mechanism for Poverty Alleviation

The NIS is not explicitly geared for assisting the poor and those in long term deprivation. It is protective in scope and is aimed at assisting workers in the formal sector (both public and private), who have made contributions to the scheme, in the face of temporary adversity and loss of income through retirement. As Table 6.11, which summarises the characteristics of the poor, indicates the highest rates of poverty exist among groups least likely to be covered by the NIS. Data collected in the Survey of Living Conditions in 1992, reveal that individuals in the lower income brackets are least likely to have NIS coverage, moreover, NIS coverage is lowest for those aged 19-24 and 55-64, and workers in the rural counties (Table 6.12).

Even for workers covered by the programme the protection which the NIS provides is limited. The very low levels of benefits reduce the scheme's effectiveness as a safety net for those in the lower income brackets. Only one group which the studies on poverty have identified as vulnerable may enjoy some measure of income security: the aged who have paid their contribution to the NIS. There is a high incidence of poverty among the aged, thus to the extent the NIS guarantees this group a source of income, this will go some way in alleviating hardship. The benefit paid to those retirees in the lower income brackets though, is likely to be inadequate to prevent them experiencing poverty. Aged persons in this income bracket are entitled to receive the government's old age pension providing their annual income does not exceed $4,500. Since the maximum pension paid by the NIS ($338 per month) does not reach this figure it is therefore possible for those receiving the NIS pension to supplement this with the state pension. The high incidence of poverty among the aged might therefore indicate that a large number of the aged are not covered by the NIS or any another pension scheme and are therefore dependent on the state pension alone.

Although there is a substantial number of households with employed heads in poverty, the NIS does not provide any relief for these households. Except for pension payments, all other NIS benefits are paid only in the case of temporary separation from employment. In addition, a number of households below the poverty line has large numbers of children. The NIS provides a family benefit only under very restrictive circumstances, that is, in the event of death of the breadwinner as a result of work related injury. A 1995 internal study by the NIB concluded that the benefits in general were not sensitive to household size, to

that the protection which the NIS gives to households diminishes for larger households.[8] The NIS thus offers limited poverty relief for those who are in 'gainful' employment. NIS does not compensate for low paying jobs.

Table 6.11 - Household and Individual Characteristics by Poor/Non-Poor

Characteristics	All T&T	Poor	Non-Poor
Household Level (HH)			
No. of HH in sample	1487	219	1234
Urban (%)	44.11	48.40	42.62
Male Headed HH (%)	73.43	63.47	75.60
Age of HH Head	48.83	47.00	49.03
HH Size	4.25	6.09	3.95
No. of Children (<16)	1.38	2.44	1.13
No. of Workers/HH	1.30	1.16	1.33
No. of Unemployed/HH	0.45	0.81	0.38
Per Capita Expenditure	7250	1702	8235
Individual Level			
Participation Rate (%)	60.2	56.4	61.1
Unemployment Rate (%)	20.4	36.0	17.1
Employed Individuals			
Sector of Work Employed			
Public	34.3	20.6	36.6
Private (Formal)	42.5	50.0	41.3
Informal	23.1	29.4	22.1
Occupation			
Senior Professionals	5.0	1.2	5.7
Professionals	3.8	0.8	4.0
Associate Professionals	9.5	3.2	10.5
Clerks	12.4	6.8	13.4
Services	13.0	12.4	13.0
Agriculture	4.5	7.2	3.9
Crafts	15.9	21.7	14.8
Machine Operators	10.7	7.2	11.3
Elementary Occupations	25.2	39.4	23.4

Source: World Bank. Trinidad and Tobago Poverty and Unemployment in an Oil Based Economy 1995 p. 157

[8] National Insurance Board. Poverty Analysis. Port of Spain, 1995, p.8.

Table 6.12 - National Insurance Coverage (Percentage Covered)

Covered	Age Groups		
	19-24	25-34	35-64
QUINTLE			
Poorest 20%	14.4	21.0	14.3
II	11.5	31.3	25.0
III	26.5	38.7	31.3
IV	31.6	48.1	36.8
Richest 20%	39.1	62.5	45.3
COUNTY			
Port of Spain	30.8	55.4	65.0
San Fernando	35.7	46.4	0.0
St. George	26.7	44.4	27.1
Caroni	28.6	45.4	47.2
Nariva	6.7	17.5	42.9
St. Andrew	15.2	23.4	14.3
Victoria	20.0	39.0	34.5
St. Patrick	17.1	41.5	27.3
Tobago	36.4	61.0	56.3
SECTOR			
Urban	27.4	45.5	31.8
Rural	22.0	40.5	36.7
OVERALL	24.3	42.7	34.7
Sample Size	666	2321	320

Source: World Bank. Trinidad and Tobago Poverty and Unemployment in an Oil Based Economy. 1995 p. 135

Female-headed households are of particular concern given their relatively higher incidence of poverty. The NIS is unsuitable for tackling the problem of female poverty. The only NIS benefit which is aimed specifically at women is the maternity benefit, the other NIS benefits are gender neutral. Additionally, a disproportionate number of women tend to find employment in the informal sector which is outside the NIS. Williams and Henry (undated) found a relative dominance of women in commerce and services.

The NIS is irrelevant to the long-term poor and the new poor (those who as a result of the crisis of the 1980s have lost their livelihood). The unemployed and informal sector workers comprise the majority of this group and they are likely to be the most vulnerable groups in Trinidad and Tobago. Low levels of income and precarious working conditions make the life of the informal sector worker extremely vulnerable. Because of the sometimes erratic nature of

informal work, this makes the extension of social insurance schemes particularly difficult. Unemployment is one of the important causes of income insecurity and of poverty, but the NIS does not cover loss of income due to unemployment. Unemployment benefit schemes are rarely provided in developing countries because they are complicated and costly to administer. Mahabir (1996) discusses some of the difficulties associated with devising unemployment insurance schemes in countries where there are large pools of unemployed and limited means of financing these. Further, the young and those with low levels of education are likely to be found among the unemployed and are also the least likely to have found jobs covered by the NIS.

Concluding Remarks

The NIS is unsuited in aim and design to tackle the issue of poverty. It is aimed at protecting those who have found gainful employment in the modern formal and who may suffer temporary or permanent loss of income through illness, disability or old age. Even for its target group, the size of the NIS benefits and the failure of these to keep pace with inflation effectively reduces the credibility of the NIS as a mechanism for providing some measure of income security. Social insurance schemes are in the main inappropriate for tackling the major causes of poverty: unemployment, low incomes, inability to find jobs, lack of assets, etc. Midgley (1984) contends that social insurance schemes in developing countries tend to accentuate inequality, and have an overall regressive effect. In the long term, poverty can only be overcome by the generation of jobs which pays a living wage. Thus skill training and access to credit and other resources are key factors in the fight against poverty.

In the short term, income transfers and provision of social services by the state are critical to alleviating the hardships associated with poverty. The longstanding components of the state's social assistance programme, the Public Assistance Programme, is given under exacting criteria and is targeted at those persons unable to earn a living because they are incapacitated, and women and children left destitute after the death of desertion of a male breadwinner.[9] Here again the vulnerable groups are excluded. Those in greatest need of assistance, are likely to be the least able to negotiate the

[9] A family grant is paid on behalf of a dependant wife and children when the breadwinner is dead, imprisoned, hospitalised or deserted.

government bureaucracy to access the various welfare services. Women face bureaucratic and legal hurdles in seeking assistance for their families. Women and their children qualify if they can prove desertion by the husband or partner and can establish that they had tried unsuccessfully to have the court impose a maintenance order on the father of their children (William and Henry (undated) p. 100). The Public Assistance Act is clearly in need of revision to reflect the fact that many women carry a disproportionate financial burden for maintaining a significant number of households. Even where the male breadwinner is technically employed, it should be possible for women to access assistance if the household's income falls below a certain critical minimum. In addition, new systems for ensuring that absent fathers maintain their offsprings, and that realistic sums be paid for child maintenance in keeping with the cost of living will have to be considered as weapons in the fight against female and child poverty. More importantly, in the design of public policy to combat poverty, the central role played by women in the survival of their households must be given due recognition. Policies which are based on the false assumption that women play a subsidiary or secondary role in many households will only lead to misguided policy prescriptions.

The Public Assistance Programme probably has the greatest potential for impacting directly on the needy, although perhaps because of budgetary constraints it has never been viewed in this light. Public assistance is not intended to assist the employed needy or able-bodied persons who may become needy due to unemployment. While the latter has been the focus of government's policy,[10] the needy employed persons have been largely ignored.

The employed poor falls between the cracks of the available social assistance programmes. Some attention therefore needs to be paid to those employed persons who subsist in poverty. Policy makers need to pay close attention, not just to the issue of job creation, but also to the types of jobs created. It is

[10] There exists a number of programmes aimed at building the human capital of displaced workers and potential entrants to the labour force (Youth Training Enterprise Programme (YTEPP). Retraining Programme for Displaced Workers, National Apprenticeship Scheme, etc.) More recently, funds have been allocated for the rehabilitation of Public Assistance recipients and other needy persons to become self-reliant, for example the Micro Enterprise Projects and the Training and Development Projects. Other social assistance programmes geared to the unemployed is the Unemployment Relief Programme (URP) which provides temporary employment, of 1-2 months duration each year is also targeted at the unemployed.

not sufficient that jobs are created, but jobs which pay a living wage to workers must be the goal of public policy to deal with the problem of the employed poor.

With deteriorating real income and job insecurity, increasingly more persons will be looking to the state for support. Budgetary constraints mean there is limited scope for expanding existing social assistance programmes, at the same time the government is being forced to cut back its provision of social services and to introduce user charges for those services provided. To ensure the needy have access to essential goods and services, therefore, requires clear objective criteria for determining access (at present the criteria are quite hazy) and better targeting to reach those most in need. The NIS controls a fairly sizeable amount of financial resources, which are currently invested in real estate, government security and bank deposits. It may be a useful idea to explore the alternative use of these financial resources in more productive ventures (projects) which will benefit those with low income and still yield an acceptable rate or return.

References

Burgess, R.N. Stern. "Social Security in Developing Countries: What, Why, Who and How? In Social Security in Developing Countries. Edited by J. Dreze et.al. Oxford: Clarendon Press (1991): 41-

Cockburn, C. "The Role of Social Security in Development" in International Social Security Review. No. ¾(1980): 337-358

Dreze, J.A. Sen. "Public Action for Social Security: Foundation and Strategy" in Social Security in Developing Countries. Edited by J. Dreze et al. Oxford: Clarendon Press (1991) 3-40.

Henry, R., J. Melville: Poverty Revisited: Trinidad and Tobago in the Late 1980s. Paper read at Regional Conference on New Direction in Social Policy, UWI, St. Augustine and Trinidad and Tobago Association of Social Workers, Hugh Wooding Law School, St. Augustine, 28-31 March, 1990.

La Foucade, A.D. A Review of the Evolution and Performance of Social Security Schemes in the English Speaking Caribbean. Port of Spain: Inter American Conference on Social Security and the National Insurance Board, 1995.

Mac Kenzie, G.A. "Social Security Issues in Developing Countries: The Latin American Experience" IMF Staff Papers, 35 (1988): 496-522.

Mahabir, D. "Unemployment Insurance in the Small Open Economy: Towards Optimal Programme Design". Journal of Caribbean Issues. 7 (1996) forthcoming.

Mc Greevy, W. "Social Security in Latin America" World Bank Discussion Papers, No. 110, 1990.

Mesa-Lago. C. "Social Security in Latin America and the Caribbean: A Comparative Assessment". In Social Security in Developing Countries. Edited by J. Dreze et.al. Oxford: Clarendon Press (1991): 356-394.

Midgley, J. Social Security, Inequality, and the Third World. New York: John Wiley and Sons, 1984.

National Insurance Board. Corporate Strategic Plan: 1994/95 - 1999/2000: Trinidad and Tobago: Planning Research Division, 1995.

_____. Poverty Analysis: Trinidad and Tobago: Planning and Research Division, 1995.

_____. Statistical Performance of the National Insurance System: July 1983 - June 1994. Trinidad and Tobago: Planning and Research Division. 1995.

Rampersad, Frank. "Rural-Urban Imbalance" in Building National Consensus on Social Policy: Trinidad and Tobago. Social Agenda Policy Group, Report of the Pilot Mission on Socio-Economic Reform of the Inter-American Development Bank (1993), Vol 2, p. 61-76.

Restructuring Support Unit, Trinidad and Tobago Survey of Living Conditions 1992: A Profile of Poverty in Trinidad and Tobago. Port of Spain: Ministry of Planning and Development, 1994.

Social Agenda Policy Group. Building National Consensus on Social Policy: Trinidad and Tobago. Report of the Pilot Mission on Socio-Economic Reform of the Inter-American Development Bank. 1993.

Teekens, R. Poverty Data from Two Family Budgetary Surveys in Trinidad and Tobago. Unpublished Report of EC Consultant to the Central Statistical Office, 1990.

The Coopers and Lybrand Consulting Group. Government of Trinidad and Tobago NHIS project: Statistical Research Report. 1993.

United Nations Development Report. Human Development Report 1994.

Williams, G. and R. Henry. "Engendering the Adjustment Process in Trinidad and Tobago: Perspectives and Policy Issues", in Women Pay the Price: Structural Adjustment in Africa and the Caribbean. Edited by G.T. Emeagwali. New Jersey: Africa World Press (undated).

World Bank. Trinidad and Tobago: Poverty and Unemployment in an Oil Based Economy. 1995.

CHAPTER 7

THE INCLUSION OF HEALTH UNDER SOCIAL SECURITY COVERAGE: ADMINISTRATIVE, FINANCIAL AND ECONOMIC CONSIDERATIONS

KARL THEODORE

AND

ALTHEA DIANNE LA FOUCADE

Introduction

The social security schemes in the Caribbean are under increasing pressure to expand coverage of both benefits and population. This pressure is no doubt related to the fiscal difficulties being experienced by many governments. With the adjustment-induced pressures on the State to maintain existing social services or introduce new ones, and with the waning of the capacity of the State to do so, it is not surprising that there would be a call for other agencies to shoulder these responsibilities. It is also not surprising that social security schemes (SSSs) are being considered first among these supplanting agencies.

One area where supplanting agencies are clearly needed is health. The continued uncertainty surrounding Central Government's expenditure on the public health sector in some countries, as well as the observed deterioration in the health infrastructure in others, point to the need for supplementary financing of health services. Among the most popular options being advocated are: (i) greater reliance on private out-of-pocket financing; and (ii) a strengthening of the existing social solidarity fabric via the social [health] insurance route.

This paper takes as given that the former - a move toward private-out-of-pocket financing of health care needs - is not a desirable option for the region at this time in our history given the negative implications for our longer-term development objectives. Rather, given the fact that an increasing number of countries are showing a desire to explore the second option, the present study addresses various issues surrounding the inclusion of social health insurance under the ambit of social security in the Caribbean. Emphasis is placed on the question of the capacity of social security schemes in the region to contribute to the provision of health security. However, while there are two approaches that are generally suggested for bringing about improvements in the health system: broadening the financing base; and strengthening both the financing and delivery system, the paper will only focus on the first of these. There are two reasons why the latter approach is not addressed here within the context of social security. First, this is not the option being considered by the English-speaking Caribbean. Second, the experience of those Latin American countries that have opted for the latter approach certainly do not recommend it to the Caribbean (Mesa-Lago 1991).

The efforts of those countries within the English-speaking Caribbean now seriously considering an extension of the social security umbrella to health insurance benefits have highlighted three (3) concerns. Firstly, in some cases, it is generally felt that the social insurance experience of the existing SSSs renders them eminently capable to administer the proposed national health insurance (NHI) systems. At the same time, however, there is a concern that the administration of a health financing system will overwhelm the SSSs with additional managerial demands.

Secondly, in the face of impending actuarial imbalances within the social security schemes, it is mandatory that any NHI system incorporated under the social security umbrella be in an independently sound financial position. In fact, there is almost no support for merging the existing social security systems with a NHI system in the hope for an overall actuarial balance. The third concern is the potential of a combined Social Security-National Health Insurance Fund to influence the operations of the capital markets these countries.

This paper addresses each of these concerns, the administrative concerns, the financial viability concerns and the capital market concerns. The issue here is whether coverage of health benefits will negatively affect the impact of social security on the working of the economic system. The overriding context is taken as one in which the social security schemes themselves have been experiencing actuarial imbalances, erosion of the value of benefits and shrinking contribution bases. Coupled with higher expectations on the part of beneficiaries, and a changing labour market structure skewed against formal employment, recommendations have been made to increase social security incomes by increasing compliance and implementing higher contribution rates.

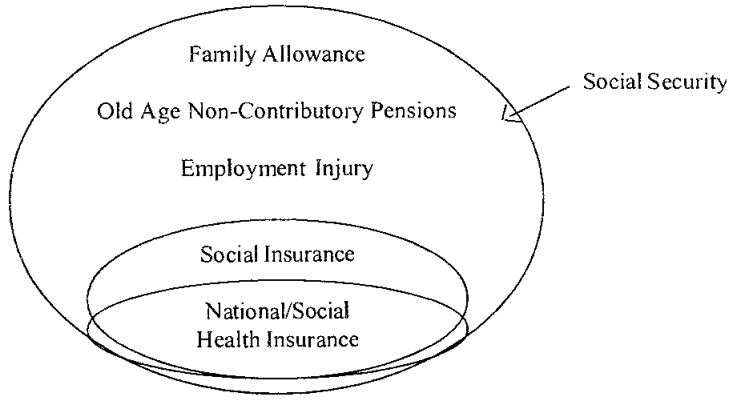
The Administrative Concern

The Social Security/Social Health Insurance Link

The term *"social security"* as used in this study encompasses all aspects of the social security umbrella (Midgley 1984). That is, it is seen as a totality of the programmes in place to reduce uncertainty in respect of income flows and in respect of the quality of living (ILO 1984). As such, social insurance of

which social health insurance is a subset, falls under the auspices of social security (Mesa-Lago 1990). The diagram below illustrates the relationship.

Figure 7.1
Link Between Social Security and National Health Insurance



National health insurance could therefore be seen as the arm of social security which ***"secures the health"*** of the citizenry. The rationale being that to the extent that health is seen as an enabling attribute with the potential to enhance the quality of life, then health security is consistent with the objective of social security- to guarantee some minimum quality of life.

Having said this however, nothing dictates that any new programme, national health insurance included, must be housed within any of the established/ existing arms of a country's social safety net arrangements (ILO 1990; Mesa-Lago 1990). By the same token though, there is also no *a priori* reason why, in principle, an existing social insurance system cannot accommodate an additional division - a NHI division. What will be important is that the implications of the new undertaking be clearly understood.

In this regard, the administrative demands on the social security system arising from an NHI responsibility will be fivefold:

- the collection of payments;
- the processing of claims;
- the payment of claims;
- the collection of information; and
- the processing of information and production of reports.

It should be clear from this listing that no "new" administrative responsibilities are called for. A major difference, however, would be the greater importance of the last two functions - data collection and report production. The accuracy and relevance of the information collected and the timeliness of the reports produced will be of critical importance to the continued viability of the NHI. For example, since a key objective of the NHI will be the enhancement of the efficiency as well as the equity of the health system, the information collected must facilitate performance monitoring (of the NHI) on these two criteria.

Related to these two criteria is the critical issue of coverage. We take up this issue in the context of the Caribbean.

Provision of Social Health Insurance in the Region

The issue of coverage, particularly as it relates to the expansion of coverage to universal provision of benefits and universal provision for the population is not new in this region (Fletcher 1976; La Foucade 1995). In many cases, there was initial commitment to eventually move the schemes in the direction of universal coverage (Fletcher 1976). However, this has not been realised (US Department of Health and Human Services 1994; La Foucade 1995). As Tables 7.1 and 7.2 indicate, some sections of the population in the Caribbean have continued to be excluded from social security coverage.

The universality of social security involves the extension of coverage to 100 percent of the population. On the one hand, universality of social insurance coverage involves 100 percent coverage of eligible contributors[1] and dependants. In all cases the governments in the countries considering implementation of national health insurance have declared their commitment to equity access to health care. This is to be achieved via a universal NHI system, made possible by the State undertaking to make contributions on behalf of those citizens who cannot contribute for themselves and their families. Health insurance coverage as a social security undertaking would therefore ideally aim at coverage of all citizens in the event of defined medical needs.

---

[1] Here a contributor is taken to refer to someone who either contributors directly - for himself/herself - or someone on whose behalf a contribution is made. For example, the State may undertake to contribute on behalf of targeted groups.

Table 7.1 - Statutory Covered and Uncovered Population

Country	Covered Population	Uncovered Population
Antigua-Barbuda	Employed 16-59	Family and Casual Employment with wages under EC$7.50 per week.
Bahamas, The	Employed, Self-employed, Voluntarily insured	---
Barbados	Employed, self-employed	Unpaid family labour
Belize	Employed 14-64, voluntarily insured	Casual labour, family labour, persons employed <8 hrs/wk, domestics working < 24 hrs/wk and military personnel.
Dominica	14-60 employed and apprentices, self-employed	---
Grenada	Employedand self-employed 16-59	---
Guyana	Employed and self-employed 16-59, voluntary coverage	Employees earning< G$7.50/wk, casual and subsidiary employment, and family labour.
Jamaica	Employed and self-employed, voluntary coverage over 18 and under retirement age	Casual workers and unpaid family labour
St. Kitts-Nevis	Employed persons includingapprentices 16-62	Unpaid family labour, self-employed
St. Lucia	Employed persons and apprentices 16-65	Civil servants
St. Vincent & The Grenadines	Employed 16-59	Self-employed
Trinidad & Tobago	Employed 16-64 including agricultural, domestics, apprentices, public employees	Self-employed

Source: U.S. Department of Health and Human Services 1994.

Table 7.2 - Types of Social Security Programs in Place

Country	OADS	Sickness/ Maternity	Employ-ment Injury	Unemploy-ment	Self-Employed	Voluntary Coverage	Medical Benefits
Antigua-Barbuda	X	X					X
Bahamas, The	X	X	X		X	X	X
Barbados	X	X	X	X	X	X	
Belize	X	X	X		X	X	
Dominica	X	X	X		X	X	X
Cuba	X	X	X		X		X
Grenada	X	X			X	X	
Guyana	X	X	X		X	X	X
Haiti	X		X				
Jamaica	X				X	X	X
St. Kitts-Nevis	X	X	X			X	X
St. Lucia	X	X	X				X
St. Vincent & The Grenadines	X	X	X				X
Trinidad & Tobago	X	X	X		X	X	

Source: U.S. Department of Health and Human Services 1994; La Foucade 1995.

However, a review of the evolution of social security in the region suggests a tendency to continue provision along the same lines as when the various individual social security schemes started. Reference here is to the range of benefits and population coverage (La Foucade 1995). In fact, it is those countries that are now providing medical benefits that appear to be showing greatest interest in NHI. The countries that have clearly signalled their intention to move in the direction of NHI include Antigua-Barbuda, Dominica, Jamaica, St. Kitts-Nevis, St. Lucia, and St. Vincent and the Grenadines. By the same token, those countries that do not now provide medical benefits under social security, for example, Barbados and Trinidad and Tobago, have not shown a strong commitment to implement NHI in the very near future.

Here it should also be noted that the Organisation of Eastern Caribbean States (OECS) and the other smaller countries of the region have been long discussing the possibility of harmonization of their social security schemes. These countries have also shown a willingness to explore the implications of consolidating the administrative efforts of the existing social security agencies with a NHI system. In the case of the British Virgin Islands, Dominica, St. Lucia and St. Vincent and the Grenadines, social security administrators are already heavily involved in the planning for the financing reforms of the health sector. What seems to be emerging in the region, is a situation in which countries with SSSs that are perceived to be making a difference in the lives of their members are more inclined to consider introduction of NHI. Moreover, in so doing they are also more inclined to explore the potential for cost savings by having the existing schemes play a major role in administration of the NHI.

In this regard, it is probably interesting to note that whereas in countries like Jamaica and Trinidad and Tobago NHI feasibility studies have been funded by external agencies, in some of the other countries initial funding for examination of NHI is actually expected to come from their social security schemes. This has certainly been the signal coming from St. Kitts-Nevis, St. Lucia, St. Vincent and the Grenadines, and possibly Dominica. One possible benefit of this approach would be the relative freedom to design the kind of NHI system, which is in tune with the overall developmental agenda of the countries concerned.

One of the more important features of the financing system being discussed is the coverage of the medically indigent under NHI.

The Medically Indigent

To the extent that universality, equity and solidarity are recognised as pillars of social health insurance, then the question of how and what provisions are to be made for the medically indigent becomes paramount. Here one should recall that according to Table 7.1, most of the social security insurance-based benefits/contributions, are not available to the non-working, non-economically active sections of the population. Indeed, in many cases NHI would be an exemplar within the region in this regard, since by all appearances it is poised to dismantle the clear demarcation that now exists between the employed and unemployed insofar as it relates to contribution-insurance-based social security programmes. The expectation is that this would be achieved via the

State. Thus far, the State in the Caribbean has never hesitated to make firm commitments to providing for the medically indigent population (Coopers and Lybrand 1994; MOH Jamaica 1997). However, since the NHI will certainly not be covering all health services it would be important to be clear about the provisions that would be made for the medically indigent for accessing services not covered under NHI.

On the question of the widening of the net to provide insurance coverage for segments of the population that are unable to contribute to the system, the general insurance approach would dictate that some other segment(s) of the populace will be required to subsidise the former category. In this sense universal coverage of defined health services will strengthen the distributive function of the Social Security Scheme.

It will be important that bureaucratic obstacles are not erected as substitutes for the previous income-related barriers to access that the NHI will be seeking to effectively neutralize. Potential citizens at risk here would include those:

- turned away at the time of genuine health need due to lack of coverage or, even worse, due to inadequate documentation of coverage;

- in dire need of medical attention who are subjected to an elaborate screening process when they access the health system, in order to establish indigence.

Financial Concerns

The major financial concern will be the possibility of the NHI becoming an extra burden on the social security system. In contemplating the possible coverage of health under social security there would seem to be at least two major considerations which must be borne in mind:

(i) the fact that the establishment of the required equilibrium between the social security system and the NHI need not be attempted as a one-off exercise; and

(ii) the fact that the viability of the NHI rests on striking a proper balance between the scope of the services covered and the need to institute effective cost

controls. One index of success would be the behaviour of administrative expenses.

We will now deal with these two issues.

Phasing of Social Health Insurance

It is important to recognise that any proposed link between the social security and the Social Health Insurance could be seen as a phased process. The justification of the phasing is derived from the recognition that the NHI essentially has two (2) basic functions. The first is a health function and the other a fiscal function.

The health function of the NHI as we have seen earlier, lies in its potential to contribute to the maintenance and improvement of the health conditions of the population. It does this not only by providing the funds necessary for continuous care but also by creating an incentive framework for providers and users of the health system to ensure good quality health services at reasonable costs. In other words, NHI could well act as the sustaining factor for the health system.

It is in recognition of the existence of this first function that NHI is usually touted as being not just a financing mechanism, but rather a resource allocation mechanism, with the power to become the *"efficiency wedge"* of the health system.

The second function is simply to provide relief to the State's coffers by transferring financing obligations from the Ministry of Finance directly to employees and employers.

However, the reality is that in order to carry out the health function, the NHI system needs to be supported by a relatively high-quality managerial structure and an efficient information system. The latter (information system) should allow for the marrying of epidemiological, financial and socioeconomic information in such a way as to be one of the main direction-providing mechanisms for the system.

Since these requirements are both time-consuming and costly, they may have the potential to become sources of delay in the implementation of the NHI. In

attempting to address this problem it is possible for the NHI/social security link to be introduced in the first phase, simply for purposes of fiscal relief to the State.

What this would mean is that the social security schemes will need to put themselves in a position to make a direct and meaningful contribution to the design and implementation of the health security budget. The model suggested in Eastern Caribbean countries like St. Kitts-Nevis, St. Lucia and Antigua-Barbuda may with some modification, become the basis of phase I of the NHI/ social security link. In this model, the contribution rate of the social security schemes can be modified to provide a targeted fraction of the overall health budget.

However, while in the countries where the model now applies the benefits are restricted to contributors and their dependants, there is no reason for any such restrictions to apply where the NHI is envisaged as being a key instrument in providing the widest possible access to the health system. Of course, the restrictions on who makes contributions: the employed, self-employed, would also be no longer feasible (on viability and equity grounds) with any extension of the community of beneficiaries.

Also of note would be the inevitable fact that this model of financing may vary in success depending on the structure of the labour force. For example, in countries like Guyana, Jamaica and Trinidad and Tobago, where the informally employed and the self-employed comprise a fairly large section of the population of working age, the social security contribution net may not be wide enough for health purposes if the base continues to be fully or majority dependent on income- based contributions.

In order to make the system more effective, the NHI/social security contribution to the health budget may be targeted towards those services which are seen to be both most cost-effective and most relevant given existing epidemiological realities.

It would of course be helpful if the NHI contribution is jointly managed by the social security agents and the Ministry of Health. In other words, the fiscal support being provided by the link must be used as an opportunity to improve the quality of management in the health sector and to ensure better value for

money. What this means is that the complexities of reimbursements do not arise.

Administrative Expenses

The social security schemes in the English-speaking Caribbean have generally been subjected to rising administrative costs. With very few exceptions, the relatively older schemes and even some of those that started operations in the second half of the 1970s, are in a reform phase with a major aim being to increase the efficiency with which the social security activities are being undertaken. A related strategy has been to realise reductions in the share of administrative expenses in total expenditures. In the case of the National Insurance Board of Trinidad and Tobago, the path to reform has included a relatively high percentage reduction of staff, beginning in 1995.

Concerns about the additional costs of having responsibility for the administration of another fund - NHI - have admittedly been a recurring issue (ISSA 1995). Coverage of the medically indigent will usually involve administering health promotion programs geared at keeping the claims of this group as few as possible. Together with this, controlling costs incurred in the actual provision of health services would normally require instituting a review mechanism linked to a sophisticated information system.

It should come as no surprise that the administrative expenses of the expanded Social Security Scheme would initially exceed past levels. In this context, the experience of administrative expenses in the countries of the region could be instructive.

According to the data in Table 7.3 below, Anguilla experienced an increase of some 65 percent in the share of administrative expenses in contribution income over the 1982-1992 period. Over the same period, Antigua-Barbuda witnessed a 9.8 percent increase, while the growth rate for the other OECS ranged from as high as 183 percent (British Virgin Islands) to a low of 8 percent (St. Kitts-Nevis) over the corresponding period. Moreover, the situation is even more worrying when looked at from the eyes of the share of administrative expenses in contribution income (see Table 7.4).

However, one needs to be weary of misconstruing the figures presented. What the data tell us is certainly not that social security schemes may not be able to

efficiently administer a NHI System at this time. The suggestion however, is that the NHI will have to be structured, implemented and managed in such a way that it does not impose any additionally unbearable burden on the existing components of social security services now provided. This takes us to the observed trend in the actuarial standing of the social security schemes in the region.

Actuarial Standing

In this sub-section, we use one measure of the actuarial position of the social security schemes. That is, the share of contribution income as a percentage of total expenditure.

In all cases we observe a decreasing trend in the percentage share of contribution income in total expenditure. This would suggest that even in the case of the smaller, less mature schemes, expenditures have been increasing at a faster rate than contributions. Table 7.5 provides detail.

According to the data therefore, what the social security schemes certainly do not need at this stage in their development is for partners (new and old), to leave cost-tabs that are not picked-up or honoured.

The point being made here is that while it may be cost-effective for the social security schemes to join forces with the NHI, in some identified areas of administration, the partners in health would need to be critically aware, and be respectful of the existing obligations of the social security schemes to provide future security to contributors and beneficiaries. At the same time social security managers must certainly be ever mindful that these are not obligations that could be jeopardised without a boomeranging effect on their continued survival and relevance.

Table 7.3 - Administrative Expenses as a Percentage of Contribution Income

Country	Incep-tion	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993
Anguilla	10.94	---	---	10.94	11.93	15.35	15.92	14.44	11.69	11.36	12.70	13.78	15.06	18.05	---
Antigua-Barbuda	---	10.82	12.84	12.73	13.84	16.74	20.52	19.19	17.01	14.45	15.09	14.31	15.71	13.98	---
British Virgin Islands	4.09	---	---	4.09	5.70	6.83	6.62	7.46	5.66	6.14	10.83	23.47	11.14	11.59	15.68
Dominica	---	17.12	17.73	16.54	17.00	15.62	13.12	15.07	13.90	14.90	20.45	27.42	20.66	20.25	19.04
Grenada	2.52	---	---	---	2.52	16.98	17.42	6.43	8.08	7.24	9.54	12.29	13.16	23.12	---
Montserrat	107.42	---	---	---	---	---	---	107.42	47.28	41.91	41.72	39.16	39.83	---	---
St. Kitts-Nevis	---	8.02	7.22	7.60	9.68	8.33	9.18	9.81	9.31	10.43	8.28	19.07	17.20	8.17	---
St. Lucia	---	8.36	11.12	13.27	16.60	12.82	16.60	10.74	13.32	11.21	10.92	17.72	20.10	15.96	---
St. Vincent and The Grenadines	---	19.06	21.75	22.44	27.56	28.27	30.86	30.58	31.72	27.17	23.98	25.26	23.14	21.76	---

Source: Annual Reports Social Security/National Insurance Schemes. (Various Editions)

Table 7.4 - Administrative Expenses as a Percentage of Total Expenditure

Country	Incep-tion	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993
Anguilla	89.42	---	---	89.42	63.02	72.00	68.54	61.54	54.39	51.68	57.43	54.85	57.74	55.88	---
Antigua-Barbuda	---	33.32	36.55	34.94	33.89	38.74	44.56	40.39	34.67	31.99	32.09	31.68	32.76	30.63	---
British Virgin Islands	34.86	---	---	34.86	40.94	46.91	39.65	43.51	58.14	33.79	44.88	61.92	46.05	42.27	45.74
Dominica	---	53.73	53.59	49.61	43.26	33.06	30.88	31.95	29.24	29.44	35.23	42.46	31.04	26.83	25.28
Grenada	90.48	---	---	---	90.48	77.46	78.48	44.10	43.53	36.70	30.24	32.62	35.17	36.41	---
Montserrat		79.37	---	---	---	---	---	79.37	86.03	72.14	69.53	73.91	70.10	---	---
St. Kitts-Nevis	---	28.99	32.25	26.69	34.11	26.33	27.36	30.92	31.15	10.01	15.40	37.30	38.66	23.87	---
St. Lucia	---	53.75	52.52	55.46	49.87	51.67	40.71	39.10	38.57	35.93	40.22	43.28	43.40	38.43	---
St. Vincent and The Grenadines	---	73.69	69.38	68.19	67.88	67.64	67.58	64.08	76.30	67.38	64.77	61.33	59.20	53.42	---

Source: Annual Reports Social Security/National Insurance Schemes. (Various Editions).

What this then means is that it becomes necessary that the level of NHI contributions needed must be determined and adjusted rigorous actuarial analyses. It would also mean that policy makers, social security administrators, contributors and beneficiaries will all have to embrace an enlightened understanding of actuarial analyses.

Since a rigorous actuarial analysis will reflect both demographic and economic changes that impact on the capability of the SSS it would not make sense for policy makers to ignore the recommendations made. Indeed, the expansion of coverage to health would benefit from the dynamic nature of actuarial analysis and highlights its usefulness in sustaining the SSS.

The issue of updates of contribution requirements (premiums) and benefits based on sound actuarial reviews becomes even more critical when benefits are provided in the eventuality of illness and unemployment. The point being made is that given the nature of the trend in the cost of health care and its percentage share of the total incomes of the economies, nothing logically justifies basing policy decisions on obsolete analyses.

Table 7.5 - Actuarial Standing of Selected Caribbean Social Security Schemes (Contribution Income as Percentage of Total Expenditure)

Country	Incep-tion	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993
Anguilla	817.3	—	—	817.3	528.1	469.1	430.5	426.2	465.2	454.9	452.2	398.1	383.5	309.6	—
Antigua-Barbuda	—	307.9	284.6	274.4	244.9	231.4	217.2	210.5	203.8	221.4	212.7	221.3	208.6	219.1	—
British Virgin Islands	851.5	—	—	851.5	718.8	686.9	599.3	583.1	—	550.3	414.4	263.8	413.3	364.9	291.7
Dominica	—	313.8	302.3	300.0	254.4	211.7	235.4	211.9	210.3	197.6	172.3	154.9	150.2	132.5	132.8
Grenada	3590.5	—	—	—	3590.5	456.3	450.6	685.8	538.8	506.8	317.1	265.5	267.2	157.5	—
Montserrat	73.9	—	—	—	—	—	—	73.9	181.9	172.1	166.7	188.7	176.0	—	—
St. Kitts-Nevis	—	361.5	446.6	351.1	352.2	316.2	297.9	315.3	334.8	95.9	185.9	195.6	224.7	292.3	—
St. Lucia	—	642.8	472.3	417.9	300.4	403.2	245.2	363.9	289.7	320.4	368.3	244.3	215.9	240.7	—

Source: La Foucade 1995; National Insurance Boards' Annual Reports (Various Editions).

The Capital Market Concern

Following the work of Feldstein (1974) there has been a long-standing concern that the social security system might be imposing a negative influence on the capital accumulation drive of the economy. It is true that the evidence in support of this claim has been strongly challenged.[2] It is also true that the proposition that the social security system derives its rationale from the efficiency benefits conferred on the economy suggests that the savings critique under estimates the value of social security systems. However, it can still be argued that it is the operations of the system that will determine whether its capital market effect will be positive or even neutral.

This capital market concern is of special significance in a small economy with an underdeveloped capital market. In fact, within this context it can be argued that the social security system has the potential to be one of the engines of growth of the economic system. This is especially true before the system has matured and is generating surpluses that can be channelled into long term productive investment. If the system is buttressed by a financially successful NHI, its capacity to influence the fortunes of the entire economy becomes even more extensive.

It is true social security and National Insurance payments represent a withdrawal from the income stream. Their benefits represent injections into the income stream. In any given period therefore it is the net effect of the payments and benefits that would matter to the capital market. If we assume that the phasing of benefits coverage will allow the NHI to build up its reserves, the NHI may just be the shot in the arm needed by social security systems on the verge of maturity.

The situation becomes even more interesting if we assume that the context is also one of social security reforms where the social security systems are seeking to play a greater role in the productive side of the economy, as a means of safeguarding their own long-term pension funds. It is now generally understood that the traditional investment role of the social security systems - mainly limited to purchasing of government securities - will not be adequate

---

[2] Koskela, Errki and Viren Matti (1983) Social Security and Household Saving in an International Cross Section, American Economic Review, 73, 212-17.

to generate the levels of income needed to offset the almost predictable erosion of long term funds. The evidence of the last twenty years indicates that the rate of inflation has eroded the real yield of social security investments.

Among the constraints here would be the normal regulations governing social security investment. A recent UWI study has shown that these investments were unrelated to capital formation. In the most positive cases the investments extended only to private mortgages or to urban services infrastructure - shopping malls, car parks, etc. Key sectors like Agriculture, Tourism and Construction have generally had no supply boosts from the social security schemes.

The inclusion of health under social security therefore provides a stronger imperative for the revision of the investment laws governing the schemes. There is greater need now for flexibility in being able to respond to domestic and international market conditions. The globalisation of trading and financial systems means that potential investors now face many more opportunities than before. By the same token, if there is no change in investing behaviour there is no question that the gap between "global" investors and other investors will continue to widen, with all that this implies for the contribution base of the social security systems.

Within this global context one of the important considerations will be the behaviour of the rate of interest - more specifically the spread between domestic and international rates. While in the long term the evolution of this spread will depend on the relative performance of the economies in question, in the short run the action that will be sometimes needed to cope with unfavourable interest rate movements, will require the intervention of a significant player in the market. Apart from the respective Central Banks the only other candidates will be the social security schemes. Strengthened by the inclusion of NHI, this role will be further enhanced.

So far we have been assuming that the inclusion of NHI will bring a level of investment sophistication to the social security schemes. This is because the proposed financial information system, the calibre of the personnel involved in social security investments, the quality of the response to actuarial reviews are all expected to lead to an upgrading of the quality of management.

Conclusion

This paper took as its starting point the fact that some countries within the English-speaking Caribbean are now seriously considering, putting systems in place to extend the social security umbrella to health coverage. Basically, two (2) developments have been taking place. Firstly, in some cases, for example St. Lucia and a number of the OECS, while it is generally felt that the experience(s) of the social security agencies render them best suited to administer the newly proposed NHI systems, there are efforts to clearly define the areas of administration that the social security agency could take responsibility for managing most cost-effectively.

Secondly, due to the experience and the threat of impending actuarial imbalance, the need to get the funding of any NHI scheme on a sound footing is engaging the efforts of many in these countries. What certainly seems clear is that the question of totally merging the proposed NHI with the existing social security-social insurance systems does not seem to be on the agenda for most of the countries where such systems are currently the subject matter of much research and policy-oriented efforts.

In considering the administrative, financial and economic issues that arise from the extension of social security to health coverage, the study makes the point that what matters to the success of this extension is the way in which the extension is designed and implemented. If the expanded system benefits from an upgraded management structure, there is every reason to believe that the proposed coverage of health will successfully link the Social Security Scheme, with the development efforts of the English-speaking Caribbean.

References

Coopers and Lybrand. *From Vision to Reality*. Trinidad and Tobago National Health Insurance Project, 1994.

Fletcher, P. L. "The Provident Fund Approach to Social Security in the Eastern Caribbean." *Journal of Social Policy* 5 (1976): 1-17.

International Labour Office. *World Labour Report: Employment, Incomes, Social Protection, New Technology*. Geneva: International Labour Office, 1984.

International Social Security Association. *Ninth Meeting of Heads of ISSA Member Organizations in the English-speaking Caribbean*. Roseau, Dominica, 28-31 March 1995.

La Foucade, A. *A Review of the Evolution and Performance of Social Security Schemes in the English-speaking Caribbean*. Port of Spain & Mexico: the National Insurance Board and InterAmerican Conference on Social Security, 1995.

Mesa-Lago, C. *Social Security and Prospects for Equity in Latin America*. World Bank Discussion Papers, 140. Washington D. C. : World Bank, 1991.

. "Social Security in Latin America and the Caribbean: A Comparative Assessment." In *Social Security in Developing Countries*, edited by J. Dreze et. Al. Oxford: Clarendon Press (1991): 356-394.

Midgley, J. *Social Security, Inequality, and the Third World*. Chichester: John Wiley and Sons, 1984.

Ministry of Health, Jamaica. *National Health Insurance Plan for Jamaica, Green Paper*. Kingston: Ministry of Health, April 1997.

National Insurance/Social Security Schemes. Annual reports. (Various Editions).

Suarez R. et. al. *National Health Expenditure and Financing in Latin America and the Caribbean: Challenges for the 1990s*. Health Development Series No 3, Washington D. C.: PAHO/WHO, 1995.

Theodore, K. "The Economics of Health Sector Reform in the Caribbean." St. Augustine, Trinidad: The University of the West Indies, School of Continuing Studies. 1996.

U. S. Department of Health and Human Services. *Social Security Programs Throughout the World: 1995*. Washington: Social Security Administration, 1994.

CHAPTER 8

FINANCING HEALTH SERVICES THROUGH SOCIAL HEALTH INSURANCE: LESSONS OF EXPERIENCE FOR POLICY MAKERS

STANLEY LALTA

Introduction

Despite wide differences in objectives and starting conditions, the current upsurge of interest in social or compulsory health insurance (SHI) among policy-makers and researchers in Industrialised and Developing Countries (IC's and DC's) generally emanate from proposals and ongoing programmes to reform their health systems and the financing of health services in particular (World Bank, 1987; OECD, 1992; World Bank, 1993; Preker et. al., 1996). The motivations for this increased attention on SHI are quite varied.

a) In DC's without SHI programmes economic and budgetary difficulties have severely constrained the ability of the State to finance and provide health services. This is reflected in declining real health budgets, low salaries, shortages of staff, equipment and supplies and generally low quality care.

Attempts to introduce and institutionalise user fees as a revenue-generating mechanism have generally not been well-accepted or successful. The examples of operational SHI and other health insurance/prepayment schemes in IC's and other DC's (Mills, 1983; Glaser, 1991; Roemer, 1993; La Forgia et. al., 1993;) as well as the recommendations of several international organisations such as the World Bank (World Bank, 1987 and 1993, Shaw and Griffin, 1993), the ILO (Ron et. al., 1990; Normand and Weber, 1994) and the WHO (Ron, 1993; Kutzin and Barnum, 1994; Serjeant and Carrin, 1995) have encouraged policy makers to explore the possibilities of SHI.

b) In DC's with SHI (or statutory health insurance) programmes e.g. States in Latin America and Asia, problems of inequity in access, cost escalation and excessive emphasis on doctor-centred, high-technology, urban-based curative services have led to serious concerns over the mission and sustainability of these programmes (Mesa-Lago, 1989; Griffin, 1990; Yang, 1990; La Forgia et.al., 1993; Kutzin and Barnum, 1994).

c) In the formerly socialist countries, the decline of the "paramount" State as the main financier of health services and the negative social impact of recently privatised health services have left policy makers searching for health financing alternatives and several recommendations are being

considered for SHI programmes (Sheiman, 1994; Ensor, 1993; Preker et. al., 1996).

d) In IC's without substantial SHI programmes and which rely more on private insurance and private health care markets e.g. USA, problems of cost escalation, inequity, suplier-induced demand and the neglect of primary care have led to a continuing debate over proposals for various SHI programmes (Navarro, 1989, Glaser, 1991 and 1993; Fuchs, 1993; Steinmo and Watts, 1995), A fairly similar situation may be said to exist in South Africa (Bachman, 1994).

e) In IC's with established SHI i.e., European States, Canada and Japan, the concerns are over the rationing of health services, cost control, efficiency in the delivery of services and consumer satisfaction (OECD, 1992).

Based on the above it seems that while some countries are moving towards the adoption of SHI programmes, others are busily engaged in reforming their programmes (or are contemplating reforms). This suggests the need for caution in the design and implementation of SHI programmes and continuous re-engineering to ensure that the objectives of the programme and the health system as a whole are being achieved. For countries contemplating the introduction of SHI it also suggests the need for a more detailed examination of the theoretical and empirical basis to avoid the pitfalls and optimise the gains of SHI.

This review seeks to synthesise the concepts of and experiences with SHI. It begins with a discussion and assessment of the theoretical principles and perspectives on health insurance and to what extent these expectations are applicable to SHI. The second Section focuses on the conceptual and design issues in SHI. It also looks at the relative merits and shortcomings of SHI as compared with other health financing mechanisms. The experiences of countries with SHI programmes as the main source of health financing are examined in Section III to ascertain what works and why, what are the specific problems encountered and how these have been tackled. The analysis will focus on performance in relation to Mills' (1983) five-point criteria for an appropriate health financing mechanism i.e.,

- distribution of financial burden and access to benefits by different groups;

- quantity and quality of services it finances;
- efficiency of service provision;
- efficiency of administration; and,
- achievement of national health goals.

The final Section will seek to integrate the findings from the review, and again using Mills' five-point criteria, to ascertain what lessons can be derived from the various experiences for countries contemplating SHI programmes.

Health Insurance: Some Theoretical Perspectives

In general terms, insurance is a risk-pooling mechanism to reduce or mitigate financial loss resulting from an unpredictable event. Adam Smith saw it as providing "great security to the fortunes of private people and by dividing among a great many that loss which would ruin an individual makes it fall light and easy upon the whole society" (Quoted in Borch, 1992). There are certain key aspects of the theory of insurance which have far-reaching implications for the design and practice of health insurance. Among these are:

i. **Risk-aversion and Utility Maximisation:** Faced with future financial uncertainties (when the "state of the world" is unknown) risk-averse individuals (as compared to risk-neutral and risk-loving persons) wishing to maximise expected utility and minimise loss of wealth may be quite willing to pay a fair premium (i.e., equal to the expected loss or the probability of the loss multiplied by the value of the loss) to an insurer for protection against the risks. Paying a fair premium may mean a reduction in current wealth but if this is compensated by increased utility in the future state then the risk-averter (and society as a whole if many more persons behave similarly) will be better-off (Arrow, 1963; Mehr, Cammack and Rose, 1985). Since it is inconceivable that all possible risks can be covered (given imperfect information of the future), the rational risk-averse individual will tend to purchase more insurance protection for events which are "low probability-high loss" rather than those of an opposite nature.

ii. **Insurability of Risks:** Not all risks are insurable or can be pooled or will be covered by an insurer (at an affordable premium). Given current information, insurers do not cover risks which are certain to occur (within a defined time period) nor do they cover eventualities already occurring ("burning houses").

At the same time, consumers do not insure for events which are certain not to occur nor do they seek cover for events which will have fairly negligible effects on their welfare (Dionne and Harrington, 1992). An insurable event/ risk is one which:

- is catastrophic i.e. causes large, measurable losses (not easily contrived.);
- affects a large number of people independently;
- is rare with a low probability of occurring;
- occurs randomly for each individual but is known for the population.

iii. **The Insurance Market:** Using the Paretian definition, an efficient insurance market is one in which "no one can be made better off without making someone worse off" This implies that there are many suppliers and buyers; that there is generally perfect information so that the type and mix of insurance products being offered cover the demand of consumers; and that the price (premium) clears the market and maximises the utility functions of both parties i.e. it is adequate to cover the expected claims on the supplier plus its loading costs while still being fair to the consumer (Borch, 1992). However, particularly the insurance market (as compared to other markets) is more generally characterised by incomplete and asymmetric information (Arrow, 1963; Pauly, 1968; Wilson, 1977). This can and has resulted in widespread market failure and disequilibria with the following being the most common:

- **Adverse Selection** ... the tendency for more high-risk persons to seek insurance cover when an average premium is used. This can lead to more frequent payments by the insurer, high premia, smaller membership as low risk persons drop out and eventually the collapse of the market.

- **Risk Selection (Cream-skimming or Cherry-picking)** ... insurers respond to adverse selection by applying sophisticated risk assessment and rating techniques (underwriting) to screen out high risk persons or to offer differentiated insurance products and premia.

- **Moral Hazard** ... the tendency for individuals, once insured, to behave in a manner which increases the probability of the covered risk occurring or to consume significantly more services than would have occurred in the absence of insurance. Various cost-sharing

arrangements (co-payments and deductibles) may be necessary to deter such behaviour by the insured.

- **Over- and Under-Insurance** ... in the absence of perfect information, the market may not appropriately match the real "needs" of consumers for insurance so that some may end up with more cover and higher costs than warranted while the opposite may occur for other persons.

In many respects these general theoretical principles and observations on insurance (as outlined above) are applicable to health insurance. However, there are also certain peculiar and particular features of health insurance and of SHI for which the general theory is silent or does not offer full explanations.

Risk-averse Behaviour

Health risks are ubiquitous and generally unpredictable - disease, invalidity and accidents. The determinant factors range from the physiological and behavioural to those which are more structural and socio-economic. This leads to considerable uncertainty over the timing, nature, cost and outcomes of treatment. As such risk-averse individuals especially income earners and heads of households will seek health insurance as a rational choice. The demand for such insurance will generally depend on the premium, self-assessment of the probability and magnitude of the loss and the degree of risk aversion (Mills, 1983) although there are several other specific variables which are taken into account in determining the type and amount of insurance which will be bought.

On the other hand, health insurance is not a typical private good or service and its demand curve may not always display the characteristic properties. There are several reasons for this:

- the value of the asset in question - the human body - cannot be related solely to income or employment losses;

- health has dual properties. It is a consumption and investment good, thus making the decision to purchase insurance contingent on some variables which are more relevant to risk-taking behaviour;

- health "needs" are quite significant and are not always reflected in health "demand" or in the demand for health insurance;

- health has properties which are not just confined to the individual. Externalities - positive and negative - in health imply that the "normal" demand curve for health insurance (based on individual ability and willingness to pay) is not always applicable and the market will consistently under-provide health insurance.

Insurability of Health Risks

Certain health risks satisfy the conditions for insurability as outlined in ii) above. However, there are many other health risks - some may say the majority - which are not insurable in the strict sense. (In fact, insurance companies and actuaries generally considered health insurance as an "oxymoron" and only recently they began to develop health insurance products as compared to other types of insurance. See La Forgia, 1993). The reasons for this can be found in the nature of health risks and health seeking behaviour:

- health risks are not always infrequent or unpredictable and in fact several are discretionary in nature i.e., directly attributable to voluntary action (or inaction).

- not all illness occurs randomly nor are independent. Externalities and interdependence are significant aspects of health and illness.

- not all costs are high or catastrophic.

The Health Insurance Market

The manifestations of market failure are even more pronounced and pervasive in the case of health insurance. In seeking to counteract **adverse selection**, insurers have had to develop sophisticated rating and underwriting techniques to segment the market and so set a "fair premium" which relates risk and expected loss as close as possible to individual behavior. The general objective is to include and rate any factor which can predict future demand for health services and future costs -age. sex, race, education, occupation, residence location, health status and medical history. Individual and group rating techniques are supplemented by exclusions, waiting periods, medical testing and at times denial of insurance cover. The overall result may be efficient for the insurer and individual insured but from a social perspective, it leaves

significant groups ineligible for insurance or insurance that is minimal or at a very high cost.

Moral hazard has implications not just for cost escalation but also for managing the behaviour of health providers. The demand curve for health services is not independent of the actions of the health service providers. In fact, some researchers ascribe more weight to "supplier-induced" demand arising from the "principal-agent" relation as being responsible for observed moral hazard (Evans, 1986; Fuchs, 1993). As the third party intermediary, the insurer has had to institute various cost sharing and utilisation limiting measures to contain demand as well as payment mechanisms (global budgets, case based payments etc. vs. retrospective fee for service) and medical management measures (prior authorisation for hospitalisation, concurrent reviews, second opinions for expensive treatments etc.) to control providers.

On the other hand, as Evans (1986) has pointed out that the health insurance market fails to deal adequately with health "needs" and "externalities" and as such at least over a range some moral hazard is justifiable.

Over-insurance is common where the individual (or the employer) is subsidised and is not or only partially responsible for the full premium. Several individuals or population groups may be **under-insured** because of the inability to pay the "actuarially fair" premium or because of choice i.e. the systematic or unknowing under-estimation of one's subjective disease risk and as such the requirement to use as many health services over a period of time.

Another aspect of market failure is the likely development of monopoly firms or cartels in the provision of health insurance. These lead to sub-optimal choices, prices and product lines in the health insurance market which generally place consumers at a disadvantage in terms of welfare maximisation.

The persistence of the above market failures (despite efforts to regulate, control, offer incentives for efficiency etc.) has resulted in serious doubts over the ability of the private and unregulated health insurance market to provide optimal solutions for risk-sharing and financial protection. These concerns are increased when issues of equity are considered (in relation to unmet health needs and the exclusion of many persons from the market through risk selection mechanisms) as well as the overall compatibility of the unregulated health

insurance market (led by the "invisible hand") with the health objectives of a country.

In DC's there are other specific factors which may affect the working of the market (Griffin,1990):

- the quantity and quality of available health services
- the extent of poverty
- the extent of free or heavily subsidised health services
- the dispersed populations
- the size of the working population in the informal and semi-formal sectors

Some of these concerns can be dealt with in SHI programmes which are based on "social solidarity" and "collective equivalence" (Glaser, 1991) and which are not just "upscaling" of private health insurance products. It should be noted however that SHI programmes are not immune from the dangers and market failures in private markets (as will be discussed in Sections III and IV). Their ability to cope with and circumvent market failures depend to a large extent on the design of the programme - this is examined in the next Section.

SHI: Expected Benefits and Design Issues

SHI is primarily a health insurance mechanism which is based on social solidarity rather than actuarial fairness. This means that its main function is to serve as a primary source of health security and financial protection to individuals and families. In addition, like other health financing mechanisms, SHI is not an end in itself but an instrument for achieving the health goals of the country (Navarro, 1989; WHO, 1993). These goals as seen by health managers and policy-makers include (Hsiao, 1990):

- mobilising adequate funds to provide the mix of services required to meet health needs and demands;

- allocating these funds and organising the delivery of services in an efficient and effective manner;

- ensuring universal and equitable access to health services.

In examining the expected benefits and design of SHI programmes, the dual functions of SHI -the individual and national objectives - must be borne in mind if it is to be acceptable, viable and appropriate. (The tendency to focus exclusively or disproportionately on the "national" functions and implications of SHI while ignoring its role in satisfying the objectives of the individual is an important aspect of the ongoing debate on its acceptability as compared to "customer-designed" private health insurance).

Expected Benefits of SHI:

Various writers - both supporters and opponents - have tended to focus on particular benefits and advantages of SHI. In general, compared to other health financing mechanisms (general taxes, user fees, private health insurance, foreign grants and aid), SHI offers the following benefits (Ron et. al., 1990; Glaser, 1991; Abel-Smith, 1992; Roemer, 1993; Normand and Weber, 1994):

- it is a stable source of financing;
- it can pay for the full cost of health services;
- it combines risk-pooling with mutual support thus reducing adverse selection and redistributing benefits and costs "from each according to his ability to each according to his needs". Those contributing more than they utilise are the high wage earners, single persons, small families and the young while those receiving more benefits than they contribute are low wage earners, the disabled/invalid, large families and the old;
- it provides a visible and dedicated flow of funds to health services without reducing the volume of funds available to the Ministries of Health;
- it establishes the rights of the individual as a customer rather than as a patient;
- it provides more bargaining power to the purchaser in negotiations with providers;
- it can be used more effectively to contain costs than private health insurance;

- it can build on existing Social Security arrangements;
- it can co-exist and supplement other health financing mechanisms.

In looking at the expected benefits of SHI, it should be noted that SHI is not the same as programmes for universal coverage. The former provides benefits on the basis of one's contributions and designation as a beneficiary while the latter provides benefits as a right of citizenship whether contributions are made or not (Mills, 1983; Hoffmeyer and McCarthy, 1994). Thus even though both may involve compulsory deductions, SHI is funded from earmarked payroll taxes or other specific contributions e.g. in Germany, France and Brazil while the latter is funded from general or local taxes e.g. in Canada, UK and Sweden.

Issues in the Design of SHI Programmes:

In designing the SHI programme, it is suggested that the following issues be addressed (Ron et. al., 1990; Glaser, 1991; La Forgia, 1993; Normand and Weber, 1994):

- the health goals and priorities of the country;
- net revenue generation - especially if inadequate funding of health services is a major constraint as in most DC's;
- equity in spreading the burden of cost and contribution and in the entitlement to benefits. This means a combination of progressive contribution rates and standard benefits for all (Wagstaff, 1992);
- reducing cost escalation and moral hazard;
- availability of timely and high quality health services;
- the availability of the required administrative capability;
- accountability and responsibility of the administrative agency or funds for the overall viability and operations of the programme;
- the structure of the labour market and the economic dependency ratio in the population;

- the level of competition. Competition among insurance suppliers or "funds" can enhance choice, lead to lower premium with profit maximisation and membership as the goals, lead to innovative policies and management and penalise inefficiency with collapse. On the other hand, competition can lead to high administrative and marketing costs, the need for costly regulative structures and inadequate risk pooling for economies of scale and viability in some funds;

- the integration of health services from the primary to tertiary levels.

Based on the above, the literature indicates that there are nine (9) key elements around which the SHI programme and policy options will be developed (bearing in mind the specific needs, capabilities and vision of the country). These are:

The Conceptual Framework

Will the programme be treated as a supplementary or alternative (the dominant) source of funding? If the former, what other financing mechanisms will be used and how will the allocation of financing responsibility take place? If the latter what will happen to current financing arrangements? Will the programme offer traditional indemnity insurance like private insurers or will it offer benefits in kind only?

The Administrative Arrangements

Will the programme be organised as a single statutory fund or will there be competing or non-competing funds? How will these smaller funds be organised - by industry, by region, by occupational groups or on an open enrolment basis? Will funds be permitted to exclude any prospective members? Will there be a central governing body to regulate and monitor these funds? Or will there be a central body collecting the contributions and distributing them among the competing funds according to the risk profile of their membership? What will be the relationship between these funds or the single statutory fund and the Ministry of Health or of Finance and the existing Social Security agencies? Which agency or agencies will be responsible for negotiating fees and contracts for services with the providers?

Package of Services to be Covered

Will this be a comprehensive package covering primary, secondary and tertiary services in the public and private sectors? Or a catastrophic care package only with the option of securing additional insurance from alternative sources? Or will this be a basic package covering a selected mix of primary and secondary care services? What services will be included and which will be excluded in any package?

Universality of Coverage

Will the programme seek to cover the entire population? or selected groups such as those in the formal sector or those in full-time occupations? Will dependents be covered also and how will dependents be defined? What special regimes will be required to enlist farmers, the self-employed, informal sector workers - lower premium, lower cost-sharing, lower income ceiling, special representation on the management board?

Contributions/Premium

Who pays - formally employed only? the self-employed? Pensioners and retirees? How much do they pay? How will the contribution be shared among the worker, employer and government? How will the contribution rate be assessed - as a fixed percentage (proportional) of income or earnings? Or on a progressive basis? Will there be differential rates for classes of risks? Will rates be set by the State or by the statutory fund or by each competing fund? Will there be ceilings and floors for insurable earnings? Will contributions be tax deductible? And how will rates be indexed to the rate of inflation or to wage indices? To the cost of health services or the fiscal capacity of the administrative agency?

Co-payments and Utilisation Limits

Will beneficiaries be faced with zero or small copayments? On all or some items of service? Will this be a fixed fee or a percentage of cost? Will this be set centrally and apply to all providers or will there be varying rates? Will extra-billing be permitted? How will utilisation limits be fixed—visits per year per family, bed-days per episode? Will members be able to choose their physician or hospital or will their be restrictions?

Provision of Services

Will the SHI agency or funds seek to own health facilities and provide their own services? Which services? Or will services be bought from competing public and private providers?

Remuneration Arrangements

How will providers be reimbursed—fee for service, capitation, salary, global budgets, per diem, per case? How will service contracts be specified - cost and volume? Will beneficiaries be permitted to make claims?

Phasing of the Programme

Will there be a gradual or aggressive approach to implementation? Which services, providers and population groups will be covered in the various phases?

There is general agreement in the literature that given the various objectives and elements, the final design of the SHI programme will reflect a mix of financial, social, political and health considerations (Normand and Weber, 1994). There is also agreement that the final design cannot be "fixed in stone" but must constantly be monitored, evaluated and re-engineered to ensure that the programme objectives are being met and that consumers and providers are satisfied.

Performance of SHI Systems

Most writers agree that the first SHI plan in modern times can be traced to Germany in 1883 (Roemer, 1993; Ron, 1990; Glaser, 1991). Since then, SHI has spread rather slowly in the first few decades after 1883 but more rapidly after the First World War to both IC's and DC's. As indicated in Table 8.1 (taken from Roemer, 1993) it is now the most common mechanism for financing personal health services.

In seeking to assess the performance of SHI systems across countries, there are two (2) observations which can be made:

- there is a fairly abundant literature on the experiences with SHI in IC's but not enough detailed studies on DC's. This is now being addressed (Ron et. al., 1990; Yang, 1990; La Forgia, 1993).

- discussion of the experiences are more meaningful in a comparative context which shows how other systems such as tax-based and private health insurance are coping with the financing of health services.

Table 8.2 (taken from Hsiao, 1990) summarises one attempt to assess the performance of the different financing systems in IC's. It uses the following criteria - universal coverage, equal access, cost control, efficient use of resources, equity in financing, consumer choice and innovation. Generally, it was found that social health insurance systems performed quite creditably on all criteria except equity in financing. It was generally "inferior" to health systems which relied on general taxes but "superior" to those relying on pluralistic and privatised modes of financing.

Mills (1983) has suggested a fairly precise set of criteria which will be used to assess the appropriateness and performance of health financing systems:- distribution of financial burden and access to benefits by different groups; quantity and quality of services being financed; efficiency of service provision; efficiency of administration and achievement of national goals. Several aspects and indicators of performance of SHI in IC's and DC's will be discussed under each criterion.

Sharing of Costs and Benefits

Equity in financing - This is defined in terms of "progressivity" i.e., those with the ability to pay more should contribute more in practice. Various writers (Wagstaff, 1992; Hoffmeyer and McCarthy, 1994; Kutzin and Barnum, 1994) assert that SHI systems in IC's and DC's are generally regressive when compared to systems dependent on general taxes. This is due to the establishment of limits on insurable earnings, tax deductible provisions for SHI pavments and provisions for " opting out" e.g. in Germany, Holland, Chile.

In several DC's e.g. South Korea (Yu and Anderson, 1992) and Egypt (Ron et. al., 1990) high copayments are required for insured services. These are more burdensome on those with lower incomes thus adding to the overall regressivity of SHI.

Table 8.1 - Countries Listed According to Social Insurance Coverage (as Percent of National Population) for Medical Care and GNP Per Capita, 1986

Coverage 90-100 percent		Coverage 25-89 percent		Coverage under 25 percent	
Country	GNP per capita	Country	GNP per capita	Country	GNP per capita
Switzerland	$17,808	Libya	$5,290	United States	$17,148
Iceland	16,444	Cyprus	4,195		
Luxembourg	15,744			Algeria	2,654
Norway	15,109	Taiwan	3,611		
Canada	14,124	Venezuela	2,922	Iraq	2,308
Sweden	13,734	Mexico	2,678	South Africa	2,077
Denmark	12,907	Korea, South	2,418	Iran	1,637
Japan	12,809	Argentina	2,373	Guatemala	1,292
Australia	12,454				
Finland	12,343	Panama	2,150	Columbia	1,290
		Uruguay	1,900	Peru	1,153
West	12,049	Brazil	1,809	Tunisia	1,121
Germany		Turkey	1,409	Ecuador	1,097
France	10,986	Chile	1,309	Paraguay	921
Austria	10,159			El Salvador	821
Netherlands	9,861	Philippines	590	Dominican	816
Italy	9,330	Bolivia	541	Republic	
		China	299	Honduras	752
Belgium	9,298			Egypt	749
Great Britain	9,009			Indonesia	491
East					
Germany	8,808			Pakistan	331
Soviet Union	8,442			Guinea	305
New Zealand	7,115			India	272
				Burma	191
Czechoslovakia	6,688				
Hungary	6,212				
Israel	6,181				
Spain	5,248				
Ireland	5,198				

Source: Roemer (1993).

TABLE 8.2 (Contd.) - Assessment of the Methods of Financing, Payment, and Delivery Organization in Developed Nations

Method of Financing	Universal Coverage	Equal Access	Cost Control	Efficient use of Resources	Equity in Financing	Consumer Choice	Innovation
General Tax							
Central government/direct provision (e.g. Great Britian)	Yes	High	Strong	Moderate	Progressive	Low	Low
Regional government/direct provision (e.g. Canada)	Yes	High	Strong	High	Progressive	High	Moderate
Local government/direct provision (e.g. Sweden)	Yes	Moderate	Strong	High		Moderate	Moderate
Social Insurance							
Government/direct provision (e.g. Spain)	Yes	High	Strong	Moderate	Mildly Regressive	Low	
Mandated insurance with global budget (e.g. Germany, Japan)	Yes	Moderate/-High	Strong	Moderate	Regressive	High	Moderate
Social Insurance							
Mandated insurance without global budget (e.g Korea)	Yes	Moderate	Weak	Low	Regressive	High	
			Strong	High	Progressive	High	Moderate
Pluralistic							
Universal provision by public hospitals with private insurance "opt-out" (e.g. Australia, Singapore)	Yes	Moderate	Weak	Low		High	
Free choice market competition (e.g. USA)	No	Low	Weak	Low	Regressive	High	High

Source: Hsiao (1990)

Equity in access - In IC's this is generally felt to be one of the successful outcomes of SHI. However, near universal coverage and equity in access in these countries do not always mean equity in utilisation. For example in France, there are noticeable disparities in utilisation among different social classes and between those living in rural as compared to urban, well-to-do areas (Rodwin and Sandier, 1993).

In DC's there are significant differences in the number of visits to health facilities by the insured and those who are not insured e.g. Brazil, Thailand, Chile as well as among those who are members of less well-endowed SHI agencies

e.g. South Korea, Argentina. The insured are normally the urban, formal sector workers and their families - thus a definite skewed pattern can be identified in terms of access to and utilisation of health services at all levels.

Quantity and Quality of Services

Mix of services covered - The package of services covered in most IC's is quite comprehensive. There are few exclusions e.g. in Holland and Belgium (Glaser, 1991) and France (Rodwin and Sandier, 1993).

In DC's SHI has led to considerable development and expansion in the range and volume of services provided. However, there has been a clear tendency to focus more on hospital-based curative services with preventive and promotive primary care being the responsibility of the Ministries of Health e.g. Costa Rica (La Forgia, 1993), Chile (Mesa-Lago, 1989); Brazil (Kutzin and Barnum, 1992) and Korea (Yang, 1993).

Quality of Services - If patient satisfaction and general health outcomes can be used as indicators of quality, IC's with SHI systems can be said to be "superior" to countries like the US which rely more on privately funded health services.

In DC's there are few systematic studies on quality of services. If general health outcomes (as judged by the standard health indicators) is used to measure quality it is quite indeterminate whether countries with SHI systems have performed better than those without.

Efficiency of Service Provision

Cost Containment - Compared to the USA, IC's with SHI systems have been more successful in containing cost and preventing unnecessary duplication of services (Glaser, 1991; OECD, 1992; Fuchs, 1993, Hoffmeyer and McCarthy, 1994). One of the major reasons for this seems to be the bargaining strength of the SHI agencies in negotiating reimbursement levels and in curtailing excessive high technology investment.

In DC's, cost control has not been one of the strong points of SHI systems. In fact, cost escalation occasioned by consumer and physician moral hazard seems to have been the norm e.g. Korea (Yang, 1990; Yu and Anderson,

1992), Brazil (Mesa-Lago, 1989; Kutzin and Barnum, 1992) Thailand (Singkaew, 1991), China (Kutzin and Barnum, 1994).

Impact of Payment Mechanism - In most IC's with SHI systems, negotiated fees and global budgets are used to reimburse providers. In addition, extra-billing is not normally permitted. This has been quite successful not just in containing costs but also in ensuring a certain level of efficiency in operations to stay in business. An exception is Japan where the drugs budget is generally unregulated leading to excessive prescription and cost escalation (Ikegami, 1992).

In DC's, fee for service especially for hospital and high technology services has led to significant cost escalation and excessive investment e.g. Korea (Kutzin and Barnum, 1994); China (Liu and Hsiao, 1995) and Brazil (Kutzin and Barnum, 1994).

Use of Gatekeepers and Referral Channels - There is much self-referral and direct access to specialist services in most IC's with SHI systems. Formal arrangements to be linked to or enlisted with a GP are not the norm—rather there is greater emphasis on free choice of physician (Glaser, 1991; Rodwin and Sandier, 1993). This has led to a much higher rate of discretionary surgery and other procedures than for example in the UK where there is a vibrant gatekeeper system (OECD, 1992; Hoffmeyer and McCarthy, 1994).

In DC's also there is little reliance on gatekeepers or on a referral system. As in IC's this has led to significantly higher rates of surgery and other diagnostic services than in countries without SHI systems e.g. Korea (Yu and Anderson, 1992); Brazil (Kutzin and Barnum, 1994).

It is difficult to say whether and by how much cost containment would have improved in these countries if a proper system of gatekeepers and referral was in place. From the evidence in the UK however one can only conjecture that this could have led to noticeable general savings in health expenditure.

Efficiency of Administration

Cost of Administration - In IC's this has been generally low in most countries i.e., less than 10% of the expenditure of the SHI funds/agencies (Glaser, 1991; Hoffmeyer and McCarthy, 1994). However there are exceptions and in France

and Germany some of the sickness funds are spending closer to 15% of their collections on administration. It is suggested that this has to do more with the relative size of the fund and the location of its membership than to administrative waste.

In DC's the cost of administration in SHI systems has generally tended to be higher than in IC's- some estimates put this closer to 20% (Mesa-Lago, 1989: Barnum and Kutzin, 1994; Yang, 1990). Some of the high percentage of administrative expenditure is due to the fact that SHI funds also own and operate several health facilities - many of these duplicate the services offered by Ministry of Health facilities especially in Latin America. In addition, economic difficulties especially in the 1980's have created havoc with labour markets thus leaving the funds in a critical position of reduced membership, reduced contributions and fairly constant overheads.

Viable Funds and Inter-fund Transfers - In IC's there is no single agency serving as the administrator of the SHI system. Rather, there are several competing and non-competing sickness funds. For example in Germany there are over 1,200 funds and in Japan about 400 (Glaser, 1991: Roemer, 1993; Hoffmeyer and McCarthy, 1994). Several of these funds are too small and uncompetitive - low economies of scale, small membership, high administrative cost - and are only kept in existence through interfund transfers at periodic intervals.

In Holland an attempt is being made to achieve more efficiency in the administration of the funds by encouraging direct competition with private insurers. This is a recent initiative and it is too early to determine whether this objective could be satisfactorily achieved.

In DC's, SHI systems are also managed by a number of regional, provincial and/or industry funds (except in smaller countries like Costa Rica where there is a single fund). In Korea there are more than 400 funds. In general, the level of administrative efficiency in these funds is sub-standard and subsidies from the State are sometimes required to bail them out (Mesa-Lago, 1989). Interfund transfers are not very common.

Achievement of Health Goals

Health Goals - Health goals are not always clearly indicated for some IC's. However, if the goals outlined by the OECD (1987) are taken as proxies -

income protection, macroeconomic efficiency, microeconomic efficiency, consumer choice and provider autonomy - it can generally be said that SHI have made a significant contribution towards meeting these goals. As discussed above not all these goals have been satisfactorily achieved and issues of cost containment, equity in access, microeconomic efficiency in the use of resources continue to test the innovativeness and ingenuity of policy-makers and health managers.

In DC's these goals still elude many countries with SHI systems. While there has been notable achievements in terms of the development of health services, general inequity and inefficiency are still the major issues confronting policy-makers.

Improved Health Status - In both IC's and DC's with and without SHI systems there has been significant improvements in health status (as measured by the standard health indicators) over the last few decades. It is difficult to say what proportion of the improvements in overall health status is due to the financing system. One can only suggest that improved access and better health security for significant segments of the population must have played a key role in attaining and sustaining these improvements.

Lessons From the Experience with SHI Systems

In IC's and DC's the experience with and performance of SHI systems have been quite varied. No system has remain unchanged over its existence and reforms and refinements have been quite frequent. From this mixed history of successes and failures, certain clear lessons have emerged for countries contemplating the introduction or reform of SHI systems. Mills' five-point criteria provide a useful basis for integrating these conclusions and suggestions coming from the various researchers.

Sharing the Costs and Benefits.

- SHI improves access to services for many persons but ease of access does not mean equity in utilisation. Significant differences will exist in the levels of utilisation by different groups with similar needs. These must be carefully researched, corrected and monitored.

- SHI systems continue to operate in favour of the urban, formal sector elite while leaving the rural and informal sector workers underserved. These must be targeted and appropriate health services and facilities be established to improve equity in the distribution of benefits.

- SHI systems which are subsidised by the state place an unfair burden on those who are non-members. Innovative ways have to be found to expand coverage of the population and to ensure that social solidarity and universal coverage are progressively and measurably achieved.

- Opting out runs counter to the principles of social solidarity and can rapidly lead to the establishment of a two-tiered health system. Persons should be required to remain in the system and purchase supplemental private insurance if they so wish.

Quantity and Quality of Services

- Legal entitlement to services must be translated into easy access to adequate, high-quality services. Otherwise, popular support for SHI will decline and the clamour for opting out and enhanced choice will increase.

- SHI systems cannot afford to ignore preventive and primary care services. Every effort should be made to have a seamless integrated health system to achieve economies of scope and synergistic benefits.

Efficiency of Service Provision

- Supply-side cost containment measures such as case based and capitation payments systems, utilisation reviews, use of gatekeepers, pre-admission reviews) are more effective in controlling costs than demand-side measures such as cost sharing, utilisation limits.

- A well-organised referral system is essential for ensuring appropriate levels of care and the efficient use of resources.

- Competition for providing services should be based on price and non-price factors. Even where the SHI agencies own and operate health facilities some competition with private providers can be encouraged to

lead to a general scaling up of the quality of services rather than a race to offer high technology services.

Efficiency of Administration

- Consolidation of small funds is necessary for economies of scale, adequate risk-pooling and overall viability. However this should not be achieved by creating excessive bureaucracies which lose the advantages of decentralised and local administration.

- Single collector and payer systems are more administratively efficient and have more bargaining strength than diverse agencies.

- The State has a major role to play in developing appropriate legislation, regulations and incentives and to provide ongoing information to stakeholders so that accountability of the SHI agencies can be constantly tested.

Health Goals

- Health goals and priorities must be clearly established. The objectives of the SHI must be consistent with these goals if health managers and SHI administrators are to work together and not frustrate each other and eventually the goals of the health system.

References

Abel-Smith, B. (1992). Health Insurance in Developing Countries: Lessons from experience. In *Health Policy and Planning 7(3).*

Arrow, K. (1963). Uncertainty and the Welfare Economics of Medical Care. In *AER 53(5).*

Bachman, M.O. (1994). Would NHI Improve Equity and Efficiency of Health Care in South Africa? Lessons from Asia and Latin America. In *South Africa Medical Journal 84(3).*

Borch, K.H. (1992). *The Economics of Insurance*. Elsevier Pubs.,Amsterdam.

Dionne, G. and Harrington, S. eds. (1992). *Foundations of Insurance Economics: Readings in Economics and Finance*. Kluver Acad. Pubs., Ger.

Ensor, T. (1993). Health System Reform in Former Socialist Countries of Europe. In *Journal of Health Planning and Mgt. 8(3).*

Evans, R.G. (1986). Finding the Levers, Finding the Courage: Lessons from Cost Containment in North America. In *JHPPL 11(4)* 585-615.

Fuchs, V. (1993). Chapter 14 "NHI Revisited". In *The Future of Health Policy* by V. Fuchs, HUP.

Glaser, W.A. (1991). *Health Insurance in Practice*. Jossey-Bass Pubs., San Francisco.

Griffin, C.C. (1990). *Health Sector Financing in Asia*. World Bank.

Hoffmeyer, U.K. and McCarthy, T.R. eds. (1994). *Financing Health Care*. Kluwer Academic Pubs., Dordrecht

Hsiao, W. (1990). *What Lessons can LDCs Learn from the Experiences of Developed Nations about a Comprehensive Health Financing Strategy*. Harvard University School of Public Health.

Ikegami, N. (1992). Japan: Maintaining Equity Through Regulated Fees. In *JHPPL 17(4).*

Kutzin, J. and Barnum, H. (1992). Institutional Features of Health Insurance Systems and Their Effects on Developing Country Health System. In *International Journal of Health Planing and Management 5* 51-72.

Kutzin, J. and Barnum, H. (1994). *Experience with Reform in the Financing of the Health Sector.* WHO.

La Forgia, G. et.al. (1993). *Health Insurance in practice: Fifteen Case Studies from Developing Countries.* HFS, MD.

Liu, X. and Hsiao, W. (1995). The Cost Escalation of Social Health Insurance Plans in China: Its Implications for Public Policy. In *SSM 41(8).*

Mehr, R.; Cammack, E. and Rose, T. (1985). *Principles of Insurance.* Irwin, Illinois.

Mesa-Lago, C. (1989). *Ascent to Bankruptcy: Financing Social Security in Latin America,* Univ. of Pittsburgh Press.

Mills, A. (1983). Economic Aspects of Health Insurance. In *The Economics of Health in Developing Countries,* K. Lee and A. Mills (eds.), OUP.

Navarro, V. (1989). Why Some Countries Have NHI, Others Have NHS and the US has neither. In *SSM 28(9).*

Norm and, C. and Weber, A. (1994). *Social Health Insurance: A Guidebook for Planning.* WHO.

OECD (1987). *Financing and Delivering Health Care: A Comparative Analysis of OECD Countries.* OECD.

OECD (1992). *The Reform of Health Care Systems: A Comparative Analysis of Seven (7) OECD* Countries. OECD.

Pauly, M.V. (1968). The Economics of Moral Hazard: A Comment. In *AER 58* 531-36.

Preker, A.S. et.al. (1996). *Trends in Health Status, Health Services and Health Financing: The Transition in Central and Eastern Europe.* World Bank Tech. Paper.

Rodwin, V.G. and Sander, S. (1993). Health Care Under French NHI. In *Health Affairs 12 (3).*

Roemer, M.I. (1993). Social Security for Health Care .In M.I. Roemer *National Health Systems of the World, Vol.II: The Issues, OUP.*

Ron, A.; Abel-Smith, B. and Tamburi, G. (1990). Health Insurance in Developing Countries: The Social Security Approach. ILO.

Sarjeant, F. and Carrin, G. (1995). *Towards a Framework for Health Insurance Development in Hai Phong, Vietnam.* MHDS#12, WHO.

Shaw, R.P.and Griffin, C.C. (1995). Financing Health Care in Sub-Saharan Africa through User Fees and Insurance.

Sheiman, I. (1994). Forming the System of Health Insurance in the Russian Federation. In *SSM 39(10).*

Singkaew, S. (1991). *Policy Options for Health Insurance in Thailand.* Unpub. Ph.D. Thesis, LSE.

Steinmo, S. and Watts, J. (1995). Its the Institutions Stupid! Why Comprehensive NHI Always Fails in America. In *JHPPL 20(2).*

Wagstaff, A. et.al. (1992). Equity in the Finance of Health Care: Some International Comparisons. In *Journal of Health Economics 11(4).*

Wilson, C. (1977). A Model of Insurance Markets with Complete Information. In *Journal of Economic Theory 16* 167-207.

WHO (1993). *Evaluation of Recent Changes in the Financing of Health Services.* WHO Technical Paper Series #829.

World Bank (1987). Financing Health Services in Developing Countries: An Agenda for Reform. World Bank Policy Study.

World Bank (1993). World Development Report ... Investing in Health. OUP.

Yang, B.M. (1990). Health Insurance in Korea: Opportunities and Challenges. In *Health Policy and Planning 6(2)* 119-29.

Yu, S.H. and Anderson, G.F. (1992). Achieving Universal Health Insurance in Korea: A Model for other Developing Countries? In *Health Planning* ***20,*** 289-99.

The Editorial Program of the Interamerican Conference on Social Security (CISS) is formed by different publications of the Studies Series, the Monographic Series, the Social Security Journal and the Newsletter. These are the means that the Conference is using to achieve one of its goals: to compile and disseminate social security's breakthroughs.

The *Studies Series* in which this publications is included will be formed by several books that show the development and current situation of Social Security in every member country in the Americas, and their publication is subject to the yearly program presented by the Permanent Interamerican Committee on Social Security (CPISS).

Interamerican Conference on Social Security
Secretariat General
Mexico City
2000