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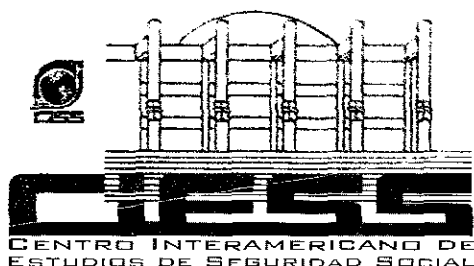
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AMENDMENTS TO THE SOCIAL SECURITY LAW

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Introduction

This document has the purpose of enhancing the implications of the latest amendment to the Social Security Law (SSL), both in the short and in the long term, in order to solve the structural problems observed in the Mexican Social Security Institute (IMSS), since the tendency of the increase in expenses is greater than that of the increase in income. This presents important challenges, mainly in the following four aspects:

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1. The personnel chapter that represents 50% of the expenses of the Institute. In actual terms, this expense tends to increase each year due to salary revisions and to the revisions of the Collective Labor Contract, as well as due to the need for new jobs to maintain the level of attention to beneficiaries.
2. The irreversible growth of medical expense for the insured, pensioners and beneficiaries, derived from the aging of population. This aging has incidence in a change in the epidemiological profile, which results in a notorious increment in the treatment of chronic-degenerative illnesses.
3. There is a deficit of medical and equipment infrastructure, as well as the periodical need for its modernization. In spite of the investment made in this respect, this has not been sufficient to compensate the deficit.
4. Finally, the most important challenge due to the high amount it implies, is the shortage of the reserve necessary to face the labor obligations of the employees working for the Institute.

To comply with its proposed objective, this document is made up of five chapters, which are briefly described below and latter on discussed with greater precision.

I. Antecedents

The Social Security Law, in force since July 1, 1997, whose main objective was to establish a new IMSS, totally free of non financed liabilities, reached the

objective mentioned only *partially*, because there were still to be covered the liabilities inherent to the Retirement and Pensions Regime of the employees working for the IMSS and to the medical expense of pensioners and their families corresponding to the law annulled.

II. Amendments to the Social Security Law - December 20, 2001

To the benefit of the employees: they establish a legal frame that contributes to allow the IMSS to progressively acquire reserves for the different fields of insurance it administers, as well for the compliance with its labor and contractual obligations, providing conditions for its professional and transparent administration.

To the benefit of the pensioners and retirees: they increase the unemployment and old age pensions and the lesser value widowhood pensions, and update all pensions according to the National Consumers Price Index.

To the benefit of enterprises and of employment: they establish better expeditious means for payment of workers and employers quotas, an increased legal and procedural certainty, and propitiate the reduction of administration and negotiation costs on the part of enterprises and of the Institute, by making available to the public modern technological media for affiliation and for the determination and collection of quotas.

To the benefit of society: they compel the strengthening of the rendering of accounts and strengthen also the

principles of budgetary discipline, productivity, austerity and transparency in the exercise of the expense.

To the benefit of the employees of the Institute: the constitution of a Fund for compliance with the Legal, Labor and Contractual Obligations of the Institute.

To the benefit of the Institute itself: the clear and precise definition of the autonomous fiscal organization nature it has had since 1944, and a better precision, transparency and safety in the administration of its technical and financial reserves.

III. Of the IMSS as an autonomous fiscal organization

The Institute will have negotiation and technical autonomy; to this effect, it will prepare its budget project and exercise the corresponding expenditure with strict respect to the criteria of discipline, productivity, saving, austerity, effectiveness, efficiency, budgetary deregulation and transparency, applying them in such manner that this will not affect the attention to beneficiaries, and will plan its expenditure in such manner that it will contribute to maintain its stability and financial equilibrium in a medium and long term horizon, according to the demographic and epidemiological tendencies of its beneficiary population.

IV. Of the constitution of reserves

This amendment marks a parting line in the history of the Institute, because for

the first time the chapter traditionally denominated "*Of the investment of reserves*" is structured as is pertinent for the largest insurance institution of the Nation.

V. Of the professionalization and development system

Confidential employees "A" who after the amendment are hired by the Mexican Social Security Institute, shall only be subject to the labor regime established in the Bylaws in the process of approval, and those that were already working for the Institute may opt for the benefits established by these Bylaws, or for the benefits that they are currently enjoying.

I. Antecedents

The Social Security Law, in force since July 1, 1997, whose main objective was to totally free the IMSS of non financed liabilities, shows the following results in its sixth fiscal period:

➤ Results

- Pensions in the course of payment, the new pensions granted under the previous regime and the payment of complements to minimum and guaranteed pensions, are covered with contributions of the Federal Government.
- The amounts insured by pensions derived from the Occupational Risks Insurance and from the Disability and Life Insurance, are paid by the IMSS to Insurance Institutions.

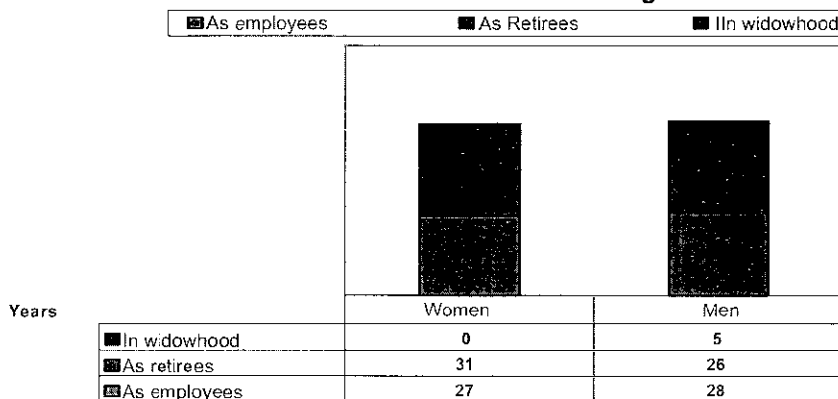
- Pensions or retirements programmed by the Retirement, Unemployment and Old Age Insurance shall be financed with the balance of the corresponding individual accounts.

In this manner, the Institute became *free of liabilities* with respect to pensions granted to the insured and their beneficiaries, which represents a solid advancement by guaranteeing in a permanent manner the financing of the pensions derived from the new Law.

However, the principal objective of the amendments –which was to establish a new IMSS totally free of non financed liabilities– was reached only *partially*, because there were left to be covered the liabilities corresponding to the:

- *Retirement and Pensions Regime of the employees working for the IMSS.*
- *Medical expense of the pensioners and their families corresponding to the law annulled.*

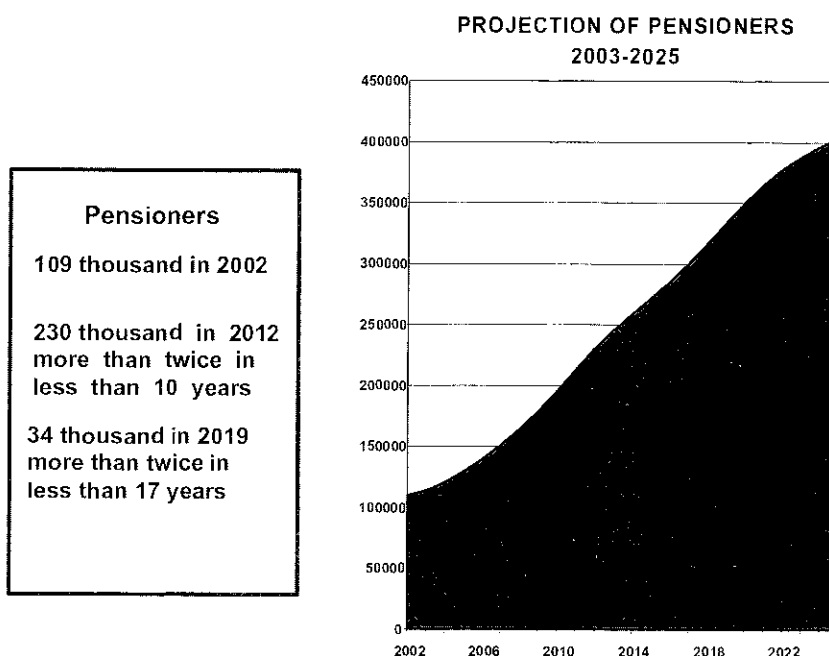
Retirements and Pensions Regime



As an average, women retire at 52 years of age and 27 years of service, with an expectation of Permanence as pensioners of 31 years.

As an average, men retire at 53 years of age and 28 years of service, with an expectation of permanence As pensioners of 26 years + 5 years for their widows.

RETIREMENTS AND PENSIONS REGIME



It should be pointed out that the commitments of a labor nature of the Institute amount to more than 76 per cent of total income, and therefore, if the pertinent actions to reduce them are not carried out, they will continue to increase day after day, until totally exhausting the availabilities of the Institution in the near future; the above mentioned percentage is composed of the following chapters:

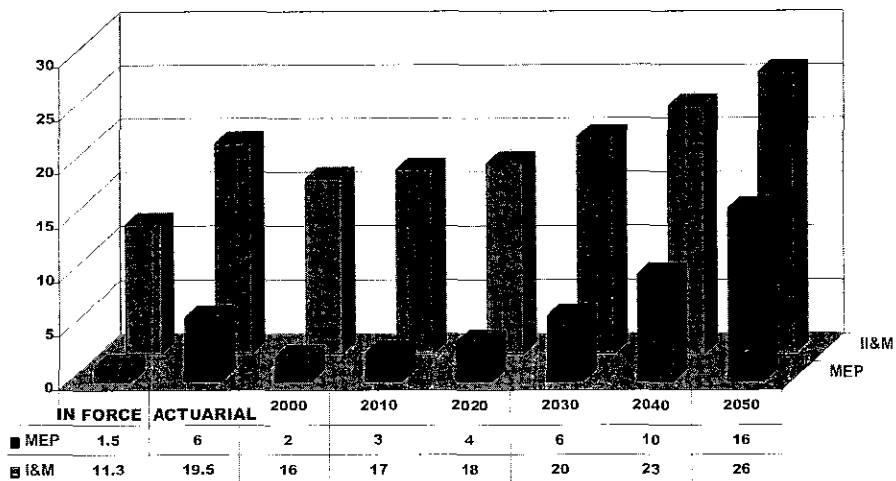
- Personnel Services 50.7%
- Retirements and Pensions 6.5%
- Labor and Financial Cost 18.8%

Summing up, the institution has serious structural problems, because the trend of the increase in expenses is higher than the trend of increase in income, which represents important challenges, mainly in the following four aspects:

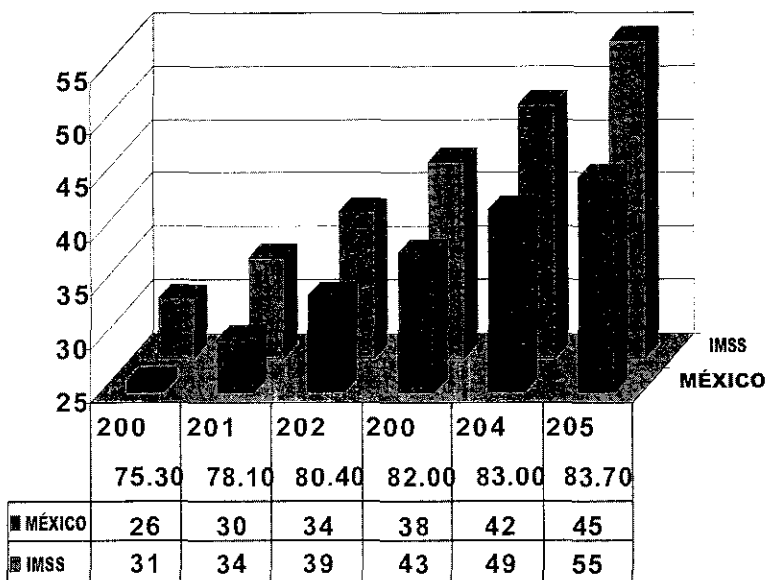
1. The chapter of personnel that represents 50.7% of the expense of the Institute, because in actual terms this expense tends to increase year after year with the salary revisions and the revisions of the Collective Labor Contract, as well as due to the need for new jobs to maintain the level of attention to beneficiaries.
2. The irreversible growth of medical expenses of the insured, pensioners and beneficiaries, derived from the aging of population. This aging has incidence on a change in the epidemiological profile that results in a notorious increment in the treatment of chronic-degenerative illnesses.
3. There is a deficit of medical and equipment infrastructure, as well as the periodical need for its modernization. In spite of the investment made in this respect, it has not been sufficient to compensate the deficit.

**MEDICAL EXPENSE OF PENSIONERS
ILLNESSES AND MATERNITY**

QUOTA IN FORCE, ACTUARIAL AND EXPENSE
IN % OF SALARIES



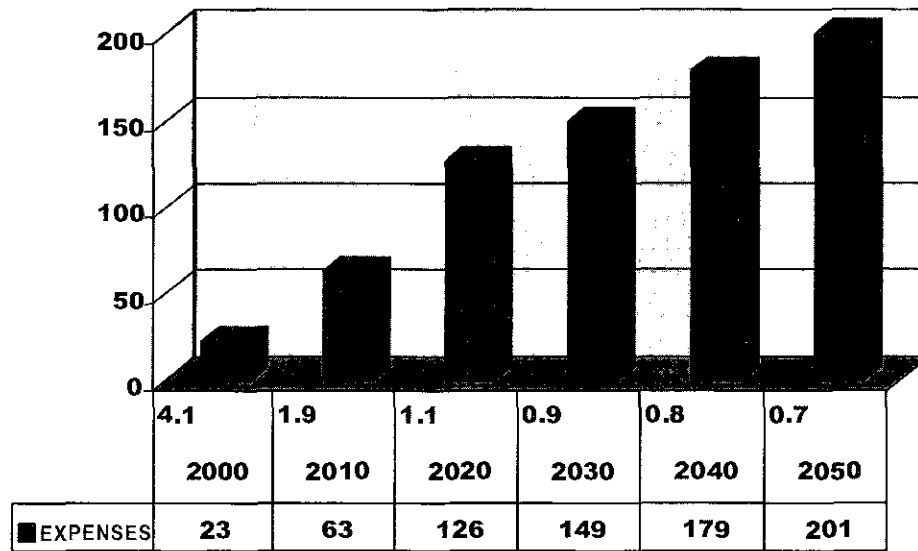
**MEXICAN POPULATION AND
ASSIGNED TO A FAMILY DOCTOR
AVERAGE AGE**



4. Finally, the most important challenge, due to the high amount it implies, is the shortage of the reserve necessary to face the labor obligations of the employees working for the Institute.

To face these challenges, the latest amendments to the Social Security Law were made, by establishing the basis that will permit covering these liabilities in the long term, together with other not less important adaptations.

NUMBER OF EMPLOYEES FOR EACH PENSIONER AND EXPENSES IN PERCENTAGE OF THE EMPLOYEES PAYROLL



II. Amendments to the Social Security Law - December 20, 2001

This amendment marks a *parting line* in the history of the Institute, because for the first time the chapter traditionally denominated “*Of the investment of reserves*” is structured as is pertinent for to the largest insurance institution of the Nation, the contents of which will be shown in detail later on.

In congruence with the above, Chapter VII of Title Fourth of the Law, which in the text in force is shown as “Of the Investment of Reserves”, was amended to be now denominated “OF THE CONSTITUTION OF RESERVES” and integrated with four new sections, which are: “Section First, Generalities”,

“Section Second, Of the Insurance Reserves”, “Section Third, Of the Annual Administration and Constitution of Reserves Program”, and “Section Fourth, Of the Investment of Reserves and of their Use for the Operation”; corresponding to articles 278 through 286 of the numbers in force and adding to the Law articles 286A through 286E.

A brief outline of the most relevant aspects of the amendments is included below:

- *To the benefit of the employees:*
 - *They establish a legal frame that contributes to allow the IMSS to progressively acquire reserves for the different fields of insurance it administers, as well as for the*

¹ IMSS. 2001 Report, Ninetieth Regular General Assembly, Mexico City, April 29, 2002.

compliance with its labor and contractual obligations, by providing conditions for its professional and transparent administration;

- They provide mechanisms for the opportune access to the services of the Institute in any part of the country, by setting the bases for the issuance of a sole identification document that, added to an updated data base, will permit in the future an agile certification of the duration of rights;
- They set the bases to expedite medical care to beneficiaries with the creation, in the coming years, of the electronic clinical records;
- They set forth the possibility that children under the custody or patria potestas of a male employee may enjoy the nursery service;
- They consider the possibility that the period of coverage of medical services for employees who have lost their jobs be extended for the time determined by the Federal Government which, as applicable, will contribute with the necessary economic resources; and,
- They assume the possibility that, if necessary, it will be possible to take care of beneficiaries in other health and social security public institutions.

➤ *To the benefit of pensioners and retirees:*

- An increment of 10% was provided for all pensioners under the unemployment and old age regime; that is, 60 years of age or older;

- No pensioner under the unemployment or old age regime will receive a pension lower than the equivalent to one minimum salary of the Federal District;
- An increase from 90% to 100% of the original pension is provided for the widowhood pension with a level of up to 1.5 minimum salaries;
- All pensions are updated according to the National Consumers Price Index.
- The quality as pensioners is recognized for railroad employees retired before 1982.

➤ *To the benefit of enterprises and of employment:*

- Better expeditious means were established for payment of workers and employers quotas: terms of up to 48 months; deferral of payment for reliable employers with temporary cash flow problems, and simplification of negotiations before the IMSS, by the establishment of the bases necessary for the adoption of information technologies and new procedures for the performance of electronic and in-line transactions;
- Decrease of the minimum range of the percentage on which fines are calculated, from 70% to 40%;
- Increased legal and procedural certainty by determining the rights and the manner in which they are exercised in a specific chapter of the Social Security Law, thus eliminating any possible application of discretionary criteria in the fiscal authority of the public servants of the Institute;

- Proportionality and differentiation are established between administrative infringements and fiscal offense.
 - A reduction in administration and negotiation costs on the part of enterprises and of the Institute is propitiated, by making available to the public modern technological media for affiliation and for the determination and collection of quotas.
 - Expeditious means are provided for payment of the workers and employers quotas by electronic transfer, Internet site of the IMSS, bank sites and automatic debit to checking accounts, among others;
 - *More equitable quotas are established for the Occupational Risks Insurance for enterprises that accredit a decrease in their disasters and that have an industrial safety program authorized by the Labor and social Welfare Ministry (STPS); and*
 - An Indebtedness Regularization Program of a general nature was adopted, which concluded last February 19, benefiting more than 50 thousand employers registrations.
- *To the benefit of society:*
- The advantage of having an institution that will progressively strengthen its financial situation and that, therefore, will contribute to the macro-economic stability of the country;
 - The legal bases are set to allow the Institute to continue providing assistance to the population in situations of contingency or catastrophe;
 - Legal certainty is granted so that, even not being beneficiaries, the population may have access to the sporting, recreative and cultural facilities of the Institute;
 - *The amendments compel the strengthening of the rendering of accounts, by determining that the Institute must present every year to the Federal Executive Government and to the Congress of the Union, complete and detailed information on its financial situation, revealing with all transparency its liabilities and contingent obligations, permitting an annual updating with respect to the demographic and epidemiological dynamics, with the purpose of learning of possible difficulties, evaluating the alternatives for solution and having the basis for the taking of decisions on the part of the competent authorities and of the legislative representation.*
 - *Strengthening of the principles of budgetary discipline, productivity, austerity and transparency in the exercise of the expense. The Institute has the obligation to publish, for information of the entire society, among other aspects: the amounts of its reserves, investments and all its liabilities; personnel remunerations and fringe benefits regime, including the number of jobs and their cost; and*
 - *The commitment is established that the IMSS will present, as from this year, studies to the Federal Executive Government and to the Congress of the Union on the financial situation and actuarial perspective of the different insurances it administers.*
-

➤ *To the benefit of the employees of the Institute:*

- ❑ *The integration, in a clear manner and with legal certainty, of a Fund for the Compliance of the Legal, Labor and contractual Obligations of the Institute; and*
- ❑ Better conditions for the development of their work, by gradually strengthening collections, modernizing the administration and expediting the institutional operation.

➤ *To the benefit of the Institute itself:*

- ❑ Its strengthening as a tripartite and socially solidary public organization;
- ❑ The clear and precise definition of the nature of autonomous fiscal organization that it has had since 1944;
- ❑ Budgetary flexibility with improved rendering of accounts in its operation, increased response capacity and better conditions to comply with its obligations before beneficiaries and employers, by strengthening, among other measures, the authority of its Technical Council;
- ❑ *More macro-economic responsibility by establishing the obligation to constitute technical, financial and actuarial reserves to guarantee compliance with its future obligations and duties;*
- ❑ *Prohibition for the Institute to become indebted, and the obligation to constitute the fund corresponding to the retirements and pensions regime for each new job.*

- ❑ Improved conditions for the modernization of its administrative, clinical and human resources development processes; and
- ❑ *Increased precision, transparency and safety in the administration of its technical and financial reserves.*

III. Of the IMSS as an autonomous fiscal organization

The Institute, in its capacity as an autonomous fiscal organization, shall be subject to the regime established in this Law, exercising the authority that this Law confers it in an executive manner, with negotiation and technical autonomy, within the ambits regulated therein (Art. 270).

On the matter of collection and administration of the contributions that pursuant to this Law correspond to the Institute, it will collect, administer and, as applicable, determine and liquidate the quotas corresponding to the insurances established in this Law, with all the authority conferred to fiscal authorities, which shall be exercised in an executive manner by the Institute, without the participation of any other fiscal authority (Art. 271).

The Institute shall prepare its budget project and shall exercise the corresponding expense, with strict respect to the criteria of discipline, productivity, saving, austerity, effectiveness, efficiency, budgetary deregulation and transparency and shall apply them in such manner that it will not affect the attention to its beneficiaries (Art. 272).

The Institute shall plan its expense in such manner as to contribute to maintain its financial stability and equilibrium in a medium and long term horizon, according to the demographic and epidemiological trends of its beneficiary population.

The quotas and contributions that according to the provisions of this Law must be paid by the Federal Government to the Institute, shall be stated in an express manner, indicating their specific destination, in an individual chapter of the corresponding decree of the Expense Budget of the Federation to be approved annually, making reference to the total expense foreseen to be exercised by the Institute itself and setting forth, as applicable, the rules for their control and follow up.

The Institute shall present to the Federal Executive Government, through the Finance and Public Credit Ministry and to the Congress of the Union, no later than June 30 of each year, a report certified by an external auditor that will include, at least, the following elements (Art. 273):

- I. *The financial situation of each one of the insurances offered by the Institute, and an actuarial report of its reserves, furnishing elements of judgment to evaluate if the corresponding premiums are sufficient to cover the current and future expenses of the benefits derived from each insurance;*
- II. *The possible risks, contingencies and liabilities involved in each insurance, and the financial capacity of the Institute to respond to them considering its income and the reserves available;*

III. Estimates of the possible modifications to the workers and employers quotas and to the quotas and contributions of the Federal Government for each insurance, as applicable, that may be foreseen, to maintain the financial viability of the Institute, and estimates of the dates on which said modifications may be required; and

IV. The situation of its total labor liabilities and liabilities of any other kind that may tie up its expense for more than one fiscal period.

For the above purposes, the Institute shall inform on the demographic trends of its beneficiary population, including modifications in life expectations, trends in the epidemiological transition and changes in the composition of gender of the labor force, among other factors.

The estimate of risks, in turn, will take into consideration factors derived from the economic cycle, from the evolution of the cost of treatments and medicines, labor costs and macro-economic situation, as well as from any other factor that will affect the capacity of the Institute to comply with its commitments.

In all cases, the estimate on risks and labor liabilities and of any other type of risks, shall be made with strict adherence to the accounting principles generally accepted by the accounting profession organized in Mexico.

The report will also contain information on the current conditions of the facilities and equipment of the Institute, mainly those used for medical care, to be able to offer a satisfactory attention to its beneficiaries.

No later than forty five calendar days before, according to the provisions of the Political Constitution of the United States of Mexico, the Federal Government sends to the Congress of the Union the initiative of the Income Law and the Project of the Expense Budget of the Federation, the Director General will propose to the Technical Council the preliminary income and expense project of the Institute, that must include operating expense and cash flow, taking into consideration the economic and budgetary policy criteria of the Federal Government, as well as the evolution of the income of the latter and the control of the expense (Art. 274).

The preliminary budget project must contain a report of the Directorate General that will include, at least, the following information (Art. 275):

- I. The analysis of the impact that the proposed budget will have for the Institute in a medium term horizon;*
- II. The budget assigned for the different programs, indicating priorities, objectives, goals and units responsible for its exercise, as well as its estimated evaluation for the different programs and the evaluation mechanisms and indicators for each program;*
- III. The express indication of the programs which, due to their nature and characteristics, must cover more than one annual budget period, subject, for the purposes of execution and payment, to the budgetary availability of subsequent years;*
- IV. Total income and cash flow, expressed as accrued from:*

- a. Workers and employers quotas;*
- b. Quotas and contributions of the Federal Government, and*
- c. Financial income of reserves and any other;*

V. Total expense and expense per chapter, expressed as accrued and as cash flow;

VI. Operating surplus;

VII. Cash flow surplus before and after the creation, increment or decrease of the Fund for the Compliance of Labor Obligations of a Legal and Contractual Nature, provided for in Article 286K;

VIII. Amounts proposed to increment, decrease or, as applicable, reconstitute the Financial and Actuarial Reserves and the General Financial and Actuarial Reserve referred to in sections III and IV of article 280 of this Law for each insurance and the Fund for Compliance of Labor Obligations of a Legal and Contractual Nature, as well as the support of financial investment that this Fund will receive;

IX. Total income and expense per insurance, expressed as accrued;

X. Total jobs to be covered, including permanent and temporary, as well as the hiring of professional services on the basis of fees;

XI. Total labor liabilities, detailing legal and contractual obligations, and the effect on these liabilities of the creation of new jobs in the fiscal period and within a period of twenty eight years;

XII. Physical Investment Program, indicating the main construction work and equipment. The Program must be specified for each insurance and shall include the analysis of the liabilities and operating expense of all types generated by the investment;

XIII. Budget of the central administration areas of the Institute, and

XIV. Other information considered convenient by the Technical Council.

The preliminary budget project approved by the Technical Council (Art. 276) will be sent to the Finance and Public credit Ministry no later than twenty five calendar days before, according to the provisions of the Political Constitution of the United States of Mexico, the Federal Government sends to the Congress of the Union the initiative of the Income Law and the Expense Budget Project of the Federation, with the purpose that the Ministry may analyze them and, if applicable, modify and approve the amounts referred to in sections IV, paragraph b) and VIII of article 275 of this Law.

To this effect, said Ministry shall take into consideration the report referred to in article 273 of the Law.

After these amounts have been approved, the Institute shall make the corresponding modifications to the effect that it may be sent in due time to the Ministry so that the latter may include it in the Initiative of the Income Law and in the Expense Budget Project of the Federation to be submitted to the approval of the Congress of the Union.

The Chamber of Deputies, when approving the Expense Budget Project of the Federation, shall take into consideration the report to which articles 273 and 274 of this Law refer.

The Technical Council and the Director General shall be responsible, within the ambit of their respective competences, to make sure that the Institute will comply with that which has been approved by the Congress of the Union.

The Institute shall exercise its budget evaluating the income received and the expense incurred in three month periods, for the purpose of verifying its development according to the budget (Art. 277).

When, in anyone of the three month periods of the year, the income obtained is higher than forecast, or the expense is lower than planned and there is a reasonable expectation based, in the opinion of the Technical Council, on the fact that the surplus generated in that period will have a net positive effect at the close of the annual period, and the three month goal of increment or reconstitution of the reserves and funds has been met in the terms of article 276 of this Law, the Institute may use them to apply them in the following three month period to the strengthening of its Operating Reserve for Contingencies and Financing, with the express agreement of the Technical Council.

In the event that, in the rest of the period it were expected that the resources considered as surplus in any previous three month period will be required to finance the operation of the Institute according to the approved budget, or that it is foreseen that it will not be possible

to comply with the reserves and funds goals set forth in the Expense Budget of the Federation, in accordance with the provisions of article 276 of this Law, the Technical Council will proceed to generate adjustments for expense reduction in the less necessary items, searching at all times not to endanger the adequate rendering of the services of the Institute (Art. 277A).

If the above mentioned adjustments for reduction of expenses were not sufficient, the Institute may use the Operating Reserve for Contingencies and Financing mentioned in article 280 of this Law, with the prior authorization of the Technical Council, informing the Federal Government of such adjustments through the Finance and Public Credit Ministry.

If, having used the Reserve indicated in the preceding paragraph, the adjustment to the expense budget necessary to comply with the reserves and funds goals established should affect sensibly the operating programs of the Institute, the latter may, with the prior authorization of the Federal Government, through the Finance and Public Credit Ministry, decrease the amounts in the reserves or funds to be increased.

The Secretariat of the Controllershship and Administrative Development shall watch the strict and timely compliance with this provision.

The Institute is not authorized to incur in financial liabilities to pay for the fringe benefits corresponding to the different insurances established by this Law (Art. 277B).

To defray its operation, the Institute may only incur in liabilities derived from non

revolving letters of credit or exchange coverage at terms shorter than one year destined to liquidate commitments with suppliers of components, without detriment to similar commitments with the latter, previously authorized by the Finance and Public Credit Ministry.

The Finance and Public Credit Ministry will authorize the maximum annual amount for the hiring of operations to which the preceding paragraph refers. To this effect, the Institute will send to the Congress of the Union and to the Federal Executive Government, through the above mentioned Dependency, in the month of January of each year, a report of the characteristics, terms and conditions in which said financial operations will be carried out.

The Institute will not have the obligation to concentrate its income in the Treasury of the Federation, with the exception of the surplus of subsidies and transfers from social solidarity programs and other programs financed directly by the Federal Government (Art. 277C).

If, at the end of the fiscal period, there should be a balance resulting from income in excess of the budget, the Institute will transfer this balance to the Operating Reserve for Contingencies and Financing provided for in article 280, section II of this Law, which, in exceptional cases, may be destined to its priority investment programs of subsequent fiscal periods.

The Technical Council, subject to budgetary provisions, will approve the salaries and fringe benefits of confidential employees referred to in article 256 of this Law, and the hiring of outside professional services on the basis

of fees, that are strictly necessary, according to the bases of mandatory observance issued by the Council itself (Art. 277D).

The salaries referred to in the preceding paragraph are determined taking into consideration the salary scales issued by the Finance and Public Credit Ministry for the dependencies and entities of the federal public sector, and the conditions prevailing in the market, according to a job evaluation system. The adjustments may be congruent with the guidelines observed for this purpose by the Federal Government, to which effect the Institute shall request the opinion of the Finance and Public Credit Ministry.

The Director General of the Institute may not receive earnings higher than those of a Cabinet Minister in the Centralized Federal Public Administration.

The Technical Council may only create jobs subject to productivity, efficiency and quality of service criteria, as well as subject to an increase in collections, provided it has available the resources approved in the respective budget for the creation of said jobs, and the resources that are indispensable to cover the cost of their repercussion, incorporating the annual cost of the future compliance with the labor obligations of a legal or contractual nature, including the allocations accrued to the corresponding Fund.

Particularly, an attempt will be made to observe the provisions relative to the amounts that, according to the contents of section VIII of article 276 of this Law, must be taken into consideration for the purposes of increment, decrease or, if applicable, reconstitution of the Fund to

which article 286K of this same Law refers.

The Institute has the obligation to publish in the *Official Gazette of the Federation*, no later than on June 30 of the corresponding fiscal period, the analytical report of all jobs and positions, including temporary, substitute, resident and similar jobs; the salaries, fringe benefits and incentives of all types of its public servants, grouped by level, degree and group of command, and the changes authorized to its organizational structure by the Technical Council, as well as the number, characteristics and total remunerations of the hiring of outside professional services on the basis of fees.

Without detriment to the provisions of the Federal Budget, Accounting and Public Expense Law, the income and expense of each insurance shall be recorded separately in the books of account (Art. 277E).

Common indirect expense shall be subject to the rules of a general nature for the distribution of costs, to the accounts catalogue and to the Accounting and Exercise of the Expense manual to be issued to this effect by the Technical Council at the proposal of the Director General, who must obtain the prior opinion of the Finance and Public Credit Ministry.

The accounts catalogue and the Accounting and Exercise of the Expense manual must have as a basis the equivalent catalogues and manual established to this effect by the competent authorities for the entities of the federal public administration, adapting them to the characteristics and needs of the Institute.

The resources of each field of insurance to which this Law refers, may only be used to cover the fringe benefits and payment of benefits and constitution of reserves corresponding to each one of them.

IV. Of the constitution of reserves

> *Generalities*

The Institute, to guarantee the due and timely compliance with its obligations derived from the payment of benefits and the rendering of services relative to the insurances established in this Law, shall constitute and record in its books of account, by field of insurance, the provision and the financial support of the corresponding reserves (Art. 278).

The resources relative to these reserves do not constitute part of the patrimony of the Institute and they may only be used to comply with the purposes provided for in this Law and to guarantee the long term financial viability.

The reserves must be recorded as a provision at the time of their constitution, and the contributions for their increment or reconstitution must be made every three months or annually, as applicable, and must be established definitely at the close of each exercise (Art. 279).

The Institute shall constitute the following reserves (Art. 280):

- I. Operating Reserves;
- II. Operating Reserves for Contingencies and Financing;
- III. Financial and Actuarial Reserves, and
- IV. General Financial and Actuarial Reserve.

The Operating Reserves and the Operating Reserve for Contingencies and Financing shall be constituted within one hundred and eighty days after the enforcement of the amendments, respecting the distribution of assets per insurance determined on the same date (Trans. XIII).

CONSTITUTION OF RESERVES

OPERATING RESERVES
Income is received to finance expenses and constitution of reserves.
FINANCIAL AND ACTUARIAL RESERVES
Constituted every three months, taking into account the <u>financial and actuarial report</u> .
OPERATING RESERVE FOR CONTINGIES AND FINANCING
Finances operative reserves and will amount to up to 60 days of the total average income of the previous year.
FINANCIAL AND ACTUARIAL GENERAL RESERVE
Covers fluctuations due to catastrophes, economic cycle, lawsuits and investments and is constituted with an annual contribution to be estimated in the <u>financial and actuarial report</u> .
FUND FOR THE COMPLIANCE WITH LABOR OBLIGATIONS

The provisions related to the Financial and Actuarial Reserves and the General Financial and Actuarial Reserve shall become effective after the enforcement of the *regulations* provided for to this effect. (Trans. XVII).

➤ *Of the insurances reserves*

An operating reserve shall be established for each one of the following insurances and coverage (Art. 281):

- Illnesses and Maternity;
- Medical Expense for Pensioners;
- Disability and Life;
- Occupational Risks;
- Nurseries and Social Benefits;
- Health Insurance for the Family, and
- Other insurances or coverage that, as applicable, may be established on the basis of this Law.

The Operating Reserves will receive the entirety of the income from workers and employers quotas and federal contributions, as well as from the quotas and contributions of voluntary insurance and other insurance to the established, except in the case of employers who operate permanently or sporadically in the construction activity, which shall cover the workers and employers quotas even in the event that it might not be possible to determine the worker or workers to which they should be applied; in this latter case, the corresponding amount will be destined to the General Financial and Actuarial Reserve,

independently of the fact that those workers who accredit their rights may be granted the deferred fringe benefits to which they are entitled.

Within one hundred and eighty days following the enforcement of the amendments, the Mexican Social Security Institute will make transfer of financial resources of the Occupational Risks Insurance to the Illnesses and Maternity Insurance in the amount of four thousand five hundred and ninety four million pesos, to the Disability and Life Insurance in the amount of two thousand million pesos, and to the Health Insurance for the Family in the amount of one thousand million pesos (Trans. XII).

Within the same period, transfers of financial resources will be made from all insurances up to the equivalent of five thousand million pesos to the Operating Reserve for Contingencies and Financing. These transfers will affect the assets and the patrimony in each case. The terms and conditions of the transfers made pursuant to this article shall be informed by the Directorate General to the Federal Government, through the Finance and Public Credit Ministry, and to the Congress of the Union, during the month after that in which they were made.

For only one occasion, as a transition towards the regime established in the amendments, the Mexican Social Security Institute may use the reserves of the insurances and the reserve for the retirees and pensioners regime up to seven thousand million pesos, to finance the operation reserves of the insurances up to a period of one hundred and twenty days, beginning as from the enforcement of this Decree. In this case, the resources

must be refunded to the corresponding reserves, including the financial interest accrued.

These reserves may only be used to face the payment of fringe benefits, administrative expense and constitution of Financial and Actuarial Reserves of the insurance and coverage to which they correspond, and for the corresponding contribution for the constitution of the Operation Reserves for Contingencies and Financing and General Financial and Actuarial Reserve.

In the case of the retirement, old age unemployment and old age insurance (Art. 282), the employers and the Federal Government, in the portion corresponding to each one of them, shall have the obligation to pay to the Institute the amount of the workers and employers quotas and the government contribution for the retirement, old age unemployment and old age insurance. These quotas will be received and deposited in the respective sub-accounts of the individual account of each worker, in the terms provided for by the Law for the Coordination of Retirement Savings Systems.

The Operating Reserve for Contingencies and Financing, shall be constituted, incremented or reconstituted until it represents sixty days of global average income of the previous fiscal year of the Institute, with the objective of providing stability and certainty in the daily operation of the Institute itself and of expediting the short term planning of the operations of the different insurances established in this Law (Art. 283).

It will be possible to allocate to this Reserve, in addition to ordinary income, the

resources that the Institute may obtain in an extraordinary manner, in which case it may exceed the limit set forth in the preceding paragraph up to the total of these extraordinary allocations.

The Institute may use, with the prior authorization of the Technical Council, the Operating Reserve for Contingencies and Financing to finance the Operating Reserves, up to an amount equivalent to ninety days of average income of the previous year of the insurance or coverage requiring the financing, and these resources must be refunded with the corresponding financial costs for the use thereof, in the terms of the regulations referred to in article 286 of this Law, within a period no longer than three years. The Institute will notify this situation to the Federal Government through the Finance and Public Credit Ministry.

The Financial and Actuarial Reserves will be constituted for each one of the insurances and coverage through a three month contribution calculated on the income of said insurances and coverage, taking into consideration the estimates of long term financial sustainability contained in the *financial and actuarial report* (Art. 284).

Each one of these reserves may be divided and handled according to the nature of the risks affecting each insurance and coverage. This separation will seek the best equilibrium between the sources and characteristics of the risk and the resources necessary for its financing.

The General Financial and Actuarial Reserve must be constituted, incremented or reconstituted through an annual contribution to be estimated in

the *financial and actuarial report* to face important catastrophic effects or variations of a financial nature in the income, or drastic increments in expenses derived from severe and long lasting epidemiological or economic problems that may provoke insufficiency of anyone of the financial and actuarial reserves (Art. 285).

All the real estate destined to the rendering of services directly derived from the insurances to which Titles Second and Third of this Law refer, shall be allocated to the General Financial and Actuarial Reserve and, therefore, shall be considered as destined to the public service of a national nature of the Social Security, pursuant to article 4 of the same Law, and shall have the nature of estate under the public ownership of the Federation.

The Institute may use the Financial and Actuarial Reserves of each insurance and coverage only to cover the needs corresponding to each one of them, with the prior agreement of the Technical Council at the proposal of the Director General, in the terms of the Regulations mentioned in the preceding paragraph, and only to face drops in income or increments in expenses derived from economic problems with a duration longer than one year, and to face fluctuations in the degree of disasters higher than those estimated in the *financial and actuarial report* or for the payment for future benefits for which the corresponding provision had been made (Art. 286A).

CONSTITUTION OF RESERVES

Millions of 2003 pesos

INSURANCES	OPERATING RESERVE (OR)	FINANCIAL AND ACTUARIAL RESERVES (FAR)	FUND FOR COMPLIANCE WITH LEGAL OR CONTRACTUAL LABOR OBLIGATIONS (FCLCLO)
OCCUPATIONAL RISKS	5,517	4,333	8,047
ILLNESSES OR MATERNITY	559		13,646
MEDICAL EXPENSE FOR PENSIONERS		268	
I DISABILITY AND LIFE	5,189	10,163	1,428
NURSERIES AND SOCIAL BENEFITS	-356		1,954
OPERATING RESERVE FOR CONTINGENCIES AND FINANCING (OPCF)	2,415		
GENERAL FINANCIAL AND ACTUARIAL RESERVE (GFAR)		587	
TOTAL	13,324	15,351	25,075

➤ *Of the Annual Administration and Constitution of Reserves Program*

At the proposal of the Director General, on the basis of the budget project for the following fiscal period and of the *financial and actuarial studies* presented each year to the General Assembly, the Technical Council must approve annually and prior to the start of the fiscal period, an Administration and Constitution of Reserves Program, which it will confirm or adapt it as necessary after learning the definite expense budget of the Institute (Art. 286B).

This program will contain as a minimum the following elements:

- I. Report on the total financial resources in the hands of the Institute, separating them by type of reserve and insurance according to the provisions of article 280 of this Law;
- II. Total cash income and expense projections for the following fiscal period;
- III. The three month and annual amounts that will be used to increment or reconstitute each one of the reserves in the following fiscal period, a projection of the rates of interest that said reserves will generate and values of these reserves expected at the end of the period, and
- IV. The annual resources that three months are expected to be allocated to the Operating Reserves for the following fiscal period.

The Technical Council, at the reasoned proposal of the Directorate General, may modify at any time the Administration

and Constitution of Reserves Program, with the exception of the amounts of increment of the Financial and Actuarial Reserves and of the General Financial and Actuarial Reserve committed for the period, when the income and expense flows throughout the period so require. The proposal of the Director General must describe the impact that this modification will have in the medium and long term, observing the provisions of the second paragraph of article 278 of this Law.

➤ *Of the Investment of Reserves and their Use for the Operation*

The Institute must have an administrative unit that, in a specialized manner, will be in charge of the investment of the resources of the Institute and of the mechanisms to be used to this effect, under prudence, safety, return on investment, liquidity, risk diversification and transparency criteria, and with respect to the healthy practices and uses of the national financial medium, seeking to reveal all information in its entirety (Art. 286C).

This administrative unit must have a professional and operating infrastructure that will permit a flexible, transparent and efficient process to operate in a competitive manner in the financial market.

Additionally, the Technical Council will establish the means of information to the public in general, so that in a periodical, timely and accessible manner, the composition and financial situation of the investments of the Institute may be made known. This information must be sent every three months to the Finance and

Public Credit Ministry, to the Banco de Mexico and to the Congress of the Union.

The Operating Reserves and the Operating Reserve for Contingencies and Financing, must be invested in securities issued or guaranteed by the Federal Government, in high quality credit securities according to classifiers of international prestige, or in sight and term deposits depending on the needs for cash, at credit institutions and investment funds, for the purpose of having available in due time the amounts necessary to face the obligations for the fiscal period (Art. 286D).

The investment of the Financial and Actuarial Reserves and of the General Financial and Actuarial Reserve,

provided for in this Chapter, may only be made in the securities, credit titles or other rights to be determined according to the Regulations to be issued by the Federal Government to that effect, which will also regulate the percentages, terms, amounts, maximum investment limits and institutions, and other issuers or depositories, and the other characteristics of the administration of the investment that the Institute may carry out, seeking always the best safety, return on investment and liquidity conditions, as well as the diversification of possible risks in terms of the greatest objectivity, prudence and transparency.

The interests or yield generated by each reserve shall be applied exclusively to the reserve that generates them.

CONSTITUTION OF RESERVES

Millions of 2003 pesos

INSURANCES	ACCOUNTING RESERVE	ACTUARIAL RESERVE	ACCOUNTING /ACTUARIAL RESERVE
OCCUPATIONAL RISKS	20,312	27,891	73%
ILLNESSES AND MATERNITY	14,205	343,279	4%
MEDICAL EXPENSE FOR PENSIONERS	268	429,099	0%
DISABILITY AND LIFE	17,367	28,964	60%
NURSERIES AND SOCIAL BENEFITS	1,598	20,382	8%
TOTAL	53,750	849,615	6%
INSURANCES	LEGAL QUOTA	ACTUARIAL QUOTA	LEGAL/ ACTUARIAL QUOTA
OCCUPATIONAL RISKS	1.90%	1.60%	119%
ILLNESSES AND MATERNITY	11.30%	19.50%	58%
MEDICAL EXPENSE FOR PENSIONERS	1.50%	6.10%	25%
DISABILITY AND LIFE	2.50%	2.65%	94%
NURSERIES AND SOCIAL BENEFITS	1.00%	1.15%	87%
TOTAL	18.20%	31.00%	59%

V. Of the professionalization and development system

The relations between the Institute and its employees are governed by the provisions of Chapter A of constitutional article 123, the Federal Labor Law, and in the case of employees classified as confidential employees "A" in the Collective Labor Contract (Article 256), by the provisions of the Interior Regulations of the Institute which, at the proposal of the Technical Council, the Federal Government will issue, and by the *Bylaws* approved to this effect by the Technical Council. (Art. 286I).

Confidential employees "A" who are hired by the Mexican Social Security Institute after the amendments, shall be only *subject to the labor regime* established in the *Bylaws* mentioned in the preceding paragraph, and those who were already working for the Institute, may opt for the benefits established in the *Bylaws* mentioned, or for the fringe benefits they have been enjoying at present (Trans. XV).

The Institute will establish its organic and occupational structure according to the needs of the service. Likewise, it will design and establish the compensation system that will serve as a base to determine the payment of remunerations, fringe benefits and incentives in favor of the confidential employees, with the purpose of maintaining their competitiveness in the labor market.

The specific regime, the processes and other characteristics of the Personnel Professionalization and Development System will be established in the *Bylaws* that are in the process of approval.

With the purpose of having a permanent body of professionals qualified and specialized in the activities and tasks corresponding to each one of them, as well as to guarantee the adequate rendering and improving of services to the benefit of beneficiaries and of the society in general, the Institute must establish the policies and carry out the necessary actions to implement a system for the professionalization and development of confidential employees to which the preceding article refers (Art. 286G).

This system will cover the recruiting, selection, hiring, compensation and development of personnel processes, including training, evaluation of their performance, promotion and dismissal.

The personnel to which this Chapter refers, may be subject to incentives on the basis of performance under the terms authorized by the Technical Council, which will be subject to the limits established annually in the Expense Budget of the Federation.

The appointments of personnel to which this Chapter refers, corresponding to the two hierarchical levels below the Director General and those that represent the Institute in the territorial circumscription established in the respective regulations, must be conferred to persons who meet the following requisites (Art. 286H):

- I. Be of recognized honorability and moral quality;
- II. Cover the profile necessary to hold the position, and
- III. Having three years of professional or technical experience in matters

related to the position for which they were proposed, or else, having performed at least five years in positions of a high decision-taking level.

The Technical Council and the Director General of the Institute will be responsible for the application and observance of the provisions of this article.

The professionalization and development system provided for by the Bylaws to which the preceding article refers, shall be governed by the following principles (Art. 286J):

- Each individual's own merits and the equality of opportunities for hiring and for promotions in the service, on the basis of the general experience, and/or of the Institute, considering performance, aptitudes, knowledge and capacity;
- Specialization and professionalization for the development of the tasks and activities assigned to each job;
- Retributions and fringe benefits linked to productivity, competitive in the labor market and that are sufficient to guarantee to the Institution the hiring and permanence of the best public servants in command positions and employees in general;
- Training and integral development related to the substantive activities of the Institute and linked to the improvement of the services rendered, with the purpose of guaranteeing efficiency in the rendering of the service, and
- Integrity, responsibility and adequate behavior of this personnel.

The Institute will constitute and, according to the guidelines to be issued by the Technical Council to this effect, will administer and handle a Fund to face the labor obligations it assumes before its employees, whether of a legal or contractual nature, which will be known as Fund for the Compliance of Labor Obligations of a Legal or Contractual Nature. To this effect, the Technical Council shall approve the rules of this Fund at the proposal of the Director General, who shall previously request the opinion of the Finance and Public Credit Ministry (Art. 286K).

The administration of the Fund shall take into consideration the policies and guidelines applied on this matter by the Federal Public Administration.

This Fund must be recorded separately in the books of account of the Institute, establishing within the Fund a special account for the obligations corresponding to the Retirements and Pensions Regime of the employees of the Institute.

The resources allocated to that Fund and the special account may only be used for the purposes established in this article.

No later than June 30, 2002, the Institute shall make an initial contribution for the constitution of the Fund for the Compliance with Labor Obligations of a Legal and Contractual Nature, to which effect it shall deposit in the special account provided therein, the resources that the Institute has at its disposal in the reserve corresponding to the "Retirements and Pensions Regime", established on the basis of the Collective

Labor Contract signed between the Institute itself and its employees, and the Institute shall deliver a proposal to the Federal Government, through the Finance and Public Credit Ministry with the purpose of establishing the dates for the gradual contributions that integrate the aforementioned Fund (Trans. XVI).

Conclusions

The amendments herein discussed set the bases to solve in the future the structural problems of the Institute; the purpose is clear in *articles 273 and 275 of this Law*, since the Chamber of Deputies, when approving the Expense Budget of the Federation, must take into consideration the *information and the report* referred to. Other not less important norms are the following:

1. The creation of new jobs must incorporate the annual cost of the future compliance with the labor obligations of a legal or contractual nature; also, the Institute has the obligation to publish in the *Official Gazette of the Federation* no later than June 30 of the corresponding fiscal period, the analytical report of all positions and jobs, including temporary, substitute, resident and similar positions or jobs; the salaries, fringe benefits and incentives of all types of its public servants, grouped by level, degree and group of command, and the changes authorized to its organizational structure by the Technical Council, as well as the number, characteristics and total remunerations relative to the hiring of outside professional services on the basis of fees (Art. 277D).
2. With respect to the constitution, the annual administration program, the investment and use for the operation of the reserves (Art. 278 through 286E).
3. The Financial and Actuarial Reserves shall be constituted for each one of the insurances and coverage through a three month contribution calculated on the income thereof, that will take into consideration the long term estimates of financial sustainability contained in *the financial and actuarial report* (Art. 284).
4. The General Financial and Actuarial Reserve shall be constituted, incremented or reconstituted through an annual contribution to be estimated in *the financial and actuarial report* to face catastrophic effects or important variations of a financial nature in the income, or drastic increments in expense derived from severe and long lasting epidemiological or economic problems that may provoke insufficiency of anyone of the financial and actuarial reserves (Art. 285).
5. The Institute may use the Financial and Actuarial Reserves of each insurance and coverage only to face falls in the income or increases in expense derived from economic problems lasting more than one year, as well as to face fluctuations in disasters greater than those estimated in the *financial and actuarial report* or for the payment of future benefits for which the corresponding provision had been made (Art. 286A).
6. Those of the professionalization and development system, to which confidential employees "A" will be subject, including the creation of a

Fund for the Compliance with Labor Obligations of a Legal or contractual Nature (Art. 286K).

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