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# THE AMERICAS SOCIAL SECURITY REPORT

# 2013



**10 Years of Strengthening  
Citizen's Well-being  
in the Americas**

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# 2013



**10 Years of Strengthening  
Citizen's Well-being  
in the Americas**



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The Inter-American Conference on Social Security (CISS) is a specialized international technical organization, with permanent character. The CISS was founded by the Social Security Directors of the Continent in a 1942 meeting in Santiago de Chile.

The CISS has as its main objective the development of social security in the Americas. In order to attain this goal it fosters the diffusion of achievements in social security, cooperation and exchange of experiences among social security institutions.

Through its publications, the CISS gathers and disseminates social security studies across the Americas, while making policy recommendations for the consideration of planners of programs and policies throughout the Continent.

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## Acronyms and Abbreviations

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CCT	Conditional cash transfer programs
DB	Defined benefit
DC	Defined contribution
EP	Emerging paradigm
FA	Family allowances
IRA	Individual retirement account
IT	Information technologies
LAC	Latin America and the Caribbean
LEP	Legislation on employment protection
LTC	Long-term care
OMCC	Organization and management of care consumption
UI	Unemployment Insurance
VAT	Value-added tax
WC	Workers' Compensation



## THE REPORT TEAM AND ACKNOWLEDGEMENTS

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## FOREWORD

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The 2013 Americas Social Security Report summarizes and reflects upon topics that have dominated the main debates on social security during the last decade. The eighties and the nineties tend to be identified as times of reform from North America to the Caribbean and South America; however, further significant reform processes occurred during the first decade of the 21st century and after.

The idea that financial regulation determines the behavior of individuals and society is a misconception that has become part of some debates. A deeper analysis shows that the opposite is true. Namely, society has a fundamental dynamic derived from the decisions by families on marriage, fertility and work, and by firms about forms of production, employment and benefit structure. A renewed process of reform is necessary to allow social security to adapt to this social dynamic. Consequently, this Report can be read as a reflection on what has happened and been debated, with the goal of focusing ideas on these core issues.

In this review, we learn that research and analysis have been abundant in some cases, but that there are gaps in knowledge in other significant topics, and that this reflection serves to balance the research and debate efforts. Debates value financial sides in a more correct dimension, return to granting the individual the central role as motivation for social security, and search for balance in the tools available to the State to achieve its goals. It has been ten years when for some time there was great global optimism, but also two severe episodes of economic recession have underlined the significance of social security. Improvements have taken place with great effort and there is still a lot to be done.

The new Recommendation Concerning National Floors on Social Protection of the International Labour Organization, adopted in 2012, is a milestone that must serve as flag to each of the agencies that form the Inter-American Conference for Social Security to pursue their mission. A message that has been repeated in the Americas Social Security Reports is that far from diminishing its importance, globalization imposes a deepening of the social security schemes. We hope this Report will be helpful to reinforce the message.

**Gabriel Martinez**  
**Secretary-General**

**CHAPTER I  
INTRODUCTION**





## CHAPTER I INTRODUCTION

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**T**he development of Social Security responds to a continuous process of adaptation of programs and agencies to new realities and information. Sometimes changes are abrupt, like in the pension reforms witnessed in the eighties and nineties in many countries; but most of the time, changes are undertaken step by step.

The direction of reforms is influenced by political considerations, but, most importantly, by the facts and information available to decision makers. Over the past ten years, the Inter-American Conference on Social Security (CISS) has issued the Americas Social Security Report. Each of these publications has tackled specific topics relevant to social security, and has been written with the aim of providing information to support the decision-making process of the CISS members and to inform the social security community of developments in specific areas.

After ten years of research, it is useful to provide a summary view of the issues that have been treated and to identify areas for further analysis. It is clear that social security is the most important tool current societies have to protect individuals and families from risks—either individual or systemic—faced along the life cycle. Social security covers risks that are universally identified, and, while at first glance solutions can be attained by different arrangements in the design of benefits, financing and organization, a detailed look of how

social security programs work in specific countries allows us to conclude that a few core principles are always followed or, at the very least, should be followed. This review highlights the common principles of the social security systems and some of the more relevant debates around the reform processes.

Broadly speaking, social security programs can be grouped into four categories: pensions, family, employment, and health programs. Countries differ in the terminology used, but the general model of social protection systems funded with the productivity of workers, firms and state, guarantees coverage of these four fields. Additionally, all programs share three basic topics: financing, management and organization, and service provision. Each of these topics has been the object of analysis in the annual reports. A more central approach has also been followed and is based upon the analysis of the situation of individuals and families across the lifecycle, with special emphasis on understanding human capital and labor market behavior of workers. Some groups have been the target of special considerations: children, women, older adults, workers around retirement age. In the global economy, labor markets in any country are affected by two interrelated phenomena: how the globalization takes place and financial crises. Since 2000, the world has witnessed two global crises, the one in 2008-2009 being the most profound. As

of this writing, there is a strong possibility of another global crisis. Two Reports addressed how these topics relate to social security, one dealt with globalization and another with world-wide recession.

Previous Reports have provided both positive and normative views on the labor markets and the social protection systems. On the positive side, the effort has been to provide the latest hard information available, either by direct production or through summarizing academic research. On the normative side, general recommendations to improve social protection programs have been provided with the understanding that each country or agency will find their own particular path to follow.

The following chapters of this Report are organized along topics. In this introduction we provide a chronological summary of previous Reports, providing the arguments behind the Annual Assembly of the CISS's choice to treat a particular topic, and the main messages of each Annual Report. We hope that this brief summary of ten years' work invites interested persons to read the full annual issue.

*2002: Financing Problems and Options for Solutions.* The topic of the first CISS Report was decided after Latin America and the Caribbean suffered two decades of low economic growth and in the middle of a global recession. It is not surprising that the main concern had to do with financing problems. The Report reviewed the theory and evidence on the causes for the financial stress faced by most countries in the region, as well as the options available to transform social security in such an environment. It highlighted that demographic changes, low productivity and wage growth, high informality, inadequate reserve funds and unbalanced design (between contributions and benefits) had put defined benefits systems in an unsustainable situation. It also mentioned that while defined contributions systems can help solve the financial problems, these schemes are not free of financial stress due to the need to finance the transition cost and the minimum guarantees usually

provided by national states. The Report posited that while each country requires a different policy, the result must come from an inclusive and transparent process, and consider the effect on national savings, labor supply, coverage of the informal sector, and social inequities across the income distributions and across different cohorts.

*2003: Evaluation of the Reforms.* By 2003, many pensions and healthcare insurance schemes across the continent had been restructured or parametrically reformed, while other countries debated the possibility of reform. The CISS Report contributed by integrating and updating evidence regarding the impact of the reforms. Empirical evidence was provided by reviewing studies or by developing specific analysis. It pointed out that while impact evaluation is a most difficult statistical task, evaluating reforms should be a priority. Not only does social security affect different persons in different ways depending on age, family structure, income, information availability and processing, but most reform episodes combine structural and parametric changes that confound effects. The Report documented positive and negative effects of the different reforms, but was cautious in drawing conclusions.

*2005: Labor Markets and Social Security Fragmentation. Financing for HIV by Social Security.* In 2004, the title of the Report was renamed by one year, so there is no 2004 edition. The 2005 Report aimed to provide a holistic view, considering the different social events and public policies that interact with social security. It recognized that previous editions focused on financial aspects, and that there was a need to provide a discussion and evaluation based on the economic and social goals. Economic and social performance of social security in the Americas is closely related to labor status of individuals and coverage of social security. The report reviewed and discussed the relationship between labor markets and social security schemes and other institutions. During the 1990s, the region underwent deregulation and privatization, and major

trade and fiscal reforms, all of them aimed at liberalizing the economies. The Report concluded that countries cannot rely on better investment environments and on a more competitive economy as magic cures for the problem of social security coverage. Across the region, there is a persistent problem of coverage of small firms and other informal segments. The Report argued that while social security-related factors may explain informality—cost of contributions, design of social security plans and administrative models for the collection of taxes and for the provision of services—the regulations on employment, the tax codes, and labor courts' efficiency may also have an important role, and that changes in social security laws may have only limited effects on coverage. The Report called for an integral approach to deal with the problems of the informal economy. The Report also identified four groups of the population that need specific policies: the self-employed, the elderly without coverage, women with low attachment to the labor market, and young workers with low skills. The last three chapters of the Report are devoted to the study of fragmentation of social security schemes within countries, social health insurance and labor markets, and HIV/AIDS financing by social security.

*2006: The Challenges of Aging and Disability: Employment and Insurance. International Social Security Agreements.* This edition argued that specific policies should be designed for persons around statutory retirement age. It also provided a revision of labor market and social security policies for the disabled. Finally, given that the Americas are a zone with significant migratory flows, the Report studied the status of International Social Security Agreements (ISSTA). Using household surveys and other public information, the Report documented that Labor Force Participation (LFP) of older workers (older than 55) has increased significantly over the past decades, with the exception of United States and Canada. The low coverage of pension benefits may explain why a larger share of the elderly works

in Latin America and the Caribbean than in any other region of the world. Older workers also have a high incidence of work in the informal economy. The understanding of how workers respond to different social security rules is necessary to implement policies that extend the participation of workers in formal labor markets. The Report also discusses the topics of disability and of long-term care (LTC). Although disability can be sometimes measured with difficulty, all countries appear to work with common definitions that include functional and contextual factors. The national governments in the developed nations, including Canada and the United States, have responded to people with disabilities through comprehensive legislation that protects their employment. Some countries of Latin America and the Caribbean (LAC) have started to implement employment programs. Disability is mostly covered by social security programs but people born with disabilities or that become disabled while not having a formal job are not entitled to benefits, with few exceptions. Certainly, extending the coverage of disability benefits is a pending topic for the region. Another pending topic is the provision of LTC coverage. Citizens in the region are living longer. It is estimated that, in the coming decades, 15 to 20% of households will have an older adult in need of LTC. Public programs should be implemented to support either the caregiver in their dual role as participant in the labor market and as caregiver, and the disabled person directly. International experiences show that in countries where public LTC insurance has been implemented, it often follows the financing rules of the social health insurance. The last chapter of the Report documents migratory flows in the continent and reviews the implementation of ISSTA. Two important conclusions emerged. First, there are important migration flows from developing countries to developed ones, and regional migration, i.e., in the southern cone. Second, while countries have been very active in signing ISSTA, many people still cannot benefit from these instruments.

*2007: Globalization and Social Protection.*

Countries and social protection systems have always faced issues posed by trade and foreign investment. Yet, in late 2000, it was evident that times were (and still are) unique in that nearly all nations were participating in a general movement involving trade, investment, exchange of information, and cross-border migration. As a response, national states are developing regulatory frameworks to deal with those and other related issues, including the environment, human rights and labor security, and industrial and consumer standards. The Report discussed the ways in which globalization interacts with social protection. It also analyzed the development of unemployment programs. The effects of globalization are probably one of the most debated issues in the last few years. While globalization in general is associated to higher growth rates of national economies, there is a general feeling in the developing nations that promises to participate in the liberalization movement have not always been realized, and international social security agreements often do not cover the migrant workers from less developed countries. Yet, there is an agenda social security agencies in the countries can follow to advance social protection: i) evaluate compliance with core labor standards including the development of institutions to certify multinational companies; ii) keep working on multinational social security agreements to protect migrant workers, on two dimensions, extend coverage to more people and extend coverage to more risk (health, disability, and death/survivors insurance); iii) extend national social protection systems to deal with the adverse effects of globalization; and especially, iv) implement unemployment insurance as the soundest tool to protect displaced workers.

*2008: Innovating Models of Social Insurance.*

This edition was written under the hypothesis that the potential for gains in the efficiency of social programs is great, and that some of the problems programs face can be solved only after a proper

focus is given to administrative and organizational issues. The Report provides information about the best general operational and organizational practices, and highlights what the role of the regulators should be in increasing the productivity of the programs. While it is recognized that operational design is a constant and dynamic process highly influenced by IT developments, the report identified critical aspects of general application that may help social security agencies improve their operations, services and productivity. One of the main recommendations of the Report is that even the most specific organizational change should conform to an overall strategy and organizational structure. The Report based most of the analysis presented on two interrelated facts. First, current technologies allow the management and organization to be centered on the individual. Second, the operating model of all social security programs shares the same core processes: product design/development, funding, management, delivery of benefits, and provision. This arrangement implies that important gains can be obtained by horizontal integration, or at least coordination of core processes common across all programs (funding for example) and vertical disintegration of core process (provision being separated from funding). Recent changes observed in some agencies of social security across the continent are in line with this arrangement.

*2009: Evaluation in Systems of Social Security.*

The 2009 Report deals with evaluation, understanding it as the way to measure administration activities, results and expectations. Contemporary best practices in administration consider that management and evaluation are part of the same integrated activity. Historically, evaluation has often been viewed as an extra or additional action that social security agencies or governments can do to improve communication, correct deviations and gain support for the agencies or for a reform process. A basic tenet of the approach of the Report is that good administration cannot be separated from

effective evaluation. Four considerations that a comprehensive evaluation of social security must include were identified: i) evaluation should respond to the concerns of different perspectives, including the economic, actuarial, administrative, fiscal and operation research; ii) the approach should be based upon the well-defined steps that are identified in evaluating best practices (gaining the involvement of key stakeholders, designing the framework, identifying the indicators, setting targets, defining the information sources, developing the elements for the evaluation, and designing the policy for disclosure of results); iii) evaluation should be performed for systems, agencies and programs in the understanding that programs are managed by agencies and systems are the collection of agencies and programs, each area having their own goals and thus indicators to be followed; and, iv) evaluation should have to be centered in the individual.

*2010: Social Security and Labor Markets through Economic Cycles.* This Report deals with the relationship between economic cycles and social insurance. The analysis in the Report is based on two facts. First, social security exists, to a large extent, to deal specifically with economic downturns. Two, by 2009, it was clear that many countries were in a recession forecasted to be deep and long-lasting, and unemployment rates had risen considerably. Thus, the Report took anew the issue of unemployment insurance and the lack of it in many countries, the challenges faced by financially weakened national governments to face the problems of coverage, and the structural deficiencies of pension systems that have been stressed by the fall in assets prices. Even after, and perhaps because of the Great Recession of 2008-2009, which was sometimes compared to the Great Depression of 1929, governments today are better prepared to support the national economy to deal with the adverse effects of recession, and social security plays a key role in protecting workers. Still, it was revealing just how many countries reached the Great Recession without a well-established

unemployment program, and how pension funds suffered major losses, affecting the persons to be retired in the next years, sometimes exposing the existence of governance problems. The final chapter of the Report dealt with an additional topic, namely, forecasting national health expenditures. Health spending will continue to grow significantly in the years to come mainly as a consequence of the high value persons give to health and longevity, and social security agencies will have to design policies to make a good use of this money.

*2011: Children and Social Security.* The topic of the 2011 Report does not need a justifier. It evaluates the way in which social security is supporting children, the most vulnerable individuals in any society. Sadly, in many LAC countries, child well-being is far from satisfactory, and labor markets and education systems are unable to provide adequate opportunities to large shares of them. Moreover, in some countries there are significant shares of disabled, orphaned and lonely-migrant children. New findings in economics, neuroscience and psychology regarding human capital formation can shed light on identifying areas of opportunity and policy options for social security programs. Regarding youth employment programs, the Report finds that the main problem may be the lack of a strong connection between education and work. In recognizing that social security programs have a window of opportunity to adapt their programs to make them more effective in improving the welfare of children, the Report recommends: i) establishing universal coverage in healthcare and financial protection for small children (through family allowances), specially for those who live in adverse conditions; ii) involving social security agencies in understanding the environment where the children live and implement preventive and corrective programs; iii) revising the portfolio of programs to assess whether they are the most effective tool to contribute to child well-being; iv) adding flexibility to benefits so they can be adapted to respond when they are needed the most; v) including gender issues

as main components of programs; vi) making an effort to increase educational levels; vi) supporting young persons to increase upper-school graduation and rates of admittance to higher education; vii) adjusting social security rules regarding affiliation, contribution and benefits to facilitate the use of schoolwork and on-the-job training for teenagers; viii) removing labor and product market obstacles to labor demand and to develop labor force skills and competencies; and ix) implementing a balanced portfolio of policies and institutions aimed at improving youth employability integrated by several programs that recognize the heterogeneity in needs, education backgrounds and other characteristics of youth that influence the possibility of their getting a job.

*2012: Fairness, Work, Retirement, and Social Protection.* The developments that lead to the financial pressures on social security are good: we are living longer, healthier lives, with more healthcare and employment options, allowing older adults to work until later in life with coincidentally responding reform movements within the complexity of these issues. Still, these are adjustments that demand major political agreements. The question about the "right age for retirement" looms large in the life of individuals, in the planning and management of social security agencies, and in the definition of national labor and social policies. While the topic has been subject to substantial national and international debates, the issues are far from settled. The decision to work, or alternatively retire, is eminently individual, but regulations on labor contracts and social security regimes affect such decisions. The Report contributes to the debate over how regulations on work and retirement should be reformed, and on how social security should evolve so as to make retirement a benefit and not a costly event. The Report is divided into two parts. The first is descriptive and generic, and provides statistics about main variables that characterize labor markets across the lifecycle, with emphasis on the period around retirement age, and

summarizes the main hypothesis provided by the social sciences on the phenomenon of retirement age. The second provides a detailed compilation of information and a significant actuarial analysis from which to obtain simple measurements of pension retirement benefits that can be compared across systems. The second part of the Report aims to compare two main indicators of retirement systems: the replacement rate and the pension wealth (the present value of benefits provided at the date of retirement). Results depend on the scenarios assumed for the main variables highlighting the difficulties in reaching simple standardized results. Although the field is wide open, standardized results are needed to promote better public policies. Social security has been a remarkable institution in terms of its ability to transform, and ongoing debates will lead to improved frameworks for individual and collective lives.

Previous Reports have covered a broad range of topics for most social security programs. Nevertheless, for the careful reader it must be clear that the work is not finished. Some programs have not been analyzed thoroughly (such as work risk insurance) and much remains to be said on gender issues. Also, several topics already studied deserve to be discussed or revised.

Chapter II of this Report describes the evolution of the main labor market variables during the first years of the century, putting emphasis on the well-being of individuals. Chapters III to VI deal with the main tendencies and debates regarding pension policy, family programs, employment policy and health insurance across the region. Chapter VII approaches a topic that has become outstanding in several Reports, namely the problem of administration and governance, and of how to build citizen-centered organizations. Chapter VIII deals with social security financing, an area where substantial conceptual progress has been achieved during these ten years.

**CHAPTER II**  
**LABOR MARKETS AND WELL-BEING AT THE**  
**BEGINNING OF THE XXI CENTURY**





## CHAPTER II

# LABOR MARKETS AND WELL-BEING AT THE BEGINNING OF THE XXI CENTURY

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### II.1 Introduction

**T**his chapter aims to provide information on the individuals, as well as on the events, characteristics, and phenomena that surround them: demographics and family composition, poverty, education, labor markets, health and risky behavior being the most important ones. Social security systems should respond to persons' individual conditions and needs.

In the past ten years, the Americas Social Security Report has provided detailed information on the aspects mentioned above. Some variables change only in the long-run, while others may have changed even during a short period, especially because the world suffered two global crises in the last decade. Labor markets (including internal and international migration) and poverty can change quickly in such an environment. Demographics and family composition, education, health and even risky behavior respond to forces in the long-term. The chapter is organized accordingly.

### II.2 Labor Markets: Formality, Employment, Wages and Poverty

In the past ten years, we have witnessed two labor market crises. The first occurred between 1999 and 2001, and was associated with the "dot.com bubble". The second, known as the "Great Recession", had

its deepest phase between 2008 and 2009, although the negative impact is still felt in some countries. This new crisis is associated with the "housing bubble" that affected several developed countries and the banking panic of September 2008. The recession of 1999-2001, was felt differently across countries, while the second had a more global effect. In the Americas, the first recession hit hardest in South America, while the second was deeper in North America.

Labor markets and poverty are affected by recessions because human capital is the largest component of national wealth. Thus, when the entire national economy fluctuates, labor incomes, poverty and employment opportunities across borders are affected. In this section of the report we would like to answer two specific questions. One, have the labor markets in the countries of the continent recovered in the decade since? And two, what has been the effect on poverty overall? The analysis compares the level of the variables when the economy peaked before these two crises. This allows quantifying "gaps", i.e., the difference between the observed level and the "potential" (in reference to the peak) level of the same variable.

There are two main limitations to performing a standard analysis for all countries. First, ideally, this type of analysis should be performed with high frequency data (i.e. monthly or quarterly), but if we want to include most of the countries in the

continent, we have to rely on annual data. Second, while in some countries the "peaks" and "valleys" of economic cycles are clear-cut, in other countries the economy is more stable, even during the two global crises. The peaks and valleys were identified in the 2010 Americas Social Security Report (CISS 2009). In the following figures the shaded area indicates the period from the "peak" to the "valley".

### **Employment**

The following figures indicate the performance of total employment in the countries for which we could obtain annual data. We can observe three patterns (all in relation to earliest peak). First, in Canada, Colombia, Mexico, and the United States, there is an employment gap by 2012. Second, there are countries for which there is not an employment gap—that is, the level of employment is similar to the potential employment. These countries are: Brazil, Chile (although it has an employment gap with respect to latest peak), Costa Rica, Ecuador, Peru, and Uruguay. Finally, there are countries where current employment is higher than potential employment: Argentina, Panama and Venezuela. In the case of Argentina, it is possible that the severity of the 1999-2001 episode has made data very unreliable.

### **Formal and Informal Employment**

Figure II.2 shows the total number of potential and observed formal employees. The potential number of formal employees is calculated in the same way as potential employment—that is, the employment and the formality ratios remain constant, at the

levels of the "peak" of the business cycle. Figure II.3 complements Figure II.2. It shows the total number of potential informal employees and the number of observed informal employees, calculated using the same reasoning for the case of formal workers. Using this information and the information regarding employment, we can observe the following: i) Mexico and Colombia—which show an important formal employment gap—register an important formal employment gap, which translates into a larger participation of informality in the recent years; ii) for the countries in which we identify no employment gap (Brazil, Chile, Costa Rica, Ecuador, Peru and Uruguay), formal employment is higher than potential formal employment and, on the contrary, informal employment is lower than potential formal employment; and, iii) in the countries where we observed higher current employment than potential (Argentina, Panama and Venezuela), formal employment is also higher than potential formal employment. Thus, it seems that informality is strongly anti-cyclical.

To assess the magnitude of these phenomena, we calculate the difference between employment, formal employment and informal employment, and their potential values for 2010. Results are shown in Table II.1. In this table, we confirm that two countries—Mexico and Colombia—have a low performance, six countries—Brazil, Chile, Costa Rica, Ecuador, Peru and Uruguay—have an average performance, and three countries—Argentina, Panama and Venezuela—have good performance. United States and Canada have a low performance in regards to total employment, while informality is not a significant issue there.

**Figure II.1**  
**Employment and Potential Employment across the Business Cycle, 2000-2010**

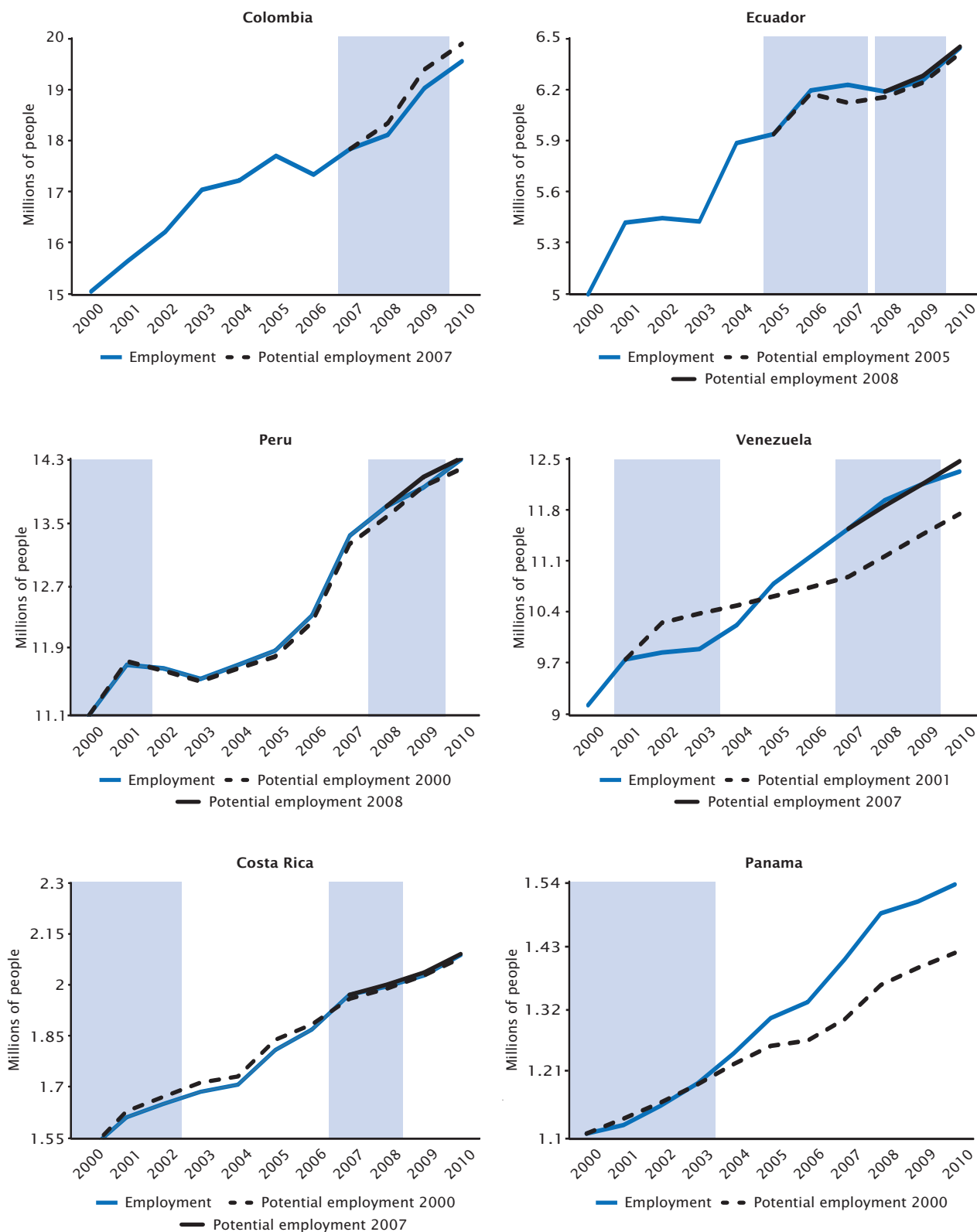


Figure II.1 (continued)

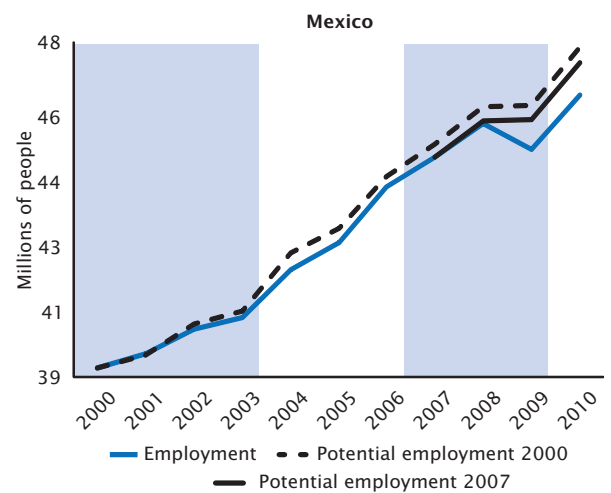
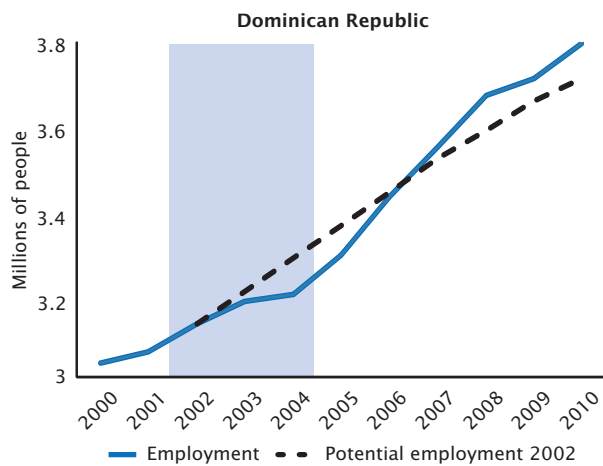
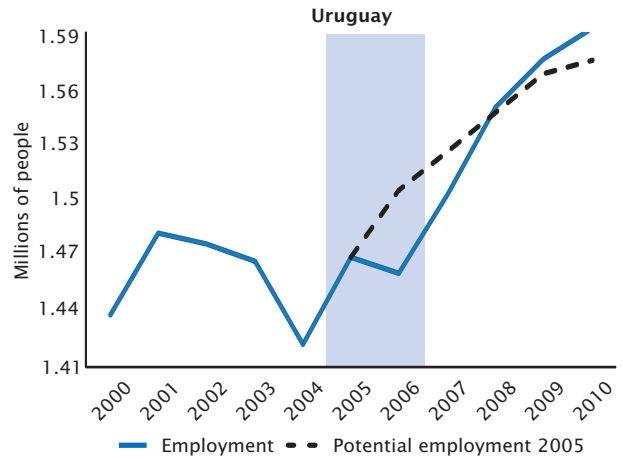
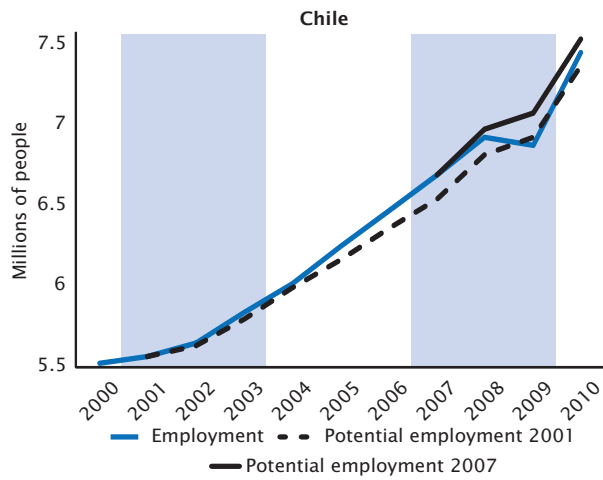
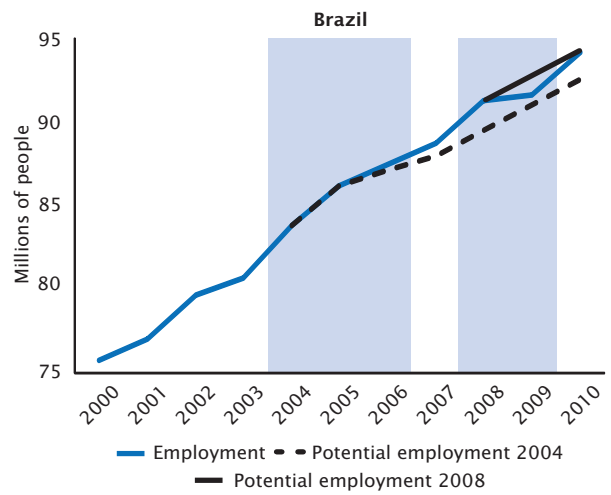
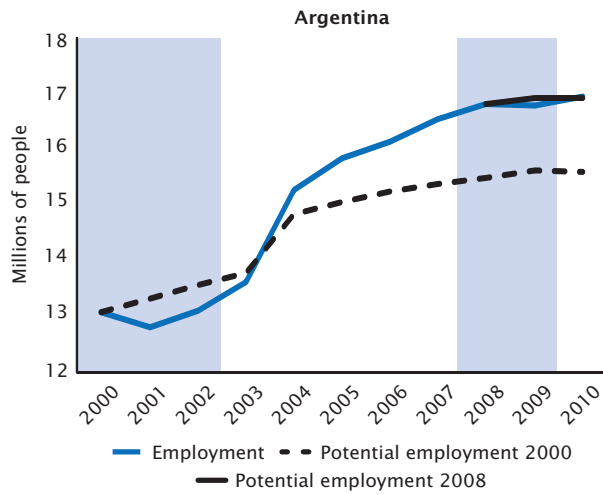
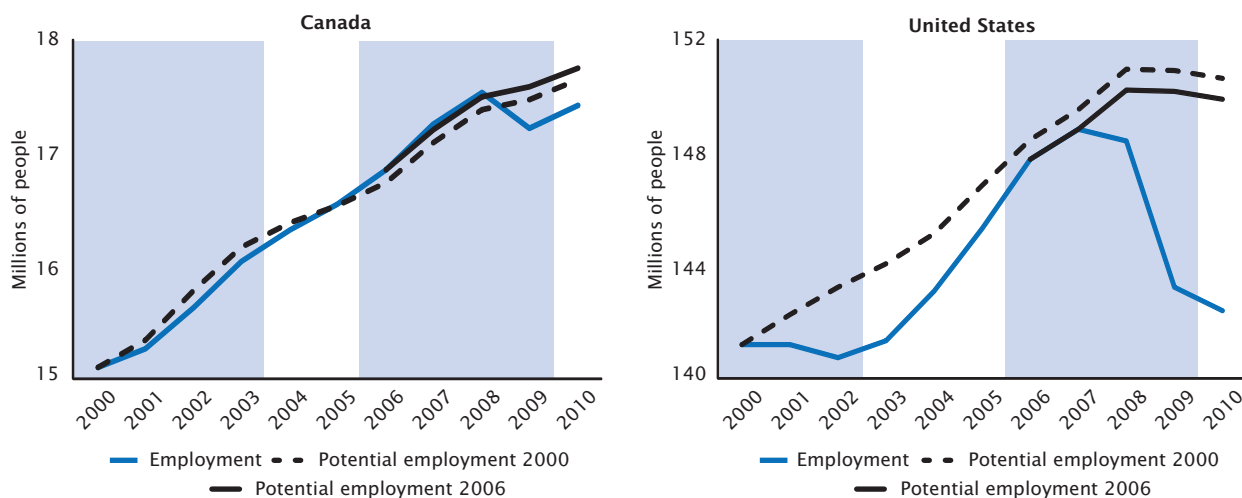


Figure II.1 (continued)



Note: Employment calculated using working age population 15+.  
 Source: Own calculations using International Labour Organization (ILO), LABORSTA (2012).

Figure II.2  
 Formal Employment and Potential Formal Employment across the Business Cycle, 2000-2010

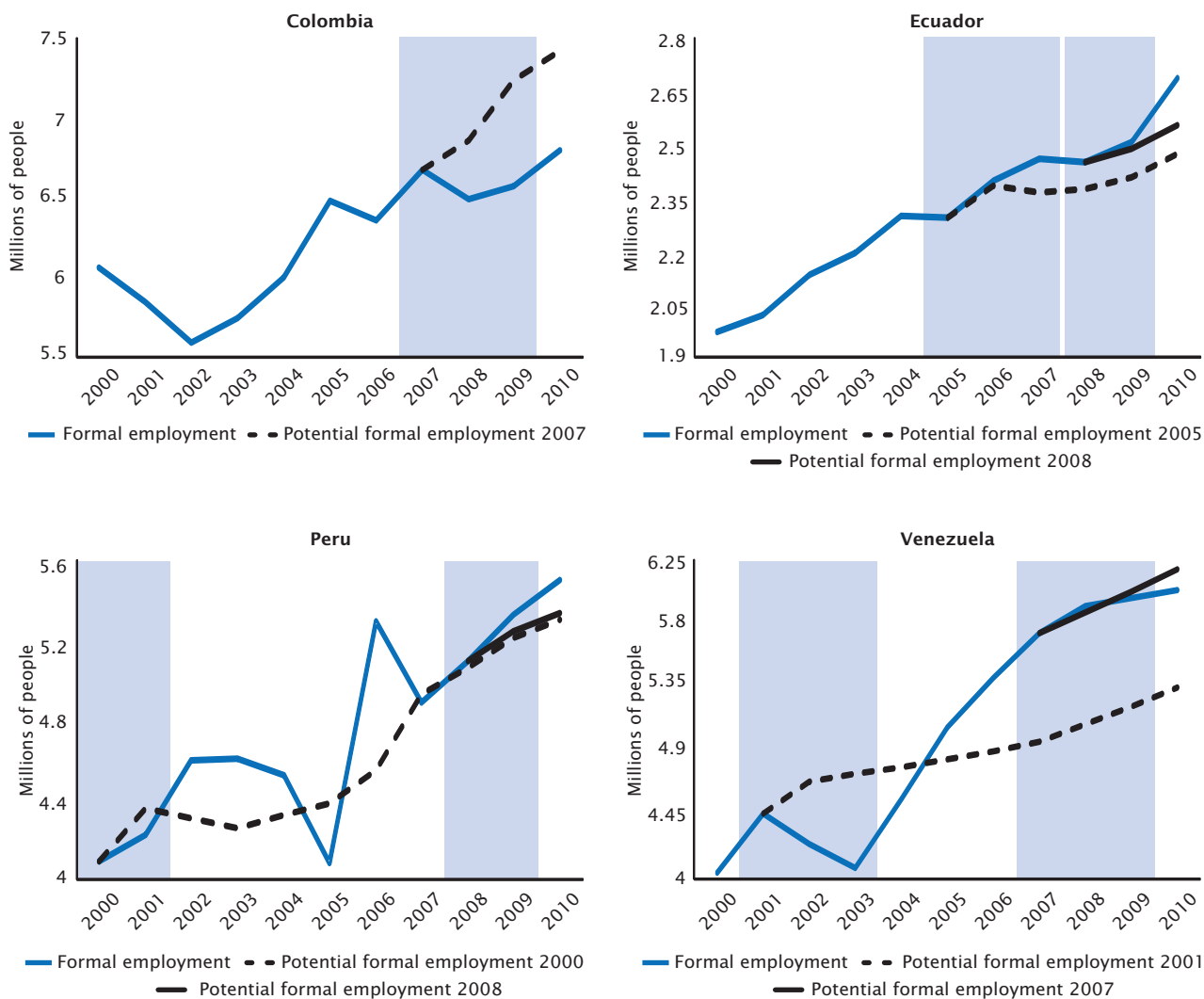


Figure II.2 (continued)

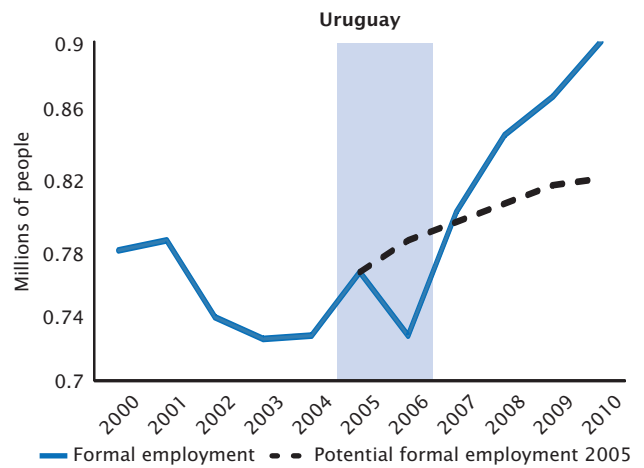
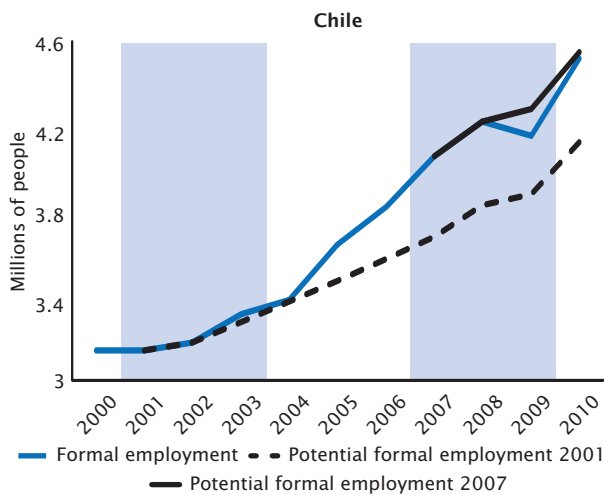
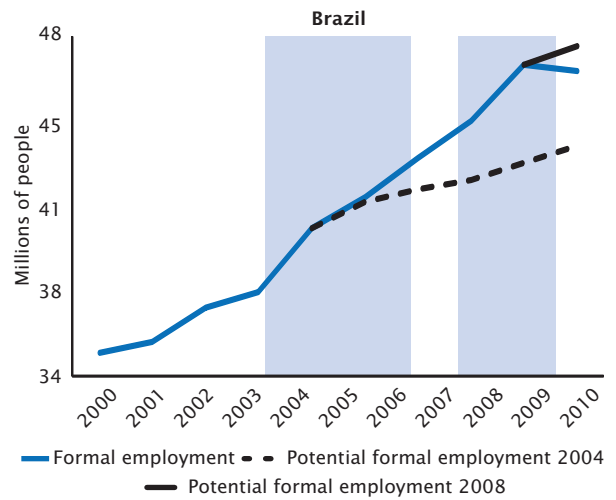
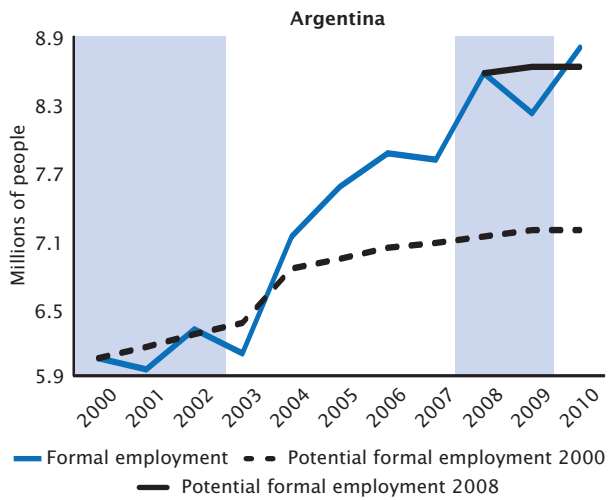
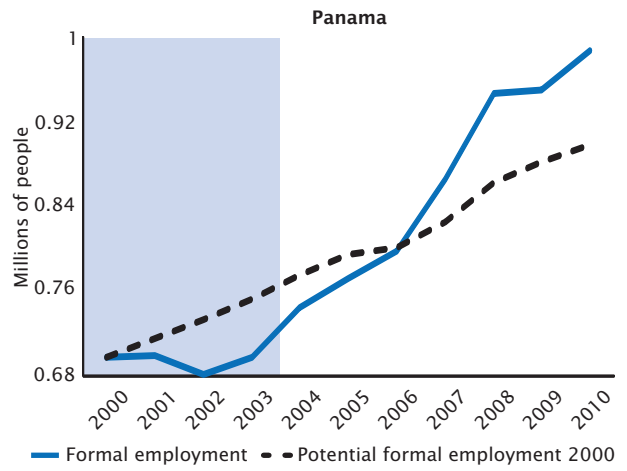
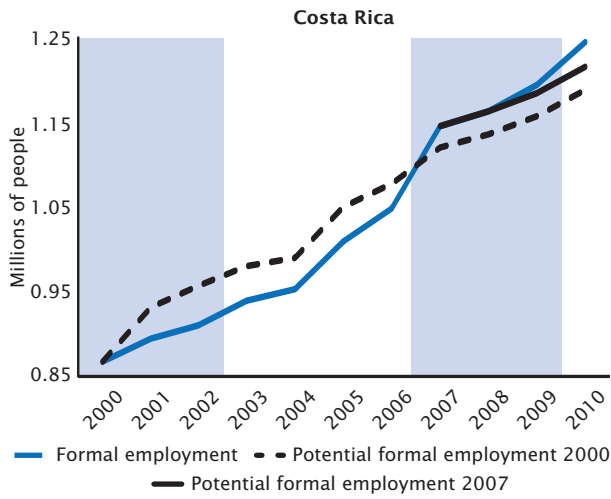
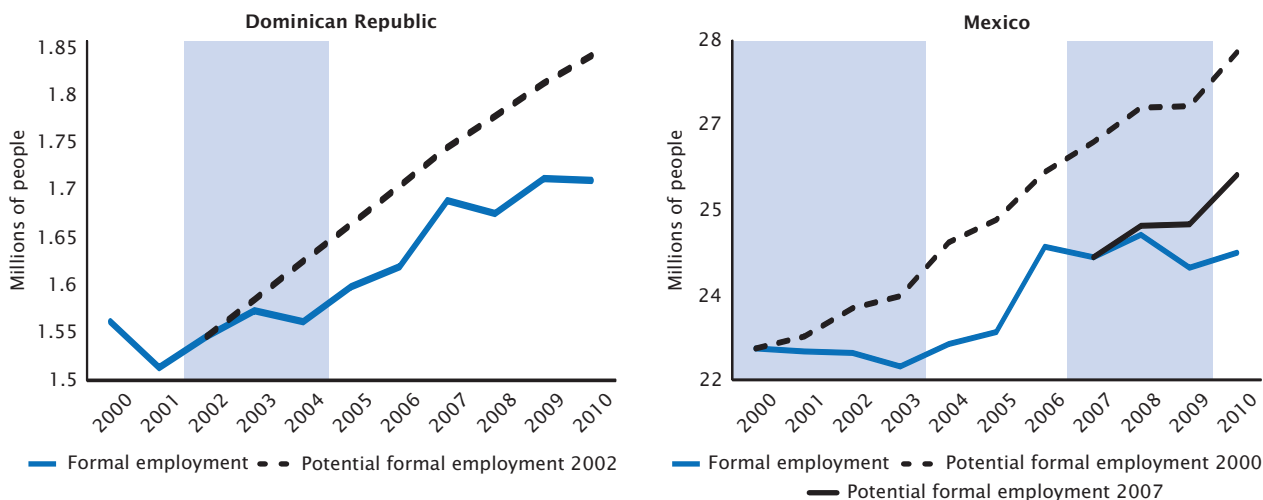


Figure II.2 (continued)



Note: Formal employment defined as salaried: private (establishments of 6 or more employees) and public sector employees.  
 Source: Own calculations using International Labor Organization (ILO), LABORSTA and QUIPUSTAT (2012).

Figure II.3  
 Informal Employment and Potential Informal Employment across the Business Cycle, 2000-2010

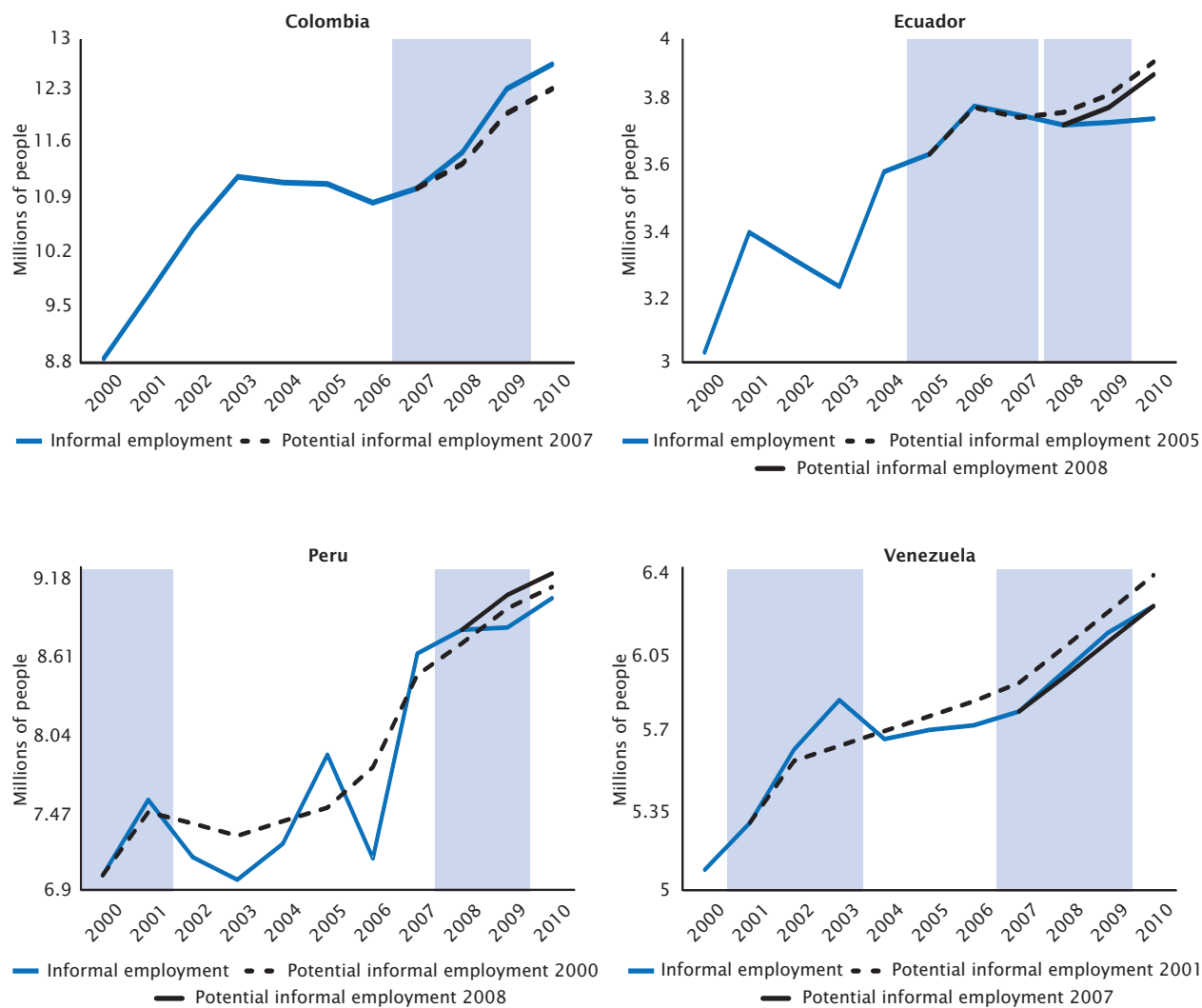




Figure II.3 (continued)

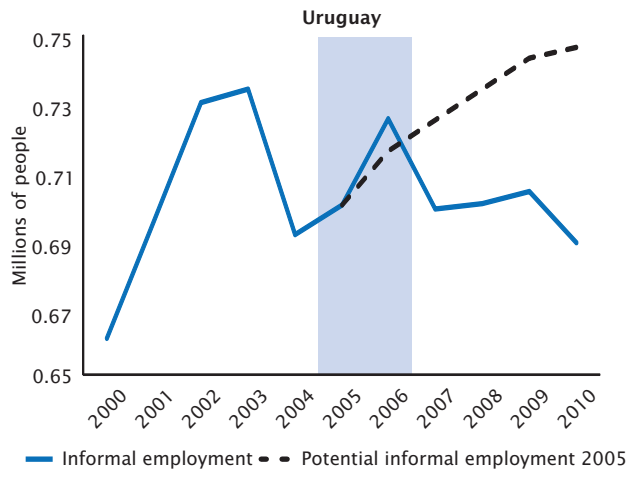
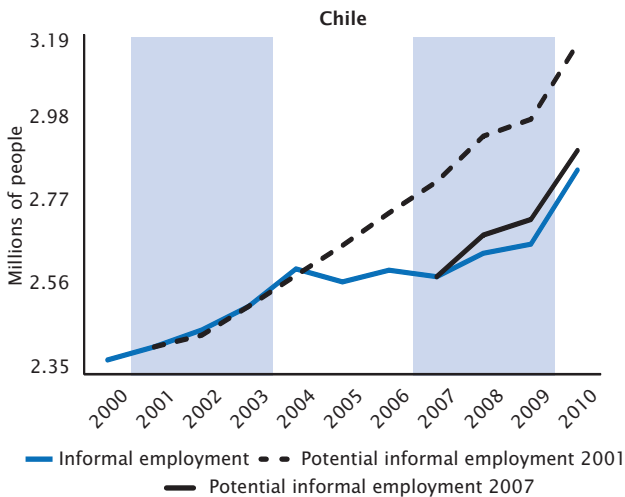
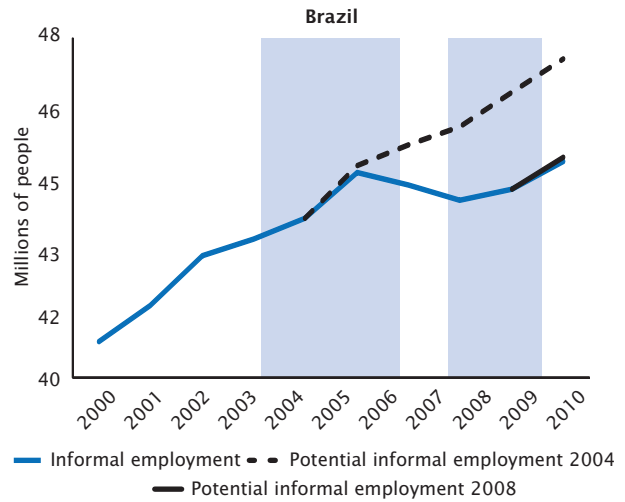
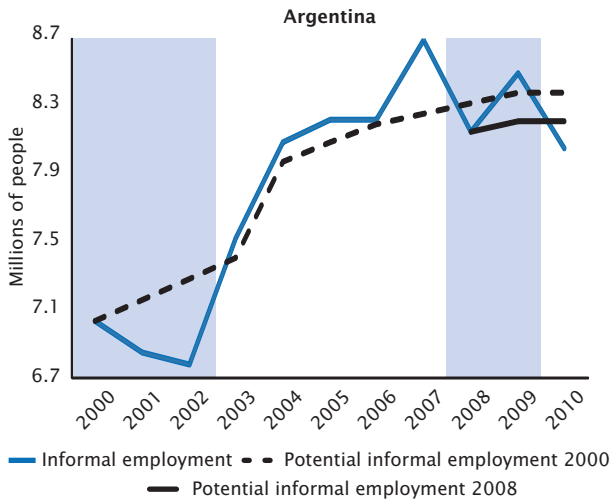
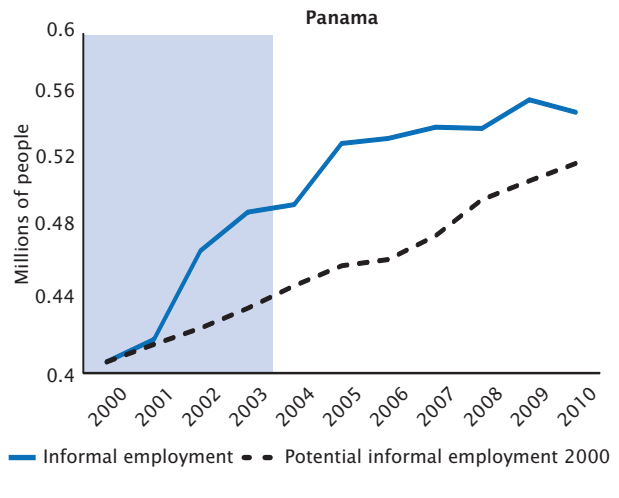
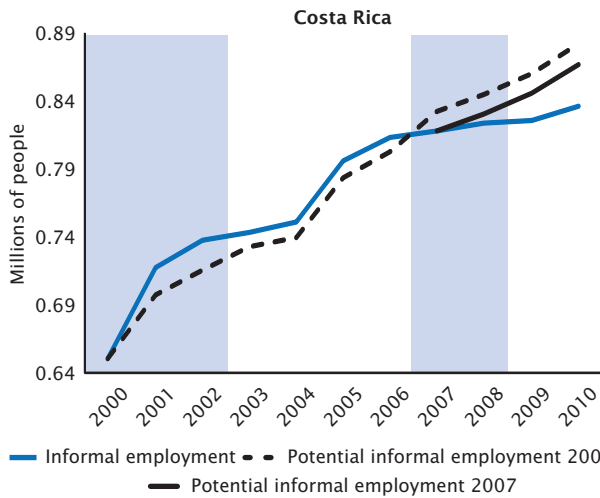
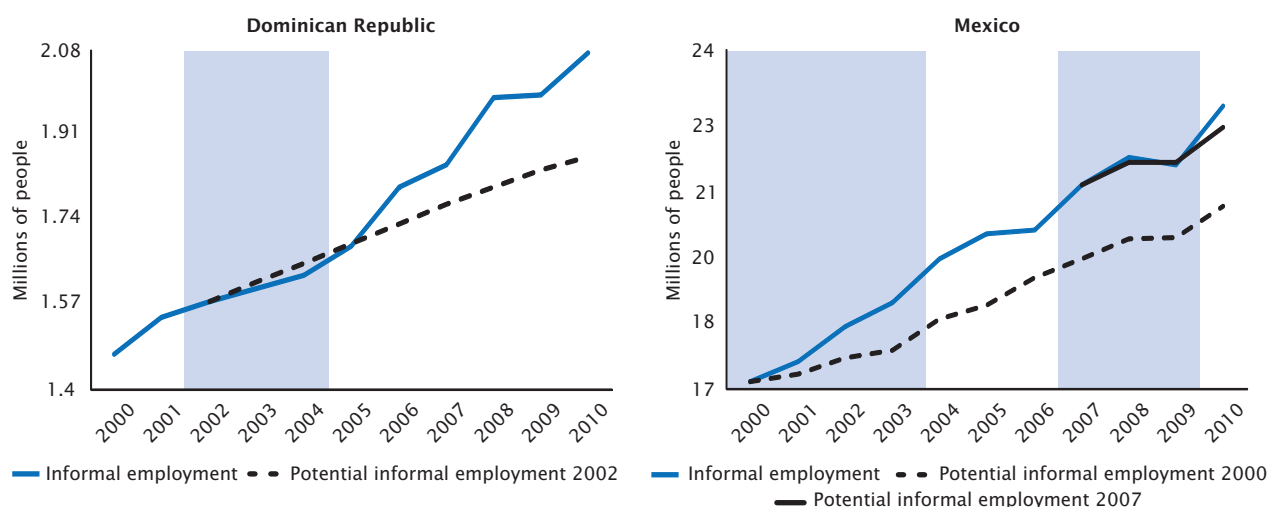


Figure II.3 (continued)



Note: Informal employment is defined as salaried: private (establishments of 5 or less employees), non-wage workers, housekeeping, family workers and others.  
 Source: Own calculations using International Labor Organization (ILO), LABORSTA and QUIPUSTAT (2012).

**Table II.1**  
**Employment, Employment Gap, Formal and Informal Employment Gap, 2010**  
 (thousands of persons)

Region/Country	Employment	Employment with respect to potential	Formal employment with respect to potential	Informal employment with respect to potential
<b>Andean</b>				
Colombia	19,541	-330	-652	322
Ecuador	6,438	33	212	-179
Peru	14,482	124	205	-81
Venezuela	12,317	574	706	-132
<b>Central America</b>				
Costa Rica	2,089	9	57	-48
Panama	1,541	119	89	30
<b>Southern Cone</b>				
Argentina	16,949	1,341	1,672	-331
Brazil	91,633	608	3,040	-2,432
Chile	7,378	79	392	-312
Uruguay	1,592	17	81	-64
<b>Mexico and the Latin Caribbean</b>				
Dominican Republic	3,799	85	214	-129
Mexico	46,993	-1,340	-3,543	2,203

Source: Own calculations using ILO, LABORSTA and QUIPUSTAT (2012).

**Wages**

Figure II.4 shows an index of average annual wages taking 2000 as base year. The sample used in each country varies significantly; in some cases it refers to the manufacturing sector, in others to urban wages and so on. Thus, comparability of the level of wages may be difficult, but perhaps the variation over time reflects better the differences across countries. In general, we observe large variation

across countries, with most registering gains on the order of 1% annually while half of the countries of Central America and Venezuela registering lower wages today than ten years ago. Argentina shows a large increase in average wages, but this is affected by the recession of 2000, which was accompanied by a monetary crisis in this country, making that year a bad base.

**Figure II.4  
Annual Average Wage (Index), 2000-2010**

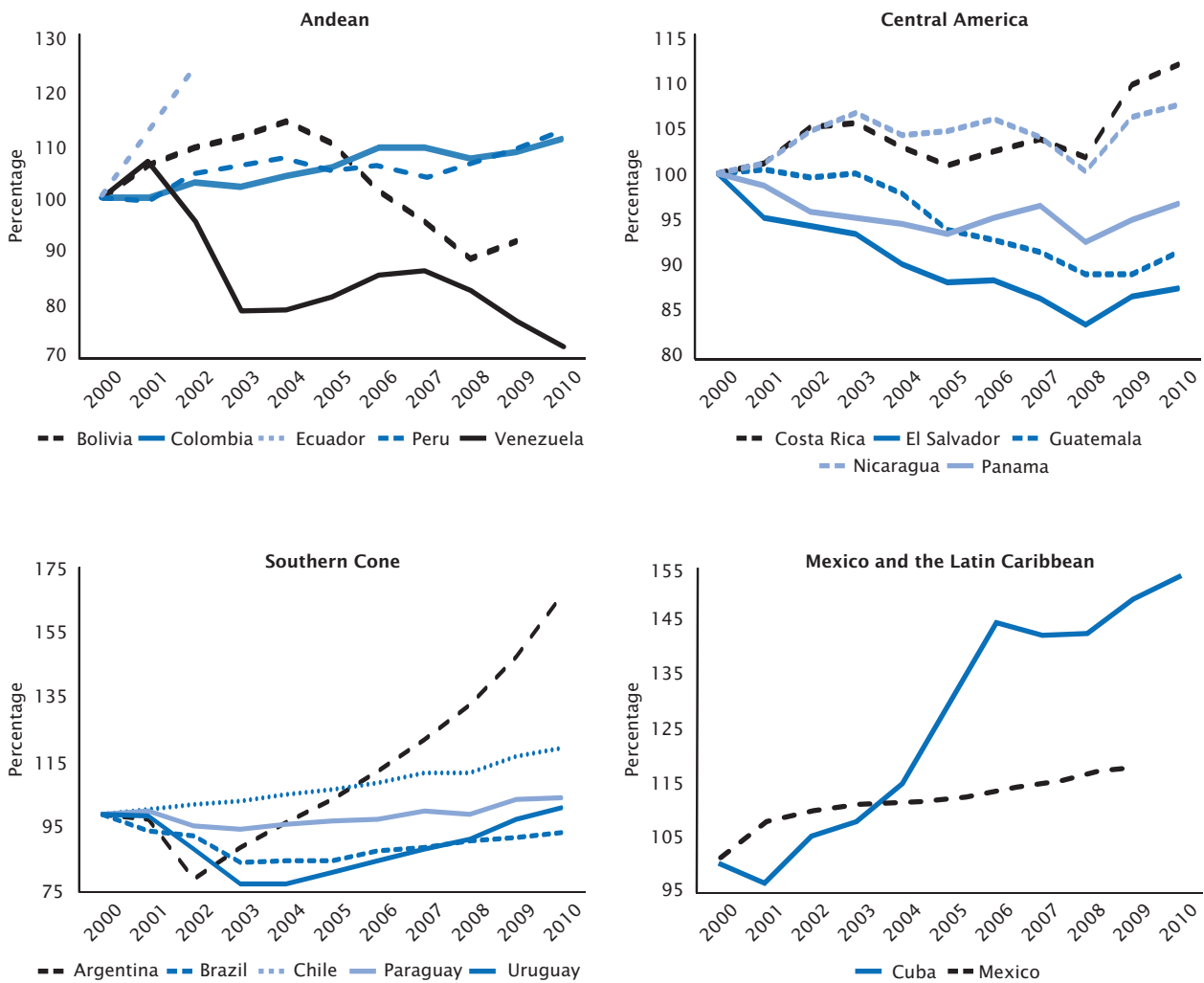
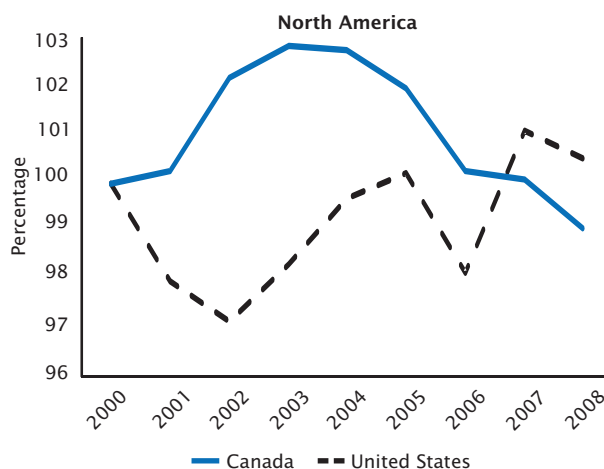


Figure II. 4 (continued)



Notes: CEPALSTAT, Argentina: Manufacturing. From 4th quarter 2001 registered private sector workers. Bolivia: Private sector in La Paz. Years 2000-2009. Brazil: Workers covered by social and labor legislation. From July 2002, wages of employees covered by private social and labor legislation. Chile: General index of hourly wages. Colombia: Workers and employees of the manufacturing industry. Costa Rica: Average wages declared by employees assigned only to Social Security. Cuba: Average monthly wage in state agencies and mixed; no payments in convertible pesos. Ecuador: Engaged in non-agricultural businesses with 10 or more employees. Guatemala: Average wages declared by workers affiliated to Social Security. México: Manufacturing. Years 2000-2009. Nicaragua: Average wages of the insured by the Social Security. Panama: Average salary of contributors to the Social Security, private and public sectors. Paraguay: Average salaries in Asuncion. Since 2002, index of wage and salary workers in nonfarm businesses with 10 or more workers and public enterprises producing goods and services. Peru: Private sector workers in the Lima metropolitan area. Years 2000-2002. Uruguay: Average salaries. Venezuela: General wage index. LABORSTA, Canada: Manufacturing. Years 2000-2008. United States: Manufacturing. Years 2000-2008. Source: Own calculations using CEPALSTAT and LABORSTA (2012).

### Evolution of Poverty

The measurement of poverty is always controversial. Not only are there different indicators, but data availability also impedes the calculation of an indicator over time that is comparable across countries. Figure II.5 shows the evolution of poverty in the countries of the continent from two sources: World Development Indicators (World Bank) and Economic Commission for Latin America and the Caribbean (ECLAC). The measure of poverty reported by the World Bank is the one defined by people living below 1.25 USD or 2.0 USD. ECLAC measures the percentage of the population below a threshold defined by the values of food and non-food essential goods; people below the line are indigent.

During the last ten years, we witnessed an important reduction in poverty across the region, although in some countries the increase in food prices and the 2008-2009 crisis halted or even reversed the gains of the previous years. Figure II.5

shows poverty rates in 2000, 2005 and 2010, ordered by the regions of the Inter-American Conference on Social Security.

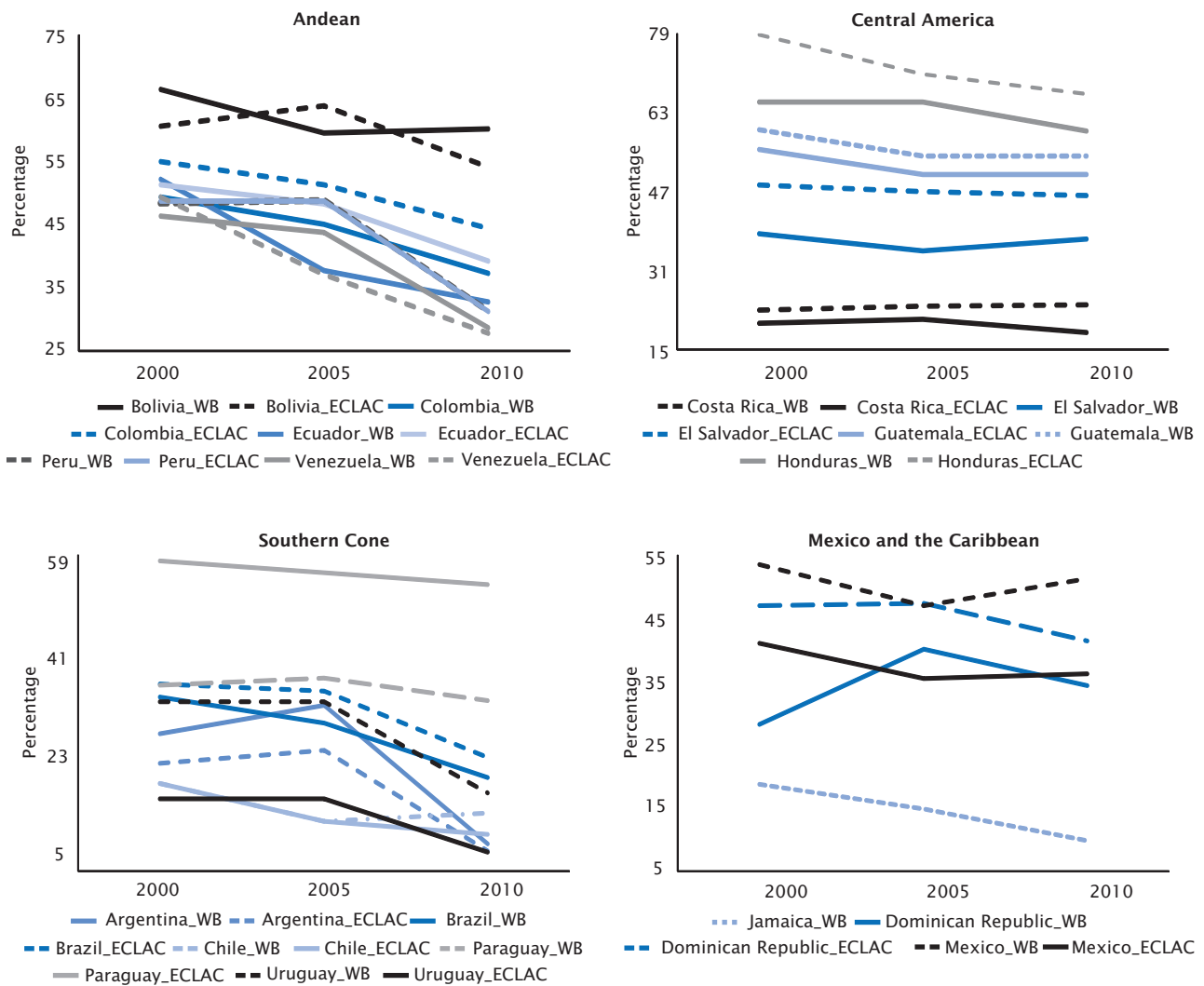
### II.3 The Individual in the Long-Run

This section provides only a summary of a rugged map relating to the long-term changes families and individuals face, which in turn define the societal context for social security programs.

#### Demographics and Family Composition

*The population of the continent is still growing.* According to population projections of several international agencies, the population on the continent continues to grow, but at lower rates. In 2000, we observed an average growth rate of 1.4%, of 1.1% in 2010, and, according to projections, 0.2% in 2050 (U.S. Census Bureau 2012a).

Figure II.5  
Poverty Index over Time



Notes: World Bank, Argentina: Urban Poverty; Bolivia: year 2007 as 2010; Brazil: year 1999 as 2000; Chile: years 2006 as 2005 and 2009 as 2010; Colombia: year 2002 as 2000; Ecuador: years 1999 as 2000 and 2006 as 2005; Guatemala: year 2006 as 2005 and 2010; Honduras: year 1999 as 2000; Jamaica: year 2007 as 2010; Paraguay: year 2007 as 2010; Uruguay: year 2006 as 2000 and 2005; Venezuela: year 2009 as 2010. ECLAC, Argentina: Urban Poverty, year 1999 as 2000; Bolivia: years 1999 as 2000; 2004 as 2005 and 2007 as 2010; Brazil: year 1999 as 2000; Chile: year 2006 as 2005 and 2009 as 2010; Colombia: year 1999 as 2000; Costa Rica: year 1999 as 2000; Ecuador: year 2004 as 2000; El Salvador: years 1999 as 2000 and 2004 as 2005; Guatemala: years 2002 as 2000 and 2006 as 2005 and 2010; Honduras: year 1999 as 2000 and 2006 as 2005; Peru: year 1999 as 2000; Dominican Republic: year 2002 as 2000; Uruguay: year 2007 as 2000 and 2005; Venezuela: year 1999 as 2000.

Source: World Bank and CEPALSTAT (2012).

The demographic process is reflected in an accelerated aging process. For most countries of the Continent, the elderly population—persons aged 65 and over—represented 8.2% of total population in 2000, 9.6% of total population in 2012 and will represent 19.3% of total population in 2050; persons aged 85 and above represented 0.8% in 2000, 1.1% in 2012, and will represent 3.4% (U.S. Census Bureau

2012a). The Americas will age, but not as quickly as Europe or Asia.

Fertility rates have steadily decreased in the last decade continuing a process that started in the second half of the XX Century; yet, fertility rates remain at above replacement levels in most countries, meaning that by mid-century there will still be population growth. The fertility rate in the Continent averages 2.25

children per woman, 14% lower in relation to the fertility rate in 2000 (PAHO 2012). Still, the fertility rate is higher than the fertility rate of the European countries at 1.51 children per woman (U.S Census Bureau 2012a).

*There will still be a younger population that can care for the elderly, but most of them will face the dual responsibility of caring for their loved ones while actively working.* Demographic data shows that there will be about 3.2 members of the population of working age (15-64 years old) per each adult over the age of 65 in the Continent in 2050, compared to the current rate of 6.9 working-age people per over-65 adult (U.S. Census Bureau 2012a), with some variations. The average labor force participation now accounts for 78% for men and 54% for women (ILO 2012). Social security needs to be prepared to support the working-age population with their dual responsibility (see CISS 2005).

*Family composition has varied over the years.* Since 2000, nuclear family households have generally decreased, while single-person households have increased. The decrease in nuclear households is reflected in other household arrangements (extended, composite and co-residential; IADB 2012).

*There is still a large percentage of orphans on the Continent with varied proportion across countries.* For example, 2% of children in Costa Rica may have lost one or both parents, and almost 10% of children in Haiti. We can deduce that being an orphan, partly due to maternal mortality is associated with poverty, a variable, which in itself is highly correlated with socioeconomic conditions (CISS 2010).

*For all variables, there are differences across regions and within countries.* These differences provide us with three groups of countries: those that show the lowest fertility rates, more aged populations and higher life expectancies—the Southern Cone and Canada; those larger countries with a higher fertility rate, young populations and a life expectancy around 76 years of age (higher in the U.S.)—United States, Mexico and Brazil; and, those

small countries of Central America, Peru, Bolivia, that still have very high fertility rates, a young population and a lower life expectancy. Haiti yields the worst results of the Continent in terms of life expectancy (62 years old) and keeps a high fertility rate (3.3 children per woman).

### **Education**

*There is a lot of variation in pre-primary enrollment rates across countries, and on average progress in the last ten years has been limited.* Pre-primary enrollment rate varies from almost 100% in Aruba, Cuba and Mexico, to between 30 to 40% in poorer countries like Dominican Republic, Honduras and Paraguay, a relative situation that has not changed significantly in the last ten years. The average pre-primary enrollment rate of the continent rose from 61% in 2000 to 73% in 2010 (World Bank 2012). Enrollment in pre-primary education is crucial especially in light of the body of evidence published regarding the importance of early childhood development for the short- and long-term social and economic outcomes of persons (see a summary in CISS 2010).

*In the American region, there is almost universal coverage of basic education.* The average coverage in basic education increased from 92% in 2000 to 93% in 2010. Also, the persistence to last grade of basic education rose from an average of 78% in 2000 to 88% in 2008. In some poor countries, there are still significant shares of school-aged children who are not in school. In Paraguay, Jamaica, and Haiti, more than 13% of primary school-aged children are not studying (World Bank 2012).

*Enrollment in secondary education has increased significantly in the last ten years.* The average secondary enrollment rate rose from 65% in 2000 to 75% in 2010. Enrollment rates have increased in the last ten years, especially in poor countries, like Dominican Republic, Guatemala and Nicaragua (World Bank 2012).

*Post-secondary education enrollment rates have increased in the last ten years.* The average post secondary enrollment rate rose from 29% in 2000 to 43% in 2010 (World Bank 2012). The increase in tertiary (or post-secondary) education coverage increases the reservation wage of individuals, and therefore may explain the decline in labor participation by young people.

### **Health and Risky Behaviors**

*Life expectancy continues to grow, and there are no signs that gains in longevity will stop for at least a few decades.* Average life expectancy grew from 72 in 2000 to 73 in 2010 (PAHO 2012). There is no consensus on whether the longevity gains will stop in the twenty-first century (see, for example, the arguments provided in Fogel 2004). Moreover, many countries lag with respect to the more developed, meaning that life expectancy shall continue inching up at the regional level.

*Citizens will live for more years, but as they age, the problem of physical and mental fragility also increases.* Social security can play an important role in providing financing and care for these persons. Regulations need to take into account that cognitive capacities of persons decrease over time (see CISS 2005 and 2011).

*There has been great progress in reducing the level of malnutrition in the past years.* The share of stunted children (height for age) under five years of age decreased (on average) from 21% in 2000 to 17% in 2008 and the share of underweight-for-age children under five years old decreased from 7% in 2000 to 6% in 2008 (World Bank 2012). Still, malnutrition rates are high in many poor countries like Guatemala and Haiti, where stunted rates remain around 30% and underweight rates are above 15%. Malnutrition is associated with poverty both between and within countries (CISS 2010).

Overweight and obesity, particularly in children, is increasing rapidly. The percentage of overweight children under five years of age increased from 7 to 8% between 2000 and 2008, and in Honduras and El Salvador the percentage almost doubled. For adults over 20 years of age, there is no standardized information prior to 2008. In addition, there are considerable differences across countries for both children and adult overweight/obesity rates. About 4% of children in Haiti and Bolivia are overweight compared to approximately 10% of children in Peru and Argentina. Overweight in adults is a serious problem in Mexico, the United States and Venezuela, affecting more than 65% of adults in those countries. Children who are overweight or obese are not only at risk for health problems, but their weight may have an adverse effect on school and labor market performance (CISS 2010 and WHO 2012a).

*Despite health gains in general, today's persons engage in riskier behavior than they did ten years ago.* Teenage pregnancy, prevalence of use of condoms during high-risk sex, alcohol consumption, and tobacco consumption are risks to children, youth and adults. Despite reliable and standardized information across countries, there is evidence that teenage pregnancy, for example, stayed at 20% from 2000 to 2010 on average, but increased in Bolivia, Colombia, El Salvador, and Peru. The same can be said about tobacco use and alcohol consumption (World Bank 2012 and WHO 2012a).

## **II.4 Conclusions**

The beginning of the twenty-first century was marked by two severe global economic crises. Nevertheless, at least in the Americas, we observe more positive or less gloomy results, while old challenges persist and new doubts about the future arise. On the positive side, employment recovered quickly in many countries after the crisis and the share of formal employment even grew, although this is not a general

trend. The performance of wages varies by country; in general, we observe positive, but in most cases modest, real gains. Finally, the first decade of the century can be remembered as a time when poverty, overall, was reduced, health improved and education coverage significantly increased.

Still, at the beginning of the second decade of the twenty-first century, there is still lack of sufficient high-quality jobs, a high level of informality, slow wage gains and a high level of poverty (the gains are far from enough). Creating good, high-quality and high-wage jobs has not been easy, but all this lays the groundwork for an important agenda for the

future. If the future is to be different from the 20<sup>th</sup> century, social security systems must be able to deliver protection to the whole of the citizenry, to coordinate effectively with the institutions in labor markets, to evolve to recognize new forms of social organization and new social ills, and to solve its long-term financing problems.

Obviously, it is simply not possible to summarize in a few pages the gamut of social risks that determine the existence of social security. The Americas Social Security Reports have attempted to deal with specific issues each year, and this chapter refers to only a few of the general issues.





**CHAPTER III  
PENSION POLICY**



## CHAPTER III PENSION POLICY

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### III.1 Social Protection in Pensions

**A**dequate social protection in pensions has become more relevant in view of the globalization process, which has increased worker uncertainty regarding job stability (CISS 2006). Contingent events such as a disability or death of the head of the family can have a considerable impact on the well-being of families. Providing adequate protection to workers, particularly to those who are most vulnerable, also includes establishing minimum rights to safety in the workplace by promoting prevention, health and hygiene (ILO 2011). The issue of pension reform has been widely debated in the last ten years. Even though most debates refer to the use of capitalization schemes to address fiscal deficits and aging, the 2012 Report (CISS 2011) focused on the age of retirement to highlight the complexity of individual and collective decisions and current uncertainty regarding the inter-relationship among technology, health and the possibility of work at older ages.

Social protection in pensions usually considers a social protection floor through welfare or non-contributive pensions provided by the government and contributive social security programs: old-age pensions to provide protection against the risk of surviving at advanced ages; disability pensions to provide protection against long-term illnesses or

accidents resulting in a significant loss of productivity; survivorship pensions to provide benefits to a worker's economic dependents in case of death; and, work risk benefits to provide protection against occupational diseases or work accidents resulting in long term disability. If, in addition, an individual is able and willing to save to receive a higher replacement rate, this third voluntary component is also a part of the social protection system.

In some countries in the Americas, such as the United States, the term *social security* refers mainly to an institution responsible for pension fund management; health insurance and workers' compensation are independently organized and managed. Still, in other countries, a single social security agency may be responsible for managing all these different types of insurance—old-age, disability, survivorship, health and work accidents and occupational diseases. Another characteristic is that some pension systems are universal while others are fragmented, as in most Latin American countries (CISS 2004).

The following paragraphs summarize what has possibly become the most generally accepted classification of pension systems into three tiers: a general benefit guaranteed by the state, a contributive general scheme, and a set of complementary, voluntary schemes. The second section of this chapter summarizes key tendencies

and debates on social security pension programs (old-age, disability, survivorship, and work accidents and occupational diseases). This review of the risk against which protection is provided addresses different aspects related to the design process, financing, management and delivery of benefits, upon which future pension program perspectives are based, which are presented in the third section.

A social security pension system, in general, includes old-age, general disability and survivorship programs. Workers' compensation usually combines pension and health elements. Traditionally, social security pensions have protected workers against the above-mentioned risks through contributive programs financed with payroll taxes. Nevertheless, considering that some people are not able to reach minimum benefit levels with social security pensions, governments are tending to provide non-contributive pensions financed with general taxes, particularly in countries where social security coverage is not universal. Table III.1 presents the characteristics of the main non-contributive pension programs in the region; most provide protection to older adults although some countries also provide benefits for the handicapped or the disabled.

To illustrate the three components or tiers of social protection in pensions in different countries, we refer to Figure III.1 elaborated by OECD (2011a), which presents a taxonomy of social protection in old-age pensions. The first-tier, on the left, provides social assistance or safety nets through transfers or non-contributive pensions for the poorest or most vulnerable population, possibly requiring a means test to prove they are in a condition of need. The second-tier (often identified with social security) represents contributive programs, which may be either publicly managed (DB, points or notional accounts) or privately managed (DB or DC). The third-tier, (on the right) consists of voluntary pension savings aimed at improving social security replacement rates by providing tax incentives.

## III.2 Tendencies and Debates

This section briefly reviews relevant aspects regarding the organization and design of pension programs providing old-age, disability, survivorship, and work accident and occupational disease related pensions in order to assess the prospects for these social security programs based on these tendencies.

### ***Shift in Paradigm in Pension Program Organization***

The organization of social security pension programs has been oriented, in a similar fashion to health programs, towards breaking away from vertical integration in three key functions: financing (affiliation and collection, financing and allocation), management (managing and handling pension funds), and delivery of benefits (CISS 2007). Reforms to old-age pension systems that have made competition among pension fund managers possible are an example of decentralization in benefit management and delivery.

### ***Old-Age Insurance***

How can pension systems balance redistributive and individual capitalization elements? This seems to be the question to be answered after a series of debates on the advantages and disadvantages of choosing a pay-as-you-go or an individual capitalization pension system (Kotlikoff 1995, 1998, Mesa Lago 2004, 2007, Mulligan and Sala-i-Martin 1999a and b, Kay and Sinha 2008 and Barr and Diamond 2008). On one hand, financial crises have made it clear that neither pay-as-you-go nor individual account systems are immune to such events (CISS 2009) and that pension benefits can be affected. On the other hand, the progression of the process of demographic transition towards population aging will eventually lead pay-as-you-go systems to look for capitalization elements, either individual or collective, for financing.

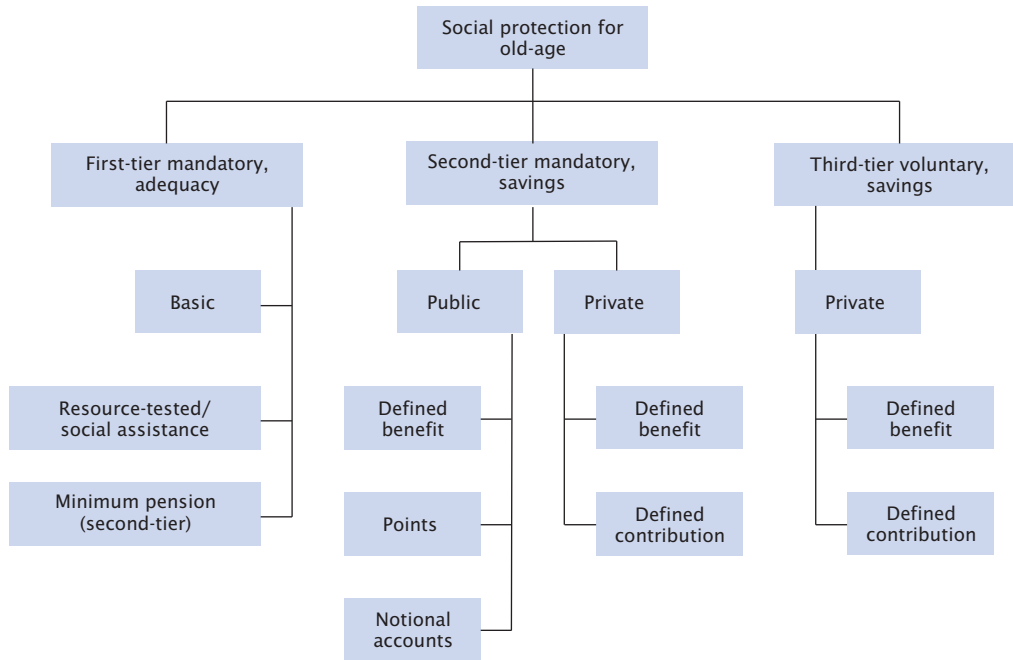
Table III.1  
Minimum Pension in Selected Countries, 2012

Country	Program	Monthly benefit		Minimum wage (USD)	Benefit/ Minimum wage
		Local currency	USD		
Bolivia	Renta Dignidad <sup>1/</sup>	150.0	21.8	145.6	0.2
	with another pension without another pension	200.0	29.1		0.2
Brazil	Mandatory Social Security System Minimum Pension	1,000.0	145.6		1.0
	Renda Mensal Vitalicia Benefício de Prestação Continuada	622.0	303.3	303.3	1.0
Colombia	Individual Savings Regime Guaranteed Minimum Pension	532,500.0	302.9	302.9	1.0
	Pension Contribution Subsidy Program	532,500.0	302.9	302.9	1.0
	Older Adult Social Protection Program	532,500.0	302.9	302.9	1.0
Costa Rica	Disability, Old Age and Survivors Scheme Minimum Pension	115,331.0	236.4	482.2	0.5
Chile	Minimum Pension Guaranteed by the State	111,855.4	225.9		0.6
	under 70 years of age	122,305.4	247.0		0.7
	70 to 75 years of age over 75 years of age	130,495.8	263.5	367.5	0.7
Dominican Republic	Basic Solidarity Old Age Pension	78,449.0	158.4		0.4
	Basic Solidarity Disability Pension	78,449.0	158.4		0.4
	Contributive Regime Guaranteed Minimum Pension	6,035.0	156.5	256.8	0.6
El Salvador	Subsidized Contributive Regime Guaranteed Minimum Pension	6,933.5	179.8		0.7
	Subsidized Regime Solidarity Pension	4,086.0	106.0		0.4
Mexico	Minimum Old Age, Disability and Survival Pension	143.6	143.6	227.1	0.6
	Guaranteed Minimum Pension, IMSS	1,894.8	137.6		1.0
	Guaranteed Minimum Pension, ISSSTE Non-Contributive Program "70 and Over"	3,789.7	275.3	137.6	2.0
Peru	Private Pension System and National Pension System Minimum Old Age Pension	500.0	36.3		0.3
		484.2	185.0	286.6	0.6
Uruguay	Non-Contributive, Old Age and Disability Pension Program	5,415.0	258.2	343.4	0.8

Note: 1/ The annual benefit was converted to monthly periods for standardization purposes.

Source: Bolivia, Ministerio de Economía y Finanzas & Ministerio de Trabajo, Empleo y Previsión Social (2012); Brazil, Ministério da Previdência Social & Ministério do Trabalho e Emprego (2012); Colombia, Secretaría del Senado, "Ley 100 de 1993" & Ministerio de Salud y Protección Social (2012); Costa Rica, Caja Costarricense de Seguridad Social & Ministerio de Trabajo y Seguridad Social, Departamento de Salarios (2012); Chile, Superintendencia de Pensiones & Dirección del Trabajo (2012); El Salvador, International Social Security Association (2012); Mexico, Secretaría de Desarrollo Social & Comisión Nacional de los Salarios Mínimos (2012); Peru, Superintendencia de Banca Seguros y AFP & Ministerio de Trabajo y Promoción del Empleo (2012); Dominican Republic, "Ley 87-01", Consejo Nacional de Seguridad Social (2012a); Uruguay, Banco de Previsión Social (2012a).

**Figure III.1**  
**Taxonomy of Old-Age Pension Schemes**



Source: OECD (2011a).

Based on the analysis of old-age pension systems in CISS (2011) the fact that Costa Rica, Panama and Uruguay already have general mixed old-age pension schemes where social security pensions (second-tier) include both a defined benefit (DB) and a defined contribution (DC) is surprising. In addition, Guatemala and Honduras and several other countries with DB social security pensions are currently looking for options to include individual capitalization or DC elements in program design. Another interesting element is that in a number of countries with DC old-age pensions (Chile, Mexico, El Salvador, Dominican Republic, Bolivia and Peru) integration of second-tier social security pensions with pensions under social assistance schemes or non-contributive pensions has been developing.

Undoubtedly, LAC countries are shifting towards convergence in the use of capitalization and redistributive elements in pension systems in the region and old-age pension scheme designs including both a solidarity component that provides a protection floor (first-tier) and a benefit originated

from a component that provides insurance and income-related benefits (second-tier). Nevertheless, there is a need to encourage voluntary savings, the third-tier, through adequate regulation and the dissemination of information on the advantages of having a savings oriented culture (CISS 2008).

All over the world, reforms to old-age pension programs have been the center of attention over the last few decades due to their high proportion of public spending required to fund them (CISS 2003, 2008). For pension programs to be financially sustainable, the country's economic environment is not the only important factor; this can be seen, for example, by looking at fiscal unbalances and unemployment levels (CISS 2008, 2009). Fund investment strategies and institutional policies regarding the use of reserve funds are key elements to achieving financial sustainability in these programs. Pension program management responsibilities should ideally use timely information (financial and actuarial studies based on microdata) in the decision making process.

The organization and design of social security institutions also determines the way funds are financed and managed (CISS 2007). Pension system design in LAC countries has to be improved, particularly the contributive portion (second-tier), in order to allow temporary and self-employed workers to contribute and improve replacement rates according to job characteristics. In addition, providing more than a minimum pension for those who perform non-remunerated work such as caretakers of sick, disabled or elderly persons should be considered.

### ***Disability and Survivorship Insurance***

Disability and survivorship insurance were traditionally managed together with old-age pensions because the benefits provided by these types of insurance represented a percentage of old-age benefits. It was only when capitalized old-age pension schemes in a number of countries substituted pay-as-you-go schemes with individual capitalization schemes that the mechanisms to manage general disability and survivorship insurance were also modified. In countries that provide old-age, second-tier pension benefits through individual capitalization systems, general disability, and survivors insurance have also usually been decentralized to private providers. The more common model is based in the inclusion of the cost of these benefits in the rates charged for the administration of retirement funds.

Differences in terms of capitalization and pay-as-you-go schemes operating in LAC countries are presented in Table III.2. Specifically, it shows the particular characteristics of countries with DC-type old-age pension schemes, such as the individual capitalization and collective capitalization components in Costa Rica. Undoubtedly, a key issue in the design of old-age pensions in purely DC systems is adverse selection, since individuals with poor health or working in a dangerous profession would be willing to pay higher rates to receive

disability and survivorship pensions. Other prominent issues in the design of disability insurance, discussed in more detail in CISS (2005, 2008), are: the difficulty in identifying extent of disability due to the possibility of partial recovery, medical uncertainty or behavioral changes; placing more emphasis on prevention and rehabilitation since future populations will live and work longer; and, with regard to the delivery or payment of disability benefits, to reduce litigation risk, certain cases could be handled differently to reduce the wait time for those who are most vulnerable, since the determination of degree of disability is required (and ideally, of the individual's possibilities to continue generating income.)

A striking fact in survivorship insurance is that in some countries the benefit for orphans may be quite low especially when the number of children is large, because the total amount is divided among the number of children according to social security legislation (Mexico, Guatemala, among others). In such cases, the proper thing to do would be to provide a fixed amount per child since large families tend to be the most unprotected. Having adequate information on family dynamics in both disability and survivorship insurances (change in marital status for widowed individuals, the exact age of each child) is a basic input to promote financial sustainability because it allows proper identification of individuals who are no longer eligible to receive benefits.

### ***Workers' Compensation***

Workers' compensation (WC) is sometimes integrated in general disability and old-age programs while other countries have specialized agencies to regulate and fund these benefits. In general, a single and usually public centralized fund operates, but competition among funds is sometimes allowed (See Table III.2). In some countries, there is an integrated program or agency managing the schemes for short-term work-related illnesses and accidents as well as long-



term (pension) benefits, and there are also differences in the integration of monetary and health benefits.

Contributions paid by employers to WC are based on their accident history, so having adequate information records is necessary to facilitate administrative processes related to health insurance. In addition, companies can be monitored over time and review premiums paid by each company based on their accident history and preventive activities carried out; otherwise, risk would not be properly spread within the social security institution.

WC is usually related to the Ministries or Departments of Labor responsible for labor regulation and with the Judiciary, which is responsible for the resolution of conflicts and litigations regarding the legitimacy of benefit payments. CISS (2007) indicates the need to balance the roles played by regulators (Labor Ministries), the Judiciary (including labor courts), and social security institutions.

### III.3 Perspectives

Changes oriented towards the acceptance of a public-private mix in program management and in the delivery of benefits can be identified as a main development in the operation of social security pension programs. The State has always remained as a main guarantor of financing through two main processes. One is the enforcement of collections, and the other is the provision of guarantees to at least minimum pensions.

To improve pension program financing, financial sustainability must be ensured to meet benefit payments. Undoubtedly, financial and actuarial studies are very helpful in examining future program solvency. However, without proper pension fund management, reserves may be extinguished

earlier than expected. Unlike reformed systems where pension fund regulation has been a key reform issue, in pay-as-you-go systems there is a risk that pension fund reserves may be considered a part of government revenues. To solve the issue of inadequate pension fund management, it has been suggested that governments should apply general accounting principles to register and recognize liabilities identified in financial or actuarial studies. In addition, the investment of reserve funds should be supervised to make sure investments are not being used to finance unprofitable programs or projects that may lead to defunding pension programs. Investment of pension funds in pay-as-you-go systems should be subject to the same regulations that apply to financial institutions with the purpose of maintaining adequate reserve levels and transparent accountability before the public sector. The 2008 Report dwells on these issues.

The last decade witnessed a qualitative change. Advances in information technologies that had been adopted to varying degrees became ubiquitous and integrated into social security administrations. While not yet fully adopted, the possibility of on-demand registration, affiliation, and collection of contributions is open to all agencies (see 2008 Report). Only then is it possible to know the family situation, employment status, and the record of payments and benefits of any worker or his dependents at any moment in time. Having updated information systems not only promotes efficiency in administrative processes, but it also facilitates the operation of the social protection system as a whole. Pension programs are interrelated to other social security programs such as health insurance or public non-contributive programs, so information generated by social security agencies is very useful for other agencies and vice versa. Thus, it is easier to monitor government benefit payments made to the most needy when the management of non-contributive benefits (first-tier) is supported by a general contributory scheme (second-tier).

Table III.2  
Type of Disability, Survivorship, Work Accidents and Occupational Disease Insurance, 2011

Country	Type of disability and survival insurance	Institution responsible for disability and survival insurance	Type of insurance against work accidents and occupational diseases
Argentina	DB	National Social Security Administration ( <i>Administración Nacional de la Seguridad Social</i> )	<i>Private.</i> Employers are allowed to self-insure as long as they are able to prove economic and financial solvency to face their workers' working risks and ensure the provision of required medical services. Those who are not able to accredit both requirements are obliged to purchase insurance against work accidents and occupational diseases from an insurance provider; it will be financed by a monthly employer fee (Law 24557; Article 3, 23)
Bahamas	DB	The National Insurance Board	<i>Public.</i> The National Insurance Board ensures income replacement in the event of work accidents and occupational diseases through this employer-funded program
Barbados	DB	National Insurance Office	<i>Public.</i> The National Insurance Office is responsible for managing workers' compensation
Belize	DB	Social Security Board	<i>Public.</i> The Social Security Board acts as program manager. Coverage excludes informal workers; individuals who work less than 8 hours a week and the military
Bermuda	DB	Department of Social Insurance	<i>Private.</i> Employers cover the cost by delivering the benefits directly or paying the insurance premium
Bolivia	DC	Public Insurance Entity ( <i>Entidad Pública Aseguradora</i> ): Insurance companies will manage disability pensions and the survival pension program	<i>Private.</i> The Insurance Companies ( <i>Entidades Aseguradoras</i> ) manage disability and survival insurance and insurance against work accidents and occupational diseases
Brazil	DB	National Social Security Institute ( <i>Instituto Nacional da Seguridade Social</i> )	<i>Public.</i> The National Social Security Institute manages cash benefits under the supervision of the <i>Ministério da Previdência Social</i> . Federal, state or municipal institutions manage medical benefits. Benefits are financed by employers
British Virgin Islands	DB	Social Security Board	<i>Public.</i> Managed by the Social Security Office
Canada	DB	Human Resources and Skills Development Canada	<i>Semi-Public.</i> Employers cover the cost. Contributions may vary by industry and risk level. In some provinces, large companies are allowed to self-insure

Table III.2 (continued)

Country	Type of disability and survival insurance	Institution responsible for disability and survival insurance	Type of insurance against work accidents and occupational diseases
Chile	DC	Pension Fund Manager ( <i>Administradora de Fondos de Pensiones</i> ): As provided by Articles 59 and 59 bis, in relation to Article 54 of D.L. 3.500, 1980, Pension Fund Managers are responsible for disability and survival pensions as well as for contributions outstanding in their individual accounts; to ensure financing, they must purchase, through public tender, insurance as a whole from one or more life insurance companies; they should be completely covered	<i>Semi-Public</i> . Insurance against work accidents and occupational diseases will be managed by: a) The Services, the Regional Ministerial Health Secretariats ( <i>Seremi</i> ) and <i>Instituto de Normalización Previsional (INP)</i> , with respect to workers in companies not affiliated with a Mutual Organization; b) Mutual Organizations created in compliance with the law and their Organic Bylaws, with respect to workers in companies that are members or adherents of Mutual Organizations; and, c) Deputy Managers. <i>INP</i> will provide medical and monetary benefits as well as pensions for workers in companies with delegated management
Colombia	(parallel) DB DC	Social Security Institute ( <i>Instituto de Seguros Sociales</i> )  Pension and Unemployment Fund Managers ( <i>Sociedades Administradoras de Fondos de Pensiones y de Cesantía</i> ) contract disability and survival insurance management with insurance providers	<i>Semi-Public</i> . The Social Insurance Institute and life insurance providers authorized by the Banking Superintendence manage the working accident and occupational disease program nationwide
Costa Rica	(mixed) DB and DC	Costa Rican Social Security Administration and Pension Superintendency ( <i>Caja Costarricense de Seguridad Social and Superintendencia de Pensiones, Supen</i> ): In addition to the Pay-as-you-go System, there is a Complementary Pension System comprising a mandatory and a voluntary scheme. Both modalities include individual accounts. Managers may offer complementary protection against disability or death, they must purchase insurance from <i>Instituto Nacional de Seguros</i> ; for educational-sector workers, the insurance comes from <i>Sociedad de Seguros del Magisterio Nacional</i>	<i>Private</i> . Employers are responsible for purchasing insurance from a public provider (National Insurance Institute)
Cuba	DB	Ministry of Labor and Social Security ( <i>Ministerio de Trabajo y Seguridad Social</i> )	<i>Public</i> . The work-accidents program is managed by government agencies under the Office of Social Assistance and Social Services and the National Social Security Institute attached to the Ministry of Labor and Social Security
Dominica	DB	Dominica Social Security	<i>Public</i> . The Office of Social Security of Dominica, managed by the Social Security Board, manages the social security program
Dominican Republic	DC	Pension Superintendency ( <i>Superintendencia de Pensiones</i> )	<i>Private</i> . The cost of insurance against work accidents and occupational diseases will be fully covered by employers. Work risks will be the responsibility of National Health Insurance and Health Risk Managers ( <i>ARS</i> , which may be public, private or mixed), and Health Service Providers ( <i>PSS</i> , which are private). Supervision is carried out by <i>Superintendencia de Salud y Riesgos Laborales (SISALRIL)</i>
Ecuador	DB	Social Security Institute ( <i>Instituto Ecuatoriano de Seguridad Social</i> )	<i>Public</i> . One of the missions of the Ecuadorian Social Security Institute (decentralized public entity) is to protect the population against work risks (Article 17)

Table III.2 (continued)

Country	Type of disability and survival insurance	Institution responsible for disability and survival insurance	Type of insurance against work accidents and occupational diseases
El Salvador	DC	Pension Fund Managers ( <i>Administradora de Fondos de Pensiones, AFP</i> ): The insurance industry participates in the pension system. <i>AFPs</i> must purchase disability and survival insurance for <i>AFP</i> affiliates and their families from personal insurance providers. The purpose of the insurance policy is to ensure payment of disability and survival pensions in case of illnesses or accidents resulting during public tender, in accordance with Pension Superintendency regulations. <i>AFPs</i> contract this service annually, in accordance to regulations by <i>Superintendencia de Pensiones</i>	<i>Public</i> . Professional risks are covered by the Social Security Institute, which is also responsible for sickness insurance
Granada	DB	National Insurance Scheme	<i>Public</i> . The National Insurance Office provides work injury medical and economic benefits
Guatemala	DB	Guatemalan Social Security Institute ( <i>Instituto Guatemalteco de Seguridad Social</i> )	<i>Public</i> . Work injury benefits are managed as part of the pension and sickness, maternity and accident regimes. The Guatemalan Social Security Institute manages the regime
Guyana	DB	Ministry of Labour, Human Services, and Social Security	<i>Public</i> . The Office of Social Insurance provides economic benefits and medical assistance in case of work injuries
Haiti	DB	National Office of Old-Age Insurance	<i>Public</i> . The Institute of Social Security's Office of Work Accidents and Sickness and Maternity Insurance manages the Work Injury program
Honduras	DB	Honduran Social Security Institute ( <i>Instituto Hondureño de Seguridad Social</i> )	<i>Public</i> . The Honduran Social Security Institute provides work injury benefits
México	DC	Mexican Institute of Social Security ( <i>Instituto Mexicano del Seguro Social</i> )	<i>Public</i> . <i>Instituto Mexicano del Seguro Social</i> which is managed by a general assembly, a technical board, a control committee and a general director, manages the work accidents and occupational disease program through regional and local boards
Nicaragua	DB	Nicaraguan Social Security Institute ( <i>Instituto Nicaragüense de Seguridad Social</i> )	<i>Public</i> . The Nicaraguan Social Security Institute manages the work injury program
Panama	(mixed) DB and DC	Social Security Institute ( <i>Caja de Seguro Social</i> )	<i>Public</i> . Employers have the obligation to insure workers with a public agency
Paraguay	DB	Social Security Institute ( <i>Instituto de Previsión Social</i> )	<i>Public</i> . The Social Security Institute provides work injury medical and economic benefits
Peru	(parallel) DB DC	Office of Social Security Normalization ( <i>Oficina de Normalización Previsional</i> ) Superintendency of Banks, Insurance and PFMs ( <i>Superintendencia de Banca, Seguros y AFP</i> ): Contracts with insurance providers for disability and survival insurance management	<i>Semi-Public</i> . Complementary insurance against work accidents and occupational diseases provides health benefits or medical assistance and economic benefits. Health benefits are provided by <i>Essalud</i> or by public or private health providers ( <i>EPS</i> ). Economic benefits are insured by employers with insurance providers or with the Office of Social Security Normalization ( <i>ONP</i> ). The Peruvian Social Security Institute ( <i>IPSS</i> ) only provides health services for work accidents

Table III.2 (continued)

Country	Type of disability and survival insurance	Institution responsible for disability and survival insurance	Type of insurance against work accidents and occupational diseases
Saint Christopher and Nevis	DB	Social Security Board	<i>Public.</i> The Social Security Board manages the work injury program
Saint Lucia	DB	National Insurance Corporation	<i>Public.</i> The National Insurance Corporation provides cash benefits (with a benefit ceiling) for work accidents and occupational diseases
Saint Vincent and the Grenadines	DB	National Insurance Scheme	<i>Public.</i> The National Insurance Board only provides benefits for work accidents or occupational diseases
Trinidad and Tobago	DB	The National Insurance Board	<i>Public.</i> Work injury medical and economic benefits are provided by the National Insurance Office
United States	DB	Social Security Administration	<i>Private.</i> Insurance against work accidents and professional risks is mandatory (optional for employers in some states), through public or private insurance providers (according to state) or employers may self-insure
Uruguay	(mixed) DB and DC	Social Security Institute and Pension Fund Managers ( <i>Banco de Previsión Social</i> and <i>Administradoras de Fondos de Ahorro Previsional</i> ): Disability and survival benefits are financed by each Pension Fund Manager; collective disability and death insurance is purchased from insurance providers	<i>Public.</i> The State, Departmental Governments, Autonomous Entities and the rest of the public entities are obliged to insure all personnel with the State Insurance Bank. Insurance costs are covered by employers according to risk (Article 5). The State Insurance Bank must ensure that all non-insured employers build the capital required to reimburse expenses (Article 8)

Source: Own elaboration based on SSA (2011).

Another advantage of having updated information on affiliates, dependents, pensioners, work histories and records of contributions paid and benefits received, is that it allows higher quality economic and financial evaluations as well as performance evaluations of agencies responsible for the programs. We do not necessarily refer to sophisticated information, but to simple statistics such as the number of orphans or disabled individuals, information which is usually unavailable. However, solving the problem of lack of basic information is a starting point from where we can advance towards recording more detailed information such as, for example, the reason why a disabled person visited his health center.

In the organization of pension programs we can see a paradigm shift, similar to health programs, where management functions and the delivery of benefits tend to be more decentralized and include public-private participation in an attempt to provide a more efficient service to the insured.

Reforms to old-age pension schemes in LAC countries started in the 80's with the Chilean reform, after which several countries substituted pay-as-you-go schemes for defined contribution and individual capitalization schemes. In these countries, disability and survivorship programs were also decentralized so fund managers and private insurance providers are responsible for providing protection in these two areas. Sometimes, debates on pension systems lean towards dichotomy positions but what we really see is that successful systems all over the world are able to combine elements of public and private delivery of benefits, of collective and individual savings, and that, in general, transparency and good governance are prerequisites for any option to be successful.

In old-age pension programs, the most important in terms of the size of managed funds, there is concern over achieving high investment returns combined with manageable and prudent risk. This has led pension systems to look for a balance between pay-as-you-go and individual capitalization based financing options. In line with the above, old-age pension schemes are tending to integrate into their design a protection floor (first-tier non-contributive pension) and a contributive pension (second-tier). If possible, voluntary savings should also become an important element to increase rates of replacement through voluntary savings (third-tier).

The analysis of the processes involved in pension program management indicates that financing, administration and the delivery of benefits can be significantly improved; mainly through an adequate design capable of efficiently integrating pensions with other social security programs and providing incentives aligned with each party involved in the processes; as well as by generating timely, updated information on affiliates, their dependents and pensioners, their individual and work characteristics and records of contributions paid and benefits received.

Pension programs face new challenges ahead. The situation of uncertainty that prevails in labor markets and the lack of well remunerated quality jobs require new solutions to ensure affiliates are covered by social security. This should be accompanied by proposals regarding the solution to financing issues in pension programs owing to changing worker characteristics: increased temporary work, potentially significant unemployment periods, and greater need to take care of sick persons and persons that require long-term care at home.



**CHAPTER IV**  
**FAMILY PROGRAMS**





## CHAPTER IV FAMILY PROGRAMS

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### IV.1 Social Protection for Families

**F**amily programs encompass benefits that have as a common denominator a trigger event that alters the family structure or the relationships among family members. These programs are implemented to assist parents to better combine their responsibility in the labor market and in the household as caregivers to children or older adults; to foster women labor force participation; to provide resources needed for a good and equal development of children; and to provide support to vulnerable members of the family. In general, family programs provide benefits for families to have more freedom with respect to personal decisions that affect family structures (OECD 2011b). Benefits are more often monetary, but in important cases they are linked to in-kind benefits. Within a social security environment, the more commonly used term to describe this class of benefits is "family allowances" (FA), which include the conditioned cash transfer programs (CCT) that have grown significantly in the region.

Family programs recognize that events that change the family structure or the relationships among its members can create conditions of risk that call for collective support. The vulnerable members of families may need increasing care. Elderly loved ones suffer periods of fragility, physically or mentally, and require on-demand care.

Children need large and high quality investments to promote their health and cognitive and non-cognitive abilities, whether or not they have a working mother. Also, the role of working-age family members as caregivers can generate undue stress. Women often end up as the caregivers for children or for frail family members. Additionally, urbanization and social dynamics means families are often split, translating into households with fewer potential caregivers, and more vulnerable members.

Family programs are diverse in their financial and organizational solutions. Sometimes the participation of the State is limited to setting regulations, while in other cases it involves also financing programs or even the final provision of services through public agencies. The portfolio of programs in each country varies significantly in response to demographic characteristics, labor market features and outcomes, and the role assigned to the government in the economy and to cultural and social heritages.

By program type, there are four main groups of family programs: family allowances, child care, maternity, and long-term care (LTC).

*Family allowance* encompasses diverse benefits per child (until certain age), at birth, at marriage, at death, and other benefits granted when a specific event occurs. In this group we include the CCT, which are FAs with specific requirements

related to child's attendance at school and health center. FAs in an unrestricted version (cash for families in the presence of a child) are common in developed European countries. In the Americas, FAs are more often linked to pensions or to health insurance, as well as to special programs that are means-tested, focused and conditioned. Nevertheless, some countries are providing universal child benefits (Argentina, Uruguay), and others have widened the social protection net substantially through CCT.

The second group is *child care* benefits, which in turn can be divided into those provided by institutional child care centers and non-institutional care with special focus in early childhood development. Some child care programs provide financing to families, while others include substantial provision and regulation. One experience worth revisiting is the Caribbean Child Support Initiative, now the Foundation for the Development of the Caribbean Children (FDCC), that had been implemented with success in Jamaica, Dominica, St. Lucia, St. Vincent and the Grenadines, Grenada and Belize, and has been extended to 14 countries of the region. The FDCC is an organization that provides an early childhood development and family support program aimed at strengthening the care environment for young children. The FDCC aims to motivate parents to adopt a more interactive style of care, which leads to improved cognitive and social development among young children growing up in disadvantaged situations.

The third group of benefits consists of *maternity programs* which include the wage subsidy that redistributes across employers the cost of the wage subsidies for new mothers, and maternity leave so the mother of a newborn, and sometimes the father, can enjoy a period away from work without penalization.

Finally, *Long-Term Care* programs comprise a series of services designated for persons that are not fully capable of self-care on a long-term basis, services aimed to minimize, restore, or compensate

for the loss of independent physical and mental functioning. LTC benefits can be for the disabled or for the caregivers. The implementation of LTC programs faces two important hurdles. First, it requires new sources of financing, which can be based on general taxation, but most probably will follow the funding scheme of health insurance (i.e., payroll contributions; see CISS 2005). Second, given that the region is still very young, there will be a significant number of potential caregivers within families. A main issue is that there is no such thing as the average family, and while for some the provision of care may be shared by several family members, in many cases families are living separately, and a collective solution may be required.

*The Americas Social Security Report 2006* analyzed in detail the LTC programs. The 2011 Report (CISS 2010) was totally devoted to children, and thus analyzed in detail family allowances, child care, maternity subsidies, and problems of youth employment. There are aspects we would like to stress in this chapter depending on the group of people toward which programs are targeted: need for collective support, programs design, and administrative issues for children and elderly in need of LTC, and how to provide support to young people in skills training and employability.

## IV.2 Tendencies and Debates

### *Children*

Social security programs often have children as beneficiaries, sometimes even as the main beneficiaries independently of the status of their parents. For example, some health insurance schemes have special provisions to cover children who would be otherwise uninsured. A question that is not always easy to answer, as it might seem in casual conversation, is the definition of what is a child. Should an age criteria even be set in the first place? Should there be some flexibility depending on whether the person has moved into the labor market, into marriage, into other "adult" endeavors?

To provide a more substantive argument, our society holds that it is a communal responsibility to care for the welfare of children, including the provision of opportunities to develop their spiritual and physical potential. Social security has to do with solidarity, but the core pension programs rarely if ever state that the collective society is responsible for providing the same pension to each person. Yet, when referring to children, our societies do believe that absolute equality in educational opportunity, in access to healthcare, and in other variables is a collective responsibility. On this basis, *the Americas Social Security Report 2011* took the view that children are the young people for whom society holds itself responsible of guaranteeing rights. The boundary of childhood and later stages in life is not set in stone and actually has several dimensions: society may find absolute agreement in precluding permanent damage to a child due to lack of health insurance, but may only be willing to provide insurance to adolescents in the transition from school to work if they agree to participate in a training program and continue to search for a job. Consequently, the 2011 Report (CISS 2010) included entries related to very small and even unborn children, and to young individuals entering the labor market.

The 2011 Report stressed that young people in the Americas live in a world that has changed a lot in a short period of time, but is still full of promise and challenge. Compared with only two or three previous generations, we see that children in the Americas live less often in nuclear families, that are smaller and that often have the mother as single or main breadwinner; and more often in extended families; they live in cities, whereas until the seventies the share of rural population was still relatively high; they are much more educated although there is a perception that the quality of education they receive may not always be as high as desired; they do not expect to marry as children, many will marry at the "old" late-twenties, and a fair share will never form a family with children (although they will have significant long-term personal relationships); few

expect a labor career free of the hassle of job changes, and they are expected to learn new abilities continuously, if they are to survive as successful workers.

One challenge that has grown across the region is how to provide an adequate transition from school to work, and how to provide social protection over that bridge. Nearly every country in the Americas has worked to address the youth employment challenge. Many of these efforts have been translated in programs for promoting youth employment, but many of them have been limited in time or reach. Most of these initiatives aim to ensure that youths leave the education system with the skills required in the labor market, combining measures ranging from education and training, to support for gaining experience and entrepreneurship development. Yet, the sheer size of the problem and the complex situation of many youths make it hard to find a "best practice" to be generalized internationally. However, there are useful partial experiences. Most government interventions for promoting employment for young people in the region have been targeting youth who have become disconnected from the educational system, and are not working or planning to return to training—the "disconnected youth" or "at-risk youth". According to Cunningham et al. (2008), youth-at-risk constitute more than half of the total population aged 12-24 in Latin America and the Caribbean, a condition confirmed by the analysis in the 2011 Report.

### ***Disabled Elderly***

The 2006 Report (CISS 2005) showed that a lack of coverage of LTC programs determines that much of the pressure to supply services falls on health systems. This is not a satisfactory solution because LTC is not really healthcare, which requires different specialized personnel, and involves a different pattern of financing and a different set of criteria to determine need. Hospitals face steep costs of

attending persons with disabilities that enter emergency rooms or occupy beds due to lack of proper LTC supply. Figure IV.1 shows a projection of the share of households that will have an older adult requiring LTC over the next few decades. The Report also analyzed the possibility of providing such care through other household members. In any case, the social challenge will affect all countries of the Americas.

### IV.3 Perspectives

Family benefits will continue to be a collection of programs and regulations where the role of the State will vary depending on the specific benefit and country. Still, it will be very important that each benefit be part of a structured portfolio designed as part of an overall strategy for the family, strategy that balances State and family responsibilities. Also, family benefits should be thought in conjunction with other social policies, such as those related to education, health insurance and pensions, because the goal is to provide overall stability to the family.

#### *Programs for Children*

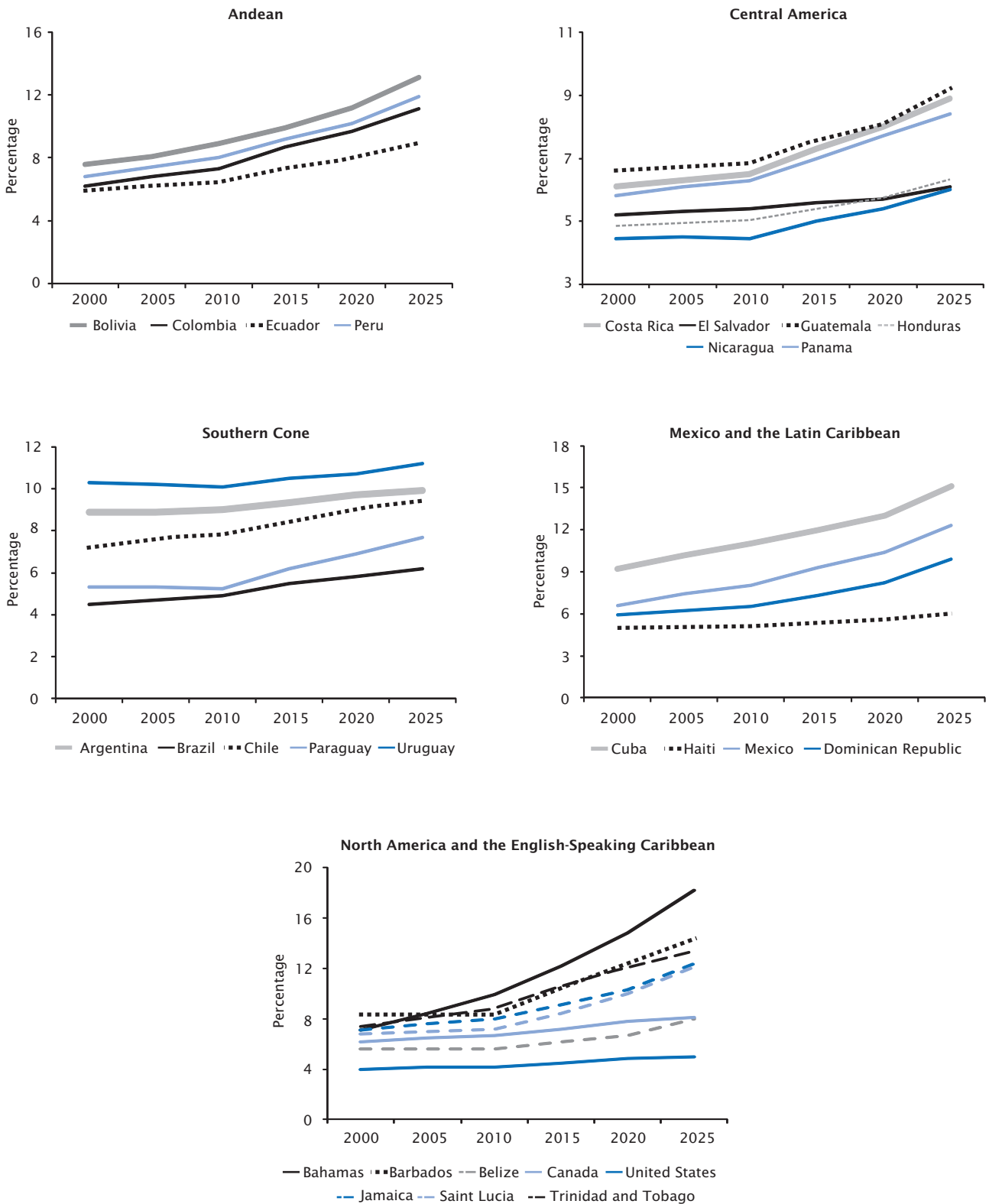
There is overwhelming evidence about the enormous benefits to young children as a result of providing care. At the same time, child disability rates are clearly underestimated in many countries simply because of the scarcity of programs to attend them. Moreover, while the health status of children has clearly improved across the region in recent decades, new risky behaviors prevail, obesity, drug-addiction, broken families, and inequity in access to education being only some of them. In this context, in addition to the traditional programs of FA, maternity leave and subsidy, and child care centers, many countries and their social security agencies are developing new benefit schemes to support early childhood care and special needs. These new approaches represent basic financial

changes and require new perspectives on design, as will be clarified in the following paragraphs. First, more resources will be devoted to little children. Second, while general disability programs are usually defined for workers, and while children of insured workers often receive health care, it has been recognized that they also need monetary support.

On the design of programs, social security agencies should adapt to conform to new realities and information. In particular, agencies should be more involved in verifying the environment of children and elderly to ensure that benefits reach them, and implement preventive and corrective programs, while always respecting the right of families to make decisions within the privacy of their own household. Benefits should be flexible so they can be adapted to characteristics of each family, its context and needs. In particular it should be guaranteed that child benefits respond to the periods when they are needed the most (sensitive and critical periods in the literature of early childhood development, see CISS 2010). Policy makers should also be aware that a successful program is defined basically by its ability to relate every family's needs with a heterogeneous supply of childcare and LTC services. For them the aim should be to provide the financial resources that facilitate this match. Maternity subsidies programs should also satisfy flexibly particular needs of mothers and fathers.

Key variables such as fertility, poverty, pregnancy, schooling outcomes, employment, and social security protection influence the situation in which young persons are living. One of the main problems faced by most countries in the Americas is that systems lack strong connection between education and work. A significant share of boys and girls begin to abandon formal schooling by ages 14-17, and do not have jobs to provide adequate learning opportunities and on-the-job training. In this context, social security agencies have a window of opportunity to reform the existing programs for

Figure IV.1  
 Projected Percentage of Households with One Elderly Member Requiring LTC:  
 Latin America and the Caribbean<sup>1/</sup>



Note: 1/ It is assumed one elderly member in need of LTC per household.  
 Source: UNHABIT (2012), OMS (2012b) and ONU (2012).

young people or create new ones to make them more effective. Programs should incorporate gender issues, recognizing the different social risks faced by males and females. Teenage pregnancy rates are still too high in several countries and are associated with maternal and child poverty. A main effort by affected countries and the international community must be directed to almost eliminate the incidence of low education levels, and continue affecting a significant increase in the incidence of medium education levels. For higher grades, countries must reform education and labor regulations to facilitate on-the-job training and mixed school-work programs. Social security rules regarding affiliation, contribution and benefits can be adjusted to facilitate the use of school-work and on-the-job training for teenagers. There is a window of opportunity and many things can be done to improve youth well-being. Moreover, while some actions lie directly within the social protection field, other policies may be implemented by other government bodies, such as labor and education ministries. In any case, each country's objective should be to implement a comprehensive and integrated approach to improve youth well-being. A balanced portfolio of policies and institutions will support the young best by recognizing the variety of needs of individuals, the possibilities of the educational sector and of combining with employers and communities.

### ***Long-Term Care***

While there is a consensus on the need to solve LTC issues, there is less agreement on the options available, not only on financing grounds, but also on design issues. The definition and measurement of disability is not always a simple task. Purely "physical" criteria can provide a cost-control solution, but the growth of mental illness and insufficient medical knowledge of some diseases mean that criteria to provide LTC benefits may end up being too restrictive. The development of a network of suppliers of LTC services is also a challenge for all countries. Most social security agencies need to additionally develop the rules and regulations to adjudicate benefits. Nevertheless, a significant part of the solution to the LTC problem is to provide an adequate framework for caregivers. For social security agencies, this specifically means the formal recognition of the possibility that a worker may need a period out of the labor market to care for a disabled family member, and the accreditation of periods of care as periods of tenure in the pension system, and certainly to provide them with health insurance while providing care.

**CHAPTER V**  
**EMPLOYMENT POLICY**





## CHAPTER V EMPLOYMENT POLICY

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### V.1 Employment Protection

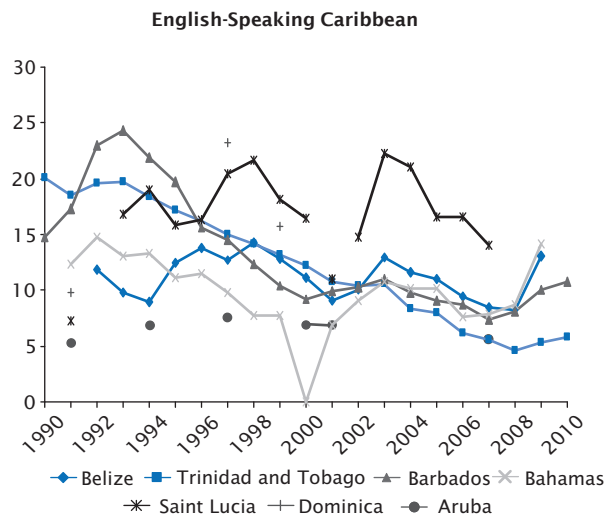
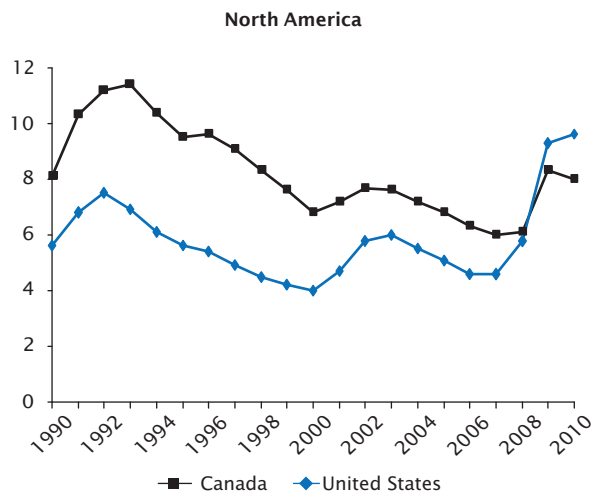
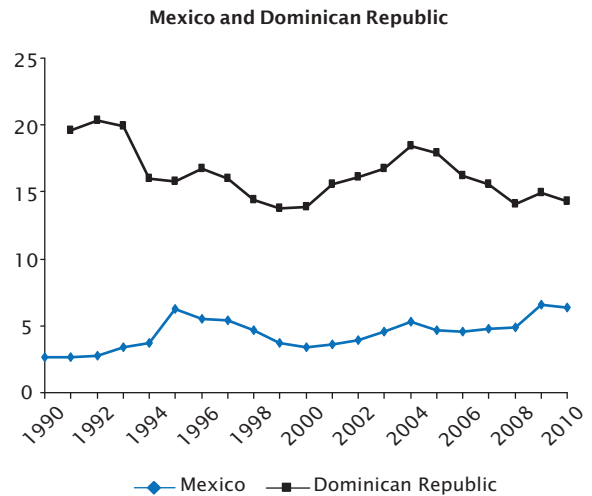
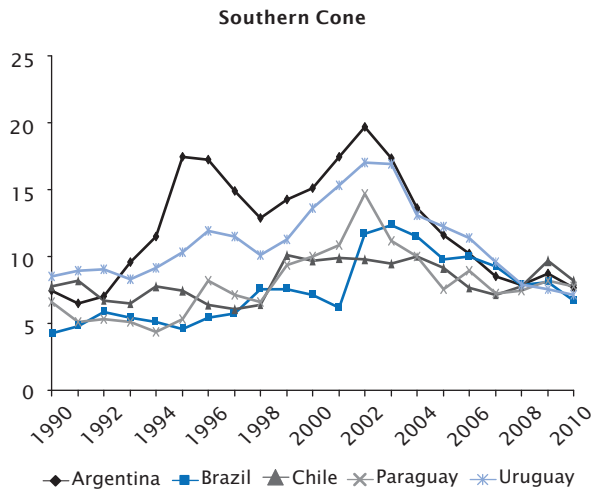
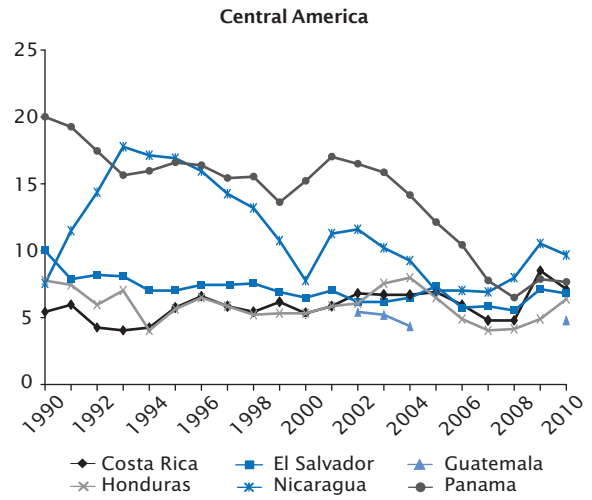
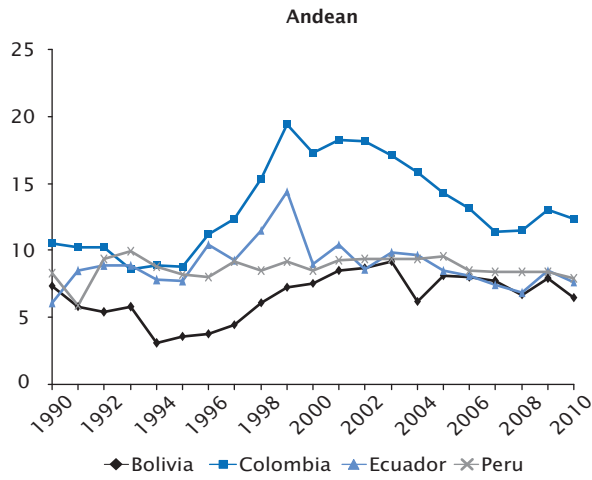
**F**or the Americas, the evolution of employment conditions over the last ten years has meant a general improvement in the first part of the period, but a haphazard time since 2007. In fact, probably for the first time since the fifties, the region in general experienced (until 2008) an environment of low inflation rates and stability or growth in purchasing power parities and lower unemployment rates. The severe economic turbulence from 2007 through 2009 had a significant impact on workers. Social protection policies on employment had been evolving since the nineties and some countries were able to face the Great Recession with renewed frameworks while many others were still using questionable unemployment insurance schemes or policies, including those cases where permanent employment policies were nearly non-existent. This chapter discusses the main developments in employment and unemployment as well as key debates surrounding employment policies.

Figure V.1 shows the evolution of unemployment by country since the nineties. Figure V.2 presents long-term unemployment figures. These figures show that, relative to the period 2000-2005, recent years show lower unemployment for most countries, with the notable exception of Mexico and the United States. Compared to the early nineties, unemployment in Central America and the Caribbean

is lower and this has been a continuing twenty-year trend (with the exception of Costa Rica). In South America, there has been more variability over time and even though unemployment has been relatively low in the last decade, unemployment rates in some countries may be even higher than the ones observed in the nineties. In general, there is more unemployment in Mexico and the United States, both short- and long-term, but this is not the case in Canada, where unemployment rates have been drifting to lower levels.

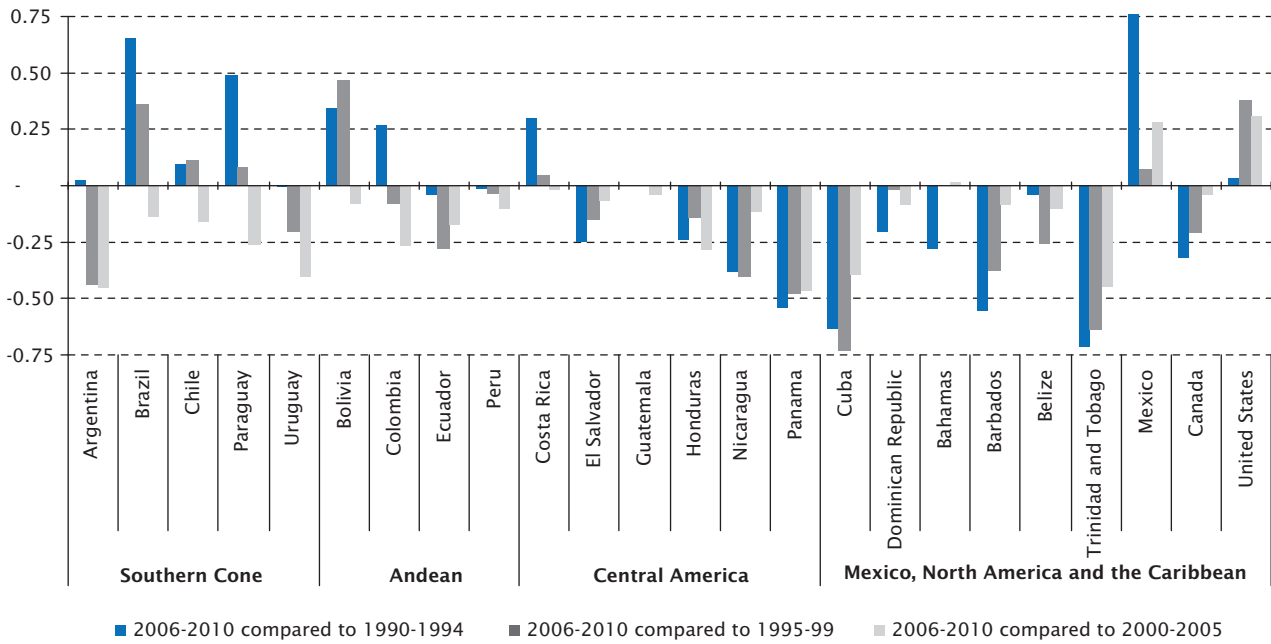
Between 2007 and 2008, the picture changed and it became clear that the global economy was entering a recessive stage. Although history is not yet written, the crisis has been characterized by a strong recovery of emerging economies, in particular by the fortitude of regions exporting primary products, as well as by the recovery of the manufacturing economy and the knowledge economy. As shown in Figure V.3, Latin American and Caribbean economies have performed better than developed economies in the last decade, and countries exporting primary products have done even better. Certainly, debates on development exceed the length of this chapter, but undoubtedly, from a social protection perspective, countries should take into account that the crisis may lead to significant changes in export markets to determine the best mechanisms to protect workers against this risk.

Figure V.1  
Evolution of Unemployment Rates by Country



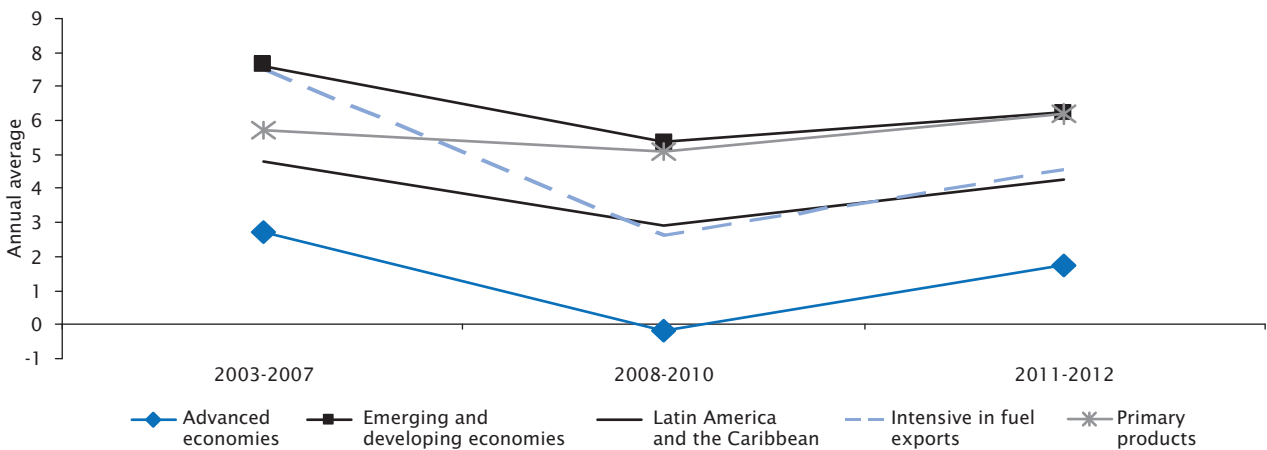
Source: CEPALSTAT (2012); for the United States, Canada and the English-Speaking Caribbean, Bureau of Labor Statistics, Statistics Canada, and World Bank (2012).

**Figure V.2**  
**Long-Term Changes in Unemployment Rates: 2006-2010 against Prior Periods**



Source: Constructed based on Figure V.1 data.

**Figure V.3**  
**Growth Rates of GDP in Different Types of Economies, 2003-2012**



Source: IMF (2011).

## V.2 Tendencies and Debates

We can summarize the development and debates on employment protection in three different areas. First, we can say that there is a growing tendency towards the use of "best practices" in employment policies, covering both unemployment insurance and active employment policies. On the other hand, the depth of the Great Recession in 2009 and the persistence of high unemployment levels or low employment growth have rekindled discussion on the use of fiscal policy to promote employment. Finally, the discussion regarding the use of employment protection legislation and its reform toward social security mechanisms actually never stopped but has also been reignited.

### **Employment Policies**

*The Americas Social Security Report 2007* and *2010* dealt with the design of unemployment insurance. They highlighted that countries were evolving from a traditional passive program that was only responsible for making benefit payments to schemes fostering labor market reintegration. This inclination towards activation policies is reflected in the structure of unemployment insurance and in the development of programs aimed at re-launching careers, completing or transforming the process of human capital recruitment, and encouraging individuals to actively search for a job.

The labor market is heterogeneous and different countries have different problems. There are significant differences in the characteristics and composition of unemployment. In Europe, unemployment tends to concentrate in long-term spells—where once workers are unemployed they remain unemployed for a long period of time—while in other countries (Mexico or the United States, for example) there is a high turnover rate, meaning a large number of unemployed workers with relatively short unemployment periods.

Female and youth unemployment levels are generally higher. Women usually serve as caregivers, not only for children but for older adults too, a situation that contributes to unemployment by increasing the probability of them quitting their job or working only part-time.

One of the main difficulties young people encounter when entering the labor market is their lower accumulation of human capital (education and experience); this results in higher unemployment rates and job offerings in occupations requiring fewer skills. The 2011 Report dedicated a chapter to youth employment. A significant share of young people is neither in the education system nor in the labor force. At least one fifth of the youth population find themselves in this situation in Colombia, Ecuador, El Salvador, Mexico, Nicaragua, Paraguay, Uruguay and Venezuela.

Unemployment insurance is considered a highly useful tool to allow competitive economies support workers and companies by allowing job turnover without the resultant reduction in family income. With respect to extending social protection, countries can be divided into two different and important groups according to their labor markets: those where worker participation in social security is almost universal, including unemployment insurance (United States and Canada); and those with significant informal economies (Latin America). According to Velasquez (2003), unemployment insurance coverage in Latin America does not exceed 14.7% of the unemployed population. Coverage data provided are the following: Argentina (2000), 10%; Brazil (2001), 11.8%; Chile (2000), 6.7%; Uruguay (2001), 14.7%; and Venezuela (1999), 7.2%. For the group of countries with large informal economies, institutional and financial conditions make it impossible for unemployment insurance to take the same form as in North America or Western Europe.

The most important developments since the nineties have been the following:

i) Considering UI programs as an insurance tool and introducing rules on incentives to constrain moral hazard among beneficiaries. This means payments have become more restrictive; in particular, payments are not provided to people who are not searching for a job, not participating in training activities or to people facing work limitations so a successful return to the labor force is not likely. On the other hand, new cash transfer programs have been implemented to support the "permanently poor", recognizing that poverty and unemployment are two different phenomena. Using individual accounts that make savings mandatory to employed workers so savings may be used when they are unemployed is also seen as a mechanism to achieve effective social protection while encouraging people to assume more responsibility.

ii) Replacement rates have been moving towards schemes where benefits are reduced as the duration of the unemployment period increases. The theory behind this shift is that right after losing their job, workers require increased liquidity and social support, but as time goes by, they should make an effort to find a job.

iii) Recognizing the growth in non-salaried work options and using the UI program to support micro credits and facilitate the development of self-employment.

iv) Allowing the UI program to make payments to mothers and to persons who have to care for disabled family members.

v) Inclusion in the UI program of workers under part-time or piece-rate contracts as well as of self-employed workers, who have traditionally been excluded from unemployment benefits.

The literature identifies three important elements in the design of unemployment insurance that can contribute to improving its performance: i) benefit duration and payment methods (lump sum payments or periodical payments) ; ii) monitoring

processes to ensure beneficiaries are searching for jobs as well as sanctions when this requirement is not complied with (for example, reducing benefits); and iii) the requirements unemployment insurance beneficiaries must meet to participate in work or training programs in exchange for receiving the benefits (Fredriksson and Holmlund 2005).

Several aspects in the design of unemployment insurance can help prevent distortions in worker behavior. One difficulty concerns the monitoring process to make sure beneficiaries (usually formal sector workers) are searching for jobs. This is a bigger issue in Latin American countries, where workers also have access to informal jobs and may not declare they have found a job while collecting benefits. "Moral hazard" is a term used to describe situations where individuals reduce their job search efforts since they are receiving unemployment benefits or find an informal job and continue collecting unemployment benefits.

To what extent can moral hazard issues in unemployment insurance be solved through private insurance? There has been a recent upsurge of interest in the 2002 Chilean reform based on individual savings and private fund management (Heckman and Pagés 2005). The notion of allowing workers to use individual accounts when they are unemployed is based on the creation of savings funds to ensure compensation when workers lose their jobs. A percentage of their salary is regularly deposited to this account. Workers may draw from these funds when they are unemployed or, ultimately, use them to complement old age pensions. One problem is that workers may have extremely low balances in their individual accounts so a State guarantee would be required.

Protection against unemployment in Chile is based on individual accounts combined with benefits from a pooled fund. The total premium is equivalent to 3.0% of the worker's salary; 2.4 points are paid by the employer and 0.6 points are paid by the worker. The employer's contribution is divided into a portion that goes directly to the worker's

individual account (1.6% points) and another one to finance the pooled fund (0.8% points). The contribution by the worker goes all into the individual account. Thus, a total amount equivalent to 2.2% of their salary is deposited in the individual account. The government contributes a fixed amount in real annual terms that is deposited to the pooled fund. Temporary workers are not entitled to benefits from the pooled funds so contributions are deposited directly to their individual account. In 2012, the government of Colombia sent Congress a proposal to adopt a system to provide protection to the unemployed similar to the one used in Chile (Ministerio del Trabajo de Colombia 2012).

In conclusion, it seems consensus has been reached with regard to the need for a national unemployment insurance program with active job search policies as one of the main components. A more controversial issue refers to expanding the use of individual accounts with a collective complement. The goal of individual accounts is to diminish the risk of individuals taking undue advantage of the system but it undoubtedly reduces its advantages as an insurance mechanism. The best option surely depends on the labor market conditions in each country and on each country's ability to manage benefits.

### ***Legislation on Employment Protection***

A second discussion, one that has actually been taking place at least since the nineties, refers to whether legislation on employment protection (LEP) or on unemployment insurance was more suitable to stabilize the well-being of workers.

*The Americas Social Security Report 2007* addressed this topic. One message was that literature on the effects of wage rigidity on employment is not conclusive for developed countries. It has been argued that lower unemployment rates in the United States than in Europe are associated with high flexibility which

allows adjusting of the real salary of less skilled workers in the presence of changes in the economic environment. It is believed that in Europe, institutional factors—such as the presence of labor unions, minimum wages and generous unemployment insurance—prevent adjustments to the salary of less skilled workers. However, Card, Kramarz and Lemieux (1999) study wage differences among low-skilled workers in the United States, France and Canada, and find no evidence indicating wage inflexibility is responsible for differences in the level of employment in these three countries.

Stress inevitably arises in unemployment programs and regulations on unemployment protection when we question the causality between these two programs and the phenomenon of unemployment. Economic theory on unemployment suggests that employment benefits can generate more unemployment by reducing individuals' incentives to work. However, it is clear that certain historical episodes of high growth in unemployment insurance coverage and benefit payments occurred because an economic crisis triggered social pressure to increase unemployment benefits. In other words, we are not dealing with stories where governments design unemployment programs that have undesired effects but with the fact that unemployment exists and that programs (or legislation) are only a means of lessening a social problem that emerge before benefits are provided.

There is no doubt that unemployment levels as well as their evolution can be affected by regulation to reduce layoffs, ensure compensation, or fix wages. This, however, does not necessarily mean that these regulations have a negative impact on well-being. Like any regulation, the extent to which they are understood and consistently applied, their outcome may improve the well-being of workers and reduce employer risk. Under those conditions, it is to be expected that companies and workers will internalize the cost of regulations so their net effect on employment will be very small or null and their

impact on wages will be compensated by the company reducing cash wages in exchange for higher future non-cash benefits. Thus, for example, in the analysis by Bernal et al. (2012), short-term employment is higher in societies where work arrangements are more flexible, but in the medium-term this situation is reversed. In addition, following the same authors, centralized collective negotiations and hiring and layoff regulations generate more long-term unemployment while mandatory severance payments do not create significantly different unemployment patterns in heavily and loosely regulated countries.

Unemployment insurance is the quintessential tool to protect workers against the effects of economic cycles. Even though there have been some favorable developments—as discussed in the previous section—the fact that most countries have no unemployment insurance remains a reality. The explanation seems to lie in the high levels of informal economy and the institutional weakness of countries in the region.

A reform undertaken in a number of countries has consisted in the capitalization and guaranteeing of liabilities arising from LEP. The more common solution consists in the employer's obligation to deposit a percentage of a worker's salary in the worker's individual account; the worker may withdraw the money upon separation from employment. In certain cases, this tool has been adopted as part of the reform to the pension system while in others it has been part of the regulation on unemployment insurance. Thus, for example, Colombia, Ecuador and Peru established that employers should deposit a percentage of the worker's salary to their account with a financial institution and that these funds were available upon separation. In Brazil, the Guarantee Fund for Time of Service receives 8% of the salaries, managed as individual accounts that may be used when workers become unemployed but also to finance affordable housing. In such cases, the issue of small companies and companies that did not use

to provide any severance pay and currently do not comply with unemployment savings either persists.

### ***Fiscal Policy***

It is possible to divide the trends regarding the use of fiscal policy to promote employment into two different groups. First, the idea that containing or even reducing "tax wedges" is necessary to avoid excessive distortions has gained acceptance in the last ten years. A tax wedge is defined as the difference between the total amount of cash paid by an employer and the cash actually pocketed by the worker, with the difference being taxes and social security contributions. In other words, relying excessively on the payroll to cover the cost of the social protection system should be avoided due to its negative effects on wages and formal employment. There seems to be significant consensus regarding this first trend, described in more detail in Chapter VIII of this report on financing.

The second hypothesis is that the State should resort to lower levels of taxation in times of crisis to promote employment, an issue that has been strongly debated. The 2007 Report discussed macroeconomic theories regarding the response of the State to reduce unemployment in times of crisis. The 2010 Report explored this topic a second time, documenting how countries had responded to the crisis that started in 2007. This second theory is a highly debated topic where empirical evidence is interpreted differently by experts. In practice, as shown in the 2010 Report, governments in the region respond to crises with subsidy and salary support policies although, in general, policies aimed at reducing the fiscal deficit have predominated. As the International Monetary Fund (IMF 2011) points out, in addition to the fact that economic conditions are different for different countries, the crisis inevitably made solving problems in the financial sector a priority which has not been entirely possible, particularly for Europe. Addressing unemployment



plus issues surrounding fiscal consolidation and financial problems has not been an easy task for governments.

### V.3 Perspectives

As 2012 approached, the Americas seemed to have avoided relapsing into recession. A significant number of American countries are among the emerging economies that have dealt better with the crisis by exporting primary products. However, economies that are more inclined towards the industrial sector have also shown positive growth rates since 2010. As a result, unemployment has not worsened and it is probably on its way to recovery, but this fact has not ended the debates

on social protection.

If there is a lesson to be learned from the critical experience lived in 2008-2009, it is that when facing a crisis, having an employment program in place is preferable to having to look for emergency exits. Complex regulations mean implementing unemployment insurance or active policies within a short period of time to address immediate unemployment surges is not possible. Developing administrative institutions and the provision of community services requires that states use long-term perspectives for their creation and use in times of crisis.

A set of trends that seem to be well established are the next: the convenience of containing or reducing salary gaps, using best practices in employment policies and unemployment insurance, and transforming employment protection tools into more certain work environments.

## **CHAPTER VI HEALTH INSURANCE**



## CHAPTER VI HEALTH INSURANCE

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### VI.1 Social Protection in Health

**B**y the beginning of the twenty-first century, many countries in the Americas had lived through reforms to social health insurance, continuing a trend that started almost thirty years ago. Reforms of different scope but of major importance were undertaken in Chile, Colombia, Dominican Republic, Mexico, Peru, Turks and Caicos, United States, and Uruguay.

When we observe all these reforms many questions arise. Is there a common thread to them? Which countries' reforms have been the most successful? What are the lessons to be learned? What are the unsolved issues that should be tackled in the near future? What are the hard issues that keep coming back after the reforms? The CISS Health Systems and Insurance Report in its three main publications (CISS 2008a, CISS 2011a and CISS 2011b) has tried to provide consistent information and analysis to answer these questions, through the research of the dynamics and evolution of systems, as a continuous and permanent project.

In this brief Chapter we would like to highlight three interrelated topics that have been put forward through editions 2005, 2008 and 2009 of the Americas Social Security Report (CISS 2004, 2007 and 2008 respectively), and in the CISS Health Systems and Insurance Report. First, we describe how health insurance coverage has evolved in the

countries and the future challenges facing those policies. Most of reforms studied have been implemented because it has been widely recognized that a significant part of the population has lacked coverage and thus there is a degree of failure in attenuating inequalities. Second, we provide an analysis on how fragmentation among different subsystems within a country has evolved, and of the policies adopted to overcome fragmentation. This topic recognizes that in most of the countries analyzed social security-based health insurance was an important player in the country before the reform and that reforms face the challenge of coordinating the old schemes with new ones created to achieve higher coverage rates. Third, we present a discussion on administrative and governance aspects of social health insurance systems, because failure in these can challenge the potential impacts of reforms.

The analysis owes to the Emerging Paradigm (EP, Chernichovsky 1995 and 2002). The EP is a term that summarizes principles followed by the series of reforms that were rooted in the late eighties and early nineties in both developed and less developed nations. We follow the EP because, among several conceptual frameworks, it can be viewed as a useful positive model that helps us understand how health systems actually work and as a normative guide for policymaking (CISS 2008a). We use these two approaches throughout this chapter. A brief description of the EP is presented first, while our

understanding of how reforms follow the EP is covered in the last section.

The EP attempts to balance the achievement of all societal goals for health systems: improvement of health status, equity among citizens, macro and microeconomic efficiency, and client satisfaction. The balance will be achieved by reconciling the seemingly conflicting attributes of "private" and "public" approaches. Indeed, the EP is a technocratic rather than an ideological paradigm. It recognizes that "competitive" need not mean "private", and that "public" need not be "State". We can think of the EP as a positive model that helps us understand how health systems actually work. In this role, the EP model has to be confronted with the current health systems. It is also possible to think about the EP as a normative guide for policymaking.

To achieve the goals of the health system, the EP recognizes that reforms continue to draw on the following principles:

- Entitlement to a socially supported package of medical care is universal.
- Funding of the package is based on means-tested rather than individual risk-related contributions.
- A substantial amount of "public" funding may be in the form of compulsory earmarked household and employer contributions to a common public fund or pool, which can be national or regional in scope. The contributions can be complemented with those from the State.
- The contributions are pooled nationally for subsidies or equalization of the funding of a standard capita.
- Supplementary private insurance and funding are sanctioned in conjunction with publicly supported entitlement.
- Through a universal risk adjustment or capitation mechanism, most pooled funds are allocated to competing budget holders' "plans" that organize and manage the consumption of care (OMCC), as opposed to its provision. "Plans" work in a regulated market.

- These institutions may contract care in ways that are different from competing or free-standing providers.

Considering these principles, a health system is regarded as one that controls at least several of the following functions: i) policymaking and regulation; ii) fundraising and allocation; iii) budget holding or organization and management of care consumption; iv) provision of care; v) training; vi) research and development, including investment; and, vii) monitoring and evaluation.

A national health care sector can be composed of numerous schemes that operate fairly independently of one another. Clearly, in a nation or administrative territory, no system is pure in that it completely controls all functions, unless the State is responsible for all, which is an uncommon case in the contemporary world.

Three functions are of main concern here: fundraising and allocation, OMCC, and provision. The EP considers these to be the core functions that define the basic relationships in a health care market or system. The other functions are supporting in that they guide, support, and enhance the core ones. Consequently, the enabling functions are largely of a public nature, involving substantial State responsibility.

## VI.2 Tendencies and Debates

In health systems, coverage has different meanings, and here we find one of the useful aspects of the EP. Coverage can measure rights to entitlements, at the level of funding (and allocation) and OMCC, and access at the level of provision (CISS 2007). In this Report, we would like to focus on rights to entitlement, because this is what has really changed during the last few years in the Americas.

Entitlements, according to the EP can be defined in three dimensions: *universality*, answering the question of who is eligible; *comprehensiveness*, that answers the question on what services are provided;

and *completeness*, that answers the question about how are services provided. Here we see another useful aspect of the EP, when it is said that a country has a universal system, it mostly refers to the dimension of number of persons covered, but it does not necessarily mean that all persons should be entitled to the same interventions (what) and with the same quality (how). This will become clearer in the next paragraphs.

In the last ten years, a movement toward universality took root in several countries of the region; that is to extend coverage to persons without affiliation to social security. The extension of coverage was pursued under a social health insurance approach, but highly (or mostly) subsidized by the State. Countries where this type of reform have been implemented include United States, Chile, Dominican Republic, Mexico, Turks and Caicos, Trinidad & Tobago, Peru, and Uruguay. Extension of coverage was still pursued as part of a previous reform in Colombia. Basically, in all countries extension of coverage was funded by general revenues, with the exception of the United States and Peru, countries that followed different paths (based on private funding, mandatory insurance and public subsidies). In 2012, we can see that enrollment in a social insurance scheme increased significantly and reached almost universal coverage (see Table VI.1).

The efforts to reach universal insurance have not been easy and we can learn from previous experiences. Two aspects of design preclude systems to reach universal coverage in countries where social security is a major player and informality is a structural phenomenon: focalization of subsidized programs, and the fact that in some cases enrollment in the subsidized system is voluntary. If a State subsidy is targeted to the poor, (Colombia, United States) by definition there is not universal coverage.

Why would a country set a targeted program for the poor? It was argued in Colombia that the main reason to re-focus the program (Act 1,122 issued in 2007) from previous objectives of universalization was the lack of enough fiscal funds to finance the

expansion of the program (Guerrero 2008). Another reason may be the fear that a health insurance program financed by general revenues may distort labor market decisions, and in particular promote informality (see recent discussion on Mexico's *Seguro Popular* in Bosch, Cobacho and Pagés 2011). Finally, the trade off between universalization versus targeted programs reflects social preferences in any country.

If a system is voluntary (Colombia, Mexico, and Uruguay) and not mandatory (Chile, Dominican Republic, Peru, Turks and Caicos, and United States) we can expect that a proportion of the population will never find it attractive to be enrolled in social security or in the public subsidized system. In Mexico, voluntary universal coverage has reached a level of 95%, recognizing that the rest will not find it in their best interest to be enrolled in social security nor in the publicly subsidized scheme. Making a system mandatory nevertheless requires strong enforceable tools.

In both cases, targeted and voluntary approaches, the reform fails to achieve universality and thus challenges the basis of health insurance: leaves the door open for moral hazard and adverse selection, decreases the possibility of risk pooling, and may impede the achievement of equity objectives.

Moving away from design issues and the restrictions imposed by the fiscal resources needed to subsidize an important fraction of the population, it has been recognized that institutional and administrative hurdles slow down the enrollment process (see Guerrero 2008 for the case of Colombia).

Now, there are two other aspects of coverage, *comprehensiveness* (what), and *completeness* (how). In this respect, recent reforms have also left us some lessons. Table VI.2 summarizes the reforms.

In Table VI.2, column 1 and column 2 are complementary, i.e., if the answer in column 1 is yes, then the answer in column 2 must be no, and *vice versa*. Moreover, if the answer in column 1 is yes and in the answer column 3 is no, then the system is universal and equal for all (not taking in to account

**Table VI.1**  
**Coverage of the Population by Financer in Selected Countries, 2011**  
 (percentage of total population)

	Mandatory of subsidized scheme	Targeting of subsidized scheme	Privately insured and others	Social Security	Insured by the State	Total with entitlement
Chile	Mandatory	All persons without social security	9.4	90.6		100.0
Colombia	Voluntary	Poor	6.3 <sup>1/</sup>	44.7	44.3	92.3
Dominican Republic	Mandatory	Self-employed workers, unemployed, disabled, and indigent	12.3 <sup>1/</sup>	24.9	20.0	57.2
Turks and Caicos Islands <sup>4/</sup>	----Mandatory in single system----		n.a.	100		100
Mexico	Voluntary	All persons without social security	4.6 <sup>1/</sup>	61.5	46.1	112.3
Peru	Mandatory	All persons without social security	1.7 <sup>2/</sup>	31.2	40.1	73.0
United States	Mandatory	All persons without social security using different programs	63.9 <sup>3/</sup>	14.3	15.7	93.9
Uruguay	Voluntary	All persons without social security	7.0	56.0	37.0	100.0

Notes: n.a.: not available. 1/ Data for 2005. 2/ Data for 2009. 3/ Mostly employer-based insurance. 4/ System in expansion.

Source: BPS Uruguay (2012b), CISS (2008a), CISS (2011a), CNSS Dominican Republic (2012b), DANE (2012), FONASA (2012), EsSalud Peru (2012), MINSA Peru (2012), MSP Uruguay (2012), U.S. Census Bureau International Database (2012a), U.S. Census Bureau (2012b).

private funding). We observe two interesting aspects. First, in most reformed countries of the continent, the guarantee to all citizens is a basic benefits package that can be provided using different procedures or even qualities, but different persons can receive a different package (having the basic package as the minimum) depending mainly on their labor status and sources of financing. This has to do with one of the more difficult topics in health reform. There is a strong statement in almost all countries in the sense that all citizens should have equitable access to health, notwithstanding the need of expenditure controls. Yet, the deep inequality in income and other social conditions makes it difficult to achieve that goal, and few countries in the region do it (for example, Cuba and Canada).

The theory of equity in health (see for example Anand 2002) argues that each society has a health inequality aversion, and trades-off equity and

efficiency. Nevertheless, it is recognized that equity in health should be pursued more than equity in income because health has intrinsic and instrumental value, and income, for example, is only instrumental for the well-being of persons; and because it is not needed to have inequality in health to have incentives for productivity, as it is the case of income. Health has intrinsic value because it is a fundamental part of the well-being of everyone. Health also has instrumental value because permits the development of the individual (Sen 1985); it is part of the human capital in terms of Becker (1975). What we can conclude by observing the different entitlements in each country is that, while they aim for eliminating certain inequalities, societies accept some inequality related to the capacity of financing of each person. Yet, almost all countries are living through social and political processes that aim for stricter equality in health access, quality and outcomes.

Table VI.2  
Entitlements in Selected Countries, 2011

	Basic explicit guarantee for all	Specific explicit guarantee for subsidized scheme	Possibility of supplementary package in social security	Comments
Chile	Yes	No	Yes	The reform that established the general entitlement took place in 2005.
Colombia	No	Yes	Yes	Rights for same benefits (across systems) adjudicated by the courts influenced the redesign of the system. In December 29, 2009, the Acuerdo 08 was issued to equalize both packages for children under 12 and increase the benefits of the subsidized packages.
Dominican Republic	Yes	No	Yes	The reform that established the general entitlement took place in 2001.
Mexico	No	Yes	No	Since the reform in 2004, the basic package in the subsidized regime has increased the number of covered interventions.
Peru	Yes	No	Yes	Reform enacted in 2009.
Trinidad and Tobago	Yes	No	No	Reform enacted in 1994.
Turks and Caicos Islands	Yes	No	No	Reform enacted in 2009.
United States	No	Yes	n.a.	All citizens are obligated to have an insurance that at least covers a minimum of interventions.
Uruguay	Yes	No	No	In 2005, the structural reform established a basic package for all, which is revised periodically.

Notes: n.a.: not available. In Chile the package is named Plan AUGE; in Colombia POS-C in the contributive regime, and POS-S in the subsidized regime; in Dominican Republic it is known as Plan Básico de Salud, PBS; in Mexico CAUSES+FPCC; in Peru Plan Esencial de Aseguramiento en Salud PEAS; in Turks and Caicos the package has no name; and in Uruguay Plan Integral de Atención en Salud, PIAS.  
Source: Own elaboration using legal information.



### **Fragmentation**

Fragmentation refers to a situation where for each specific group in the population there are specific entitlements, source of funds, and institutions—commonly, but not necessarily vertically integrated—performing the three core functions: fundraising and allocation, OMCC, and provision. In legal terms each subsystem has its own regulation. In a fragmented system, there are basically very little flows of funds or patients across subsystems.

Fragmentation challenges health systems goals (health improvement, equity, macro- and micro-efficiency, and client satisfaction, Chernichosky 1995) in several dimensions, and indeed the important and recent reforms in Israel and the Netherlands, for example, focused in eliminating fragmentation (in already universal systems). First, fragmentation impedes the achievement of equity. While by design an unequal system does not arise from a fragmented system, it is common to observe different entitlements or access to healthcare with the same source of funding for different subsystems. Second, fragmentation in a system where asymmetric information is the norm leaves a green field for opportunistic behavior. Different participants in healthcare systems face different incentives and information structures that can use in their favor. For example, insurers may avoid "bad risks"; providers "may not accept sick persons"; patients "may look for schemes that provide the best coverage for a disease". Opportunistic behavior threatens health systems schemes by impeding a wide risk pooling and thus risking its financial viability. Finally, in fragmented systems, efficiency and client satisfaction is hampered because affiliates do not have a choice among OMCC or among providers, limiting the possibilities of quality improvement through consumer choices. Moreover, if the functions performed within a subsystem are vertically integrated in an institution, most commonly providers receive a line-item budget and are not paid according to productivity.

Fragmentation regarding funding and entitlement can be avoided by defining a guaranteed package of

benefits for all, funded from same pool of resources, and, funding supplementary benefits out of other specific contributions. This is related to the discussion in the previous section.

Fragmentation of the organizational structure can be overcome in two opposite ways: i) by defining a unique OMCC for all which always includes the fundraising and allocation function, probably vertically integrated with providers (Costa Rica) or with separate providers (Canada); or, ii) by allowing affiliates choice of OMCC, with the respective movement of financial flows across OMCC. Recent reforms to healthcare systems in the continent were intended to eliminate fragmentation following the second approach, with the exception of Mexico and Peru. In Chile, Colombia, Dominican Republic, the United States and Uruguay citizens are given the opportunity to choose their OMCC agency (see CISS 2008a and CISS 2011a). In Mexico and in Peru with the introduction of the subsidized scheme, fragmentation was strengthened, with more resources allocated to each scheme, without the possibility to allow movement of persons and money across subsystems.

Before concluding this section, it is worth commenting on the role of competition among providers within the context of fragmentation. Competition among providers of the network of an OMCC can be a positive aspect in health systems, although it is not easy to achieve. When there is more flexibility for families to choose their provider of final services, when the networks of alternative plans are available to receive funding from alternative sources, when budgets and money flow on the basis of demand, quality and efficiency can be improved. Nevertheless, if the OMCC function is fragmented, even if there is competition in the provision, the main problems associated with fragmentation are not overcome; inequality and opportunistic behavior may persist, while potential gains in efficiency and client satisfaction are limited and health plans can lose the possibility of containing costs. Thus, the issues of choice and competition can be useful only in the context of a well-structured system.

### ***Governance and Administrative Issues***

Along the previous lines we have introduced some relevant aspects in governance and administrative issues. In this section we would like to briefly highlight them. In particular, we will focus on three aspects that we believe are extremely important. First, affiliation with a universal health insurance system should be made mandatory. Doing this eliminates opportunistic behaviors in relation to affiliation and thus guarantees the widest risk pooling available in the country, guarantees that all consumption of care is organized by specialized institutions (OMCC), and integrates private and public spending. Second, explicit guarantees and their sources of financing should be set at the highest regulatory level to avoid systematic litigation against the system (for example, root regulations in Constitutional statutes). Third, in a country where several OMCC exist, the reliable operation of a database of affiliates has proven to be crucial for a healthy system that efficiently directs budgets to the needs of affiliates.

### **VI.3 Perspectives**

In the last twenty years health systems across the continent have been reformed. Some of countries implemented structural reform, while others made adjustments to already reformed systems. The EP, by disaggregating systems in core functions, allows comparative analysis across countries. In general, we can conclude that to a greater or lesser extent most countries are following the EP. Countries that have followed more principles are Uruguay, Dominican Republic and Colombia (see Table VI.3).

Health systems reforms are a continuous process. In comparison with programs of pension reform, a change in the financial rules of health insurance is far from being sufficient to bring on a significant change in the ways families access services, and in the way services are provided. Reform processes are slow and require substantial institutional development to take hold. We conjecture that in general, countries will continue embracing the principles of the EP in the future, but national legacies and capabilities determine substantial differences in the way those principles can be applied.

Can the EP be conceptualized as a normative paradigm? This is a difficult question. There are still many different health systems, and as of today no one can say one generic option is better than the other. Still, the EP has a priori political, institutional, and substantive advantages: 1) it can appeal to opposing political constituencies; 2) it takes advantage of existing institutions, primarily insurers, health plans, and sickness funds; 3) it preserves all contributions to the system (such as the employer and employee contributions) in a relatively transparent fashion; 4) it helps control aggregate costs of care, in part by potentially reducing the cost of administering the system; 5) it facilitates labor mobility by uncoupling the association between specific employment and public entitlement to care, even when employers continue to finance entitlement; and, 6) most importantly, it balances the multiple objectives of the health system that secure universal entitlement, it is a platform to achieve a fair solution.

Table VI.3  
Characteristics of EP versus Reforms in Selected Countries

	Colombia	Chile	Dominican Republic	Mexico	Peru	Turks and Caicos Islands	United States	Uruguay
<b>Entitlement to a socially supported package of medical care is universal</b>	Partial: Two packages and uninsured population (targeted affiliation)	Partial, one package but still uninsured population (mandatory affiliation)	✓	X	✓	✓	X	Partial, one package but still uninsured population (voluntary affiliation)
<b>Funding of the package is based on means-tested rather than individual risk-related contribution<sup>1/</sup></b>	✓	✓	✓	✓	✓	✓	X	✓
<b>A substantial amount of “public” funding may come from compulsory earmarked household and employer contributions. The contributions can be complemented with those from the State</b>	✓	✓	✓	✓	✓	✓	Several subsystems	✓
<b>The contributions are pooled nationally for subsidies or equalization of the funding of a standard capita</b>	Partial, only a fraction of payroll contributions are pooled	X	Partial, there are still three subsystems	X	X	✓	X	✓
<b>Supplementary private insurance and funding are sanctioned in conjunction with publicly supported entitlement</b>	✓	✓	✓	X	✓	✓	Depending the subsystems	✓
<b>Through a universal risk adjustment or capitation mechanism, most pooled funds are allocated to competing budget holders’ “plans” that organize and manage the consumption of care (OMCC), as opposed to its provision</b>	✓	Partial, no risk pooling although competing OMCC	✓	X	X	Fund functions as unique OMCC and pays directly to providers	X	✓

Notes: 1/ If funding comes from payroll contributions and general taxation, we assume these are means-tested rather than risk-related contributions.

**CHAPTER VII**  
**MANAGEMENT AND ORGANIZATIONAL POLICIES**



## CHAPTER VII

# MANAGEMENT AND ORGANIZATIONAL POLICIES

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### VII.1 Management and Organization

**T**he *Americas Social Security Report 2008* and *2009* gave prominence to the organization and the structural design of social security. If there is a central message, it is that the efficiency of social security systems is largely defined by corporate, governance and management solutions as well as by their ability to organize the whole group of institutions, agencies and programs around the needs of individuals.

A national social security system is very seldom a clearly ordered group of agencies and programs. Usually, it is the result of a long process of decades searching for models, of political competition among different views on what social security should be, as well as of historical circumstances often beyond the control of national societies, such as economic recession and even war. Therefore, it would be naive to expect a purely technocratic or schematic point of view to define an appropriate approach to organization, management and evaluation. The most important task is to understand the different approaches and tools, the reason they exist and the question they are trying to answer in order to determine the most adequate path to system evolution.

The group of programs we call social protection systems—public, private or community—share the same goal: to provide stability and well-

being to families. Some of the most significant opportunities to achieve gains from transformation arise from collaboration among institutions (service providers and regulators), governments and communities to reach this common objective.

### VII.2 Tendencies and Debates

The vision of a good social security administration can be summarized as follows: providing citizen-centered services, to which the organizational design of the whole system should adjust. When we say organizational design we are referring, on the one hand, to whether services should be both vertically integrated (for example, from affiliation to provision) and horizontally integrated (if the different programs are to be managed by the same organization, for example, so the same institution is responsible for unemployment, health and retirement insurance), as well as to the internal map of the institution (for example, whether institutions are designed around programs, users or regions, and the role of shared service centers, among others).

In previous decades, when countries proceeded to vertically integrate institutions, a set of large and complex processes were also horizontally integrated. Currently, a tendency towards vertical separation (in particular, for financing and provision to be carried out by different institutions) has opened the door to more effective

organizational models where strong horizontal cooperation at certain levels is compatible with dynamic decentralization in others. While so-called "political restrictions" are usually considered to be the main cause of obsolete organizational designs, developing a clear map of goals and strategies, and a well-defined organizational design should provide sufficient incentives to reform social insurance institution processes and their organizational structures.

Over the years there has been increased awareness of the need to define the "right incentives" that social security should create for the population: incentives to work or to retire; incentives to stay healthy or to excessively utilize social security benefits, among others. The 2008 Report pointed out that little had been discussed on the incentives faced by administrations, communities and governments, and that, generally speaking, modernizing operations was not relevant to these agendas. Is reorganization a result of benefit and tax reforms or is it an integral part of a vision of social security? The 2008 and 2009 Reports are inclined towards the latter; in other words, reforming social security without analyzing the changes it introduces in system governance, in important public agencies, in the mix of public and private elements, cannot be done. Some of the most important changes that have occurred and continue to occur are the following:

- *Changes in the degree of vertical integration in programs.* Organizations combining insurance functions (such as health and retirement) have been, in many cases, divided and replaced by specialized agencies (in health insurance, pensions, or work risks agencies). However, national public agencies are still the main actors in certain affiliation and financing issues. Nevertheless, a large group of countries has preserved the integrated agency model. There is also a tendency towards increased horizontal coordination of specified processes among agencies.

- New social programs providing benefits similar to those provided by social security have been

incorporated. For example, programs responsible for paying non-contributive pensions to low-income older adults. In certain cases, positive synergies have been created; but in others, the adaptation of new programs has been poorly designed or executed, fostering an environment of bureaucratic competition or budget competition between programs.

- On the whole, reforms have facilitated the adoption of new information technologies (IT) and new approaches to user service.

- *Vertically, there has been a tendency towards separation* aimed at achieving improved governance and specialization outcomes:

- Specialized regulatory agencies have been created such as, for example, pension or health insurance regulatory boards or commissions.

- The financing process and the service provision process have been separated or specialized in independent organizations, or through internal agency regulation. For example, different programs may share affiliation processes, use common databases to manage benefits, or use the same mechanism to collect contributions.

A central message of the "citizen-centered approach" is simply that each citizen is different and management solutions should adjust to social diversity. Certainly, developing large-scale massive affiliation and benefit delivery processes are some of the competitive advantages of social security agencies, but this is compatible with the creation of special structures and channels for neglected groups. The issue of independent workers, of domestic workers and workers in micro companies is distinctive. On average, as shown in Figure VII.1, only limited progress has been made in providing coverage to workers in small companies in Latin America. There were substantial improvements in coverage for workers in small companies in Brazil, Chile, Colombia and Uruguay. Costa Rica, has achieved coverage exceeding 42% for this group, which although much

higher than the regional average of 18.5%, is still half of the 95% observed for large companies in the country. It should be noted that all these countries with relatively high rates of inadequate coverage or less-than-adequate coverage of workers in small companies have had fundamental reforms to address this issue. Regardless of general issues regarding contributions and benefits, social security administrations should develop special strategies and procedures to affiliate independent workers and workers in small companies.

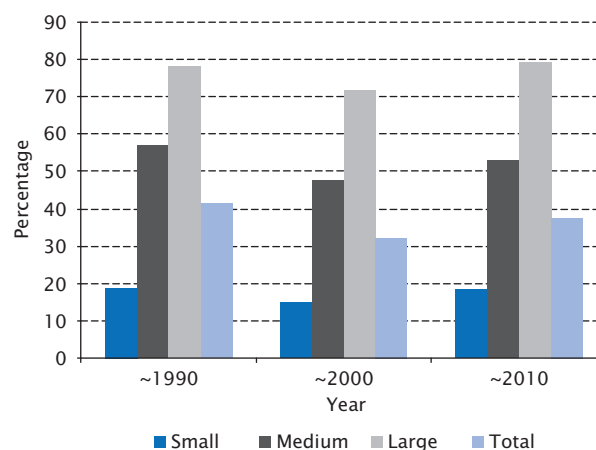
**Evaluation**

The 2009 Report discussed the approaches that are more applicable to the evaluation of social security. There are basically four aspects that should be considered in a comprehensive evaluation. First, the evaluation should respond to the concerns of different points of view: economic, actuarial, administrative, fiscal, and operations research (see Tables VII.1 and VII.2). Because each of these points of view are different, the purpose of the evaluation, including indicators and goals, may differ in each approach. Each view represents the concerns of different stakeholders. Any evaluation of social programs considering isolated opinions is likely to fail as a tool for potential program enhancement.

Second, it should be based on well-known follow-up and evaluation design steps: participation of key stakeholders, designing a framework for follow-up and evaluation, establishing indicators and setting goals, defining information sources, developing evaluation elements, and designing policies for the dissemination of results. Every step is important to the success of the evaluation and their order has implications in taking as much advantage as possible of this tool. Third, evaluations should be made of systems, agencies and programs. We conceptualize that programs are managed by agencies and that a system is a group of agencies and programs. In addition, it should be recognized that agencies perform many processes and that evaluation systems should be developed accordingly. Fourth, the object of evaluation should be the citizen, in other words, the use of microdata should be a rule, and any contact between the individual and the agencies and programs should be recorded on a consolidated basis.

In summary, a successful evaluation strategy lies in its comprehensiveness, in recognizing that even though the priority of different social groups may be acquiring certain system information, only a well-structured strategy incorporating the views of the organizations and processes involved will be an instrument capable of successfully improving agencies and programs and thus, system performance.

**Figure VII.1**  
**Worker Coverage Levels by Establishment Size,**  
**Average for Latin America, 1990-2010**



Source: Rofman and Oliveri (2011).



**Table VII.1  
Key Concepts in Evaluation Approaches**

<b>Economic</b>	Key concept: causality. Economists use behavioral models to identify how the environment or an intervention affects a variable. For example, an economic model may evaluate whether an increase in old-age economic benefits reduces the average age of retirement or whether a change in a formula to finance healthcare increases utilization of services.
<b>Actuarial</b>	Key concept: actuarial balance. Actuaries use numerical models to restrict the evolution of a system over time, given the rules and assumptions regarding behavior. Thus, predictions on demographics and financials are obtained and systems are evaluated in terms of their financial balance over time.
<b>Administrative</b>	Key concepts: customer satisfaction, efficient operations, consistent financials, and effective personnel management. In comparison with the other approaches listed in this table, administrative approaches do not strongly relate to a specific academic discipline. Administrative approaches are highly influenced by the training of administrators and the products offered by vendors for evaluation (e.g., the software solutions).
<b>Fiscal</b>	Key concept: solvency. Governments are interested in the feasibility of social security programs, and, as such, combine actuarial and other statistical models to evaluate the impact of programs on public expenditures and deficits.
<b>Operations research</b>	Key concept: optimization of a complex system. OR engineers utilize statistics, optimization, stochastics, queuing theory, game theory, graph theory, decision analysis, and simulation to measure the efficiency of a system, the sources of inefficiency, and recommend ways to find optimal solutions.

It is convenient to recognize that in general, agency and program managers have incentives to comply precisely with what is established in laws and regulations. After all, they are evaluated regarding fiscal aspects and the scope of long-term strategies usually goes beyond the period for which they were appointed to serve. Thus, an adequate strategy requires not only committed top executives but also for other government spheres such as finance ministries and Congress, key actors in the evaluation of public agencies, to open their evaluation approach, abandon an exclusively fiscal point of view and embrace an all-encompassing approach.

### VII.3 Perspectives

In this section we list administrative and organizational topics that should be included in the "checklist" of any organization. Every institution and program has gone through some modernization and it is likely that many discussed most of the following points in their change process:

I. Identifying administrative processes that may be common to different agencies and programs to be able to develop redesign opportunities. Some of the most important are:

a) Personal identification processes. Efforts should not be centered on a particular identification mechanism (specified number or technique), since contemporary technology allows great diversity and evolution of identification mechanisms.

b) Program registration and deregistration processes.

c) Transfer of common information among programs and between agencies regarding benefits.

d) Collection of contributions for different programs and agencies.

e) Integral information on the rights and obligations with respect to the social protection system, as well as interactive access capabilities.

f) Having an adequate system allowing: rapid calculation of amounts owed by companies, worker and type of insurance covered, accurately recording collections by company, worker and type of insurance covered, and, timely error calculation at company level, workers, days worked and salaries. In addition, databases should not only include affiliates, but their dependents as well since this would be useful when performing administration and provision functions.

**Table VII.2  
Strengths and Weaknesses of the Major Evaluation Approaches**

	<b>Strengths</b>	<b>Weaknesses</b>
<b>Economic</b>	<p>Potential for analysis of behavioral responses</p> <p>Use of more sophisticated statistical (econometric) techniques</p> <p>Ability to use today's very large databases</p>	<p>No existing theories of behavior for important cases</p> <p>Too much "faith" in theory; higher risk of political bias</p> <p>Requires information which is very often unavailable</p> <p>Lack of standardization; comparability of studies is usually only possible after long research periods</p>
<b>Actuarial</b>	<p>Hard use of numerical models</p> <p>Consistent use of sampling theories and methods</p> <p>Regulations on the profession and reports to ensure consistency and comparability across time and organizations</p> <p>More reliable to the extent that administration has control over rules of access to programs, premiums, and benefits</p>	<p>Difficulties in modeling programs in which individual family members change behavior as a consequence of the program</p> <p>Risk of assigning permanent status to predictions based upon time-specific assumptions</p> <p>Social security agencies and other social programs may have little control over access, rates, and benefits in the midterm, and behavioral responses to programs can be very large and fundamentally alter assumptions</p>
<b>Administrative</b>	<p>Ability to obtain balanced views</p> <p>Provides useful tools to make day-to-day decisions</p> <p>Provides tools designed to evaluate and manage</p> <p>Ability to communicate with personnel in charge of the agency or program</p>	<p>Risk of bias due to administrative "conveniences"</p> <p>Tunnel vision; lack of criticism for deviation of social goals</p> <p>Risk of falling into disorganized state due to excessive volume of information and criteria and the presence of many contradictory indicators</p>
<b>Fiscal</b>	<p>Capacity to provide government with information on feasibility of public programs</p> <p>Ability to present programs in a form amenable to understanding by legislators</p>	<p>Ignores considerations of individual welfare to evaluate aggregate results</p> <p>Emphasis on cash flows; accrual accounting viewed as secondary</p>
<b>Operations research</b>	<p>Careful modeling of the administrative process</p> <p>Ability to evaluate operational costs by process</p> <p>Very useful for established high-volume, repetitive processes</p>	<p>Requires quality and flow of data not supplied by many organizations</p> <p>Assumes adequate definition of process within the organization</p>

g) Establishing procedures which: allow swift exchange of information with companies and markets; allow social security institutions to present an "invoice" with the amount owed by the worker and the risk covered before the payment date; allow continual registration and payment of benefits by company, worker and insurance; allow searches on

rights and benefits, among other relatively sophisticated transactions; allow notification of errors in affiliation/collection, fines or initiation of legal proceedings to recover amounts owed; and, provide information to workers on contributions according to risk covered or owed by the employer.

## II. Management quality

a) Creating individual accounts, which include information on individuals, including any formalities carried out, verifiable by the individual. Establishing individual accounts for each worker regardless of the program's financial structure. In other words, both pay-as-you-go and capitalized systems, as well as any kind of health programs, should be capable of recording liabilities and contributions on an accumulated basis at individual and employer levels. This will determine the possibility of having effective user account and user service management processes.

b) Organizing service according to company type, particularly to attend to micro and small companies and independent and domestic worker needs.

c) Coordinating all agencies responsible for making economic benefit payments to ensure payments reach the beneficiary via a single account.

d) Adopting a strict and conservative personal data protection and access policy. Any errors involving this issue can reverse years of progress and create very expensive situations.

## III. Evaluation

a) Focusing the evaluation on the well-being of individuals rather than on agencies and programs. Ultimately, the target is the well-being of children, the elderly, the disabled, the sick and for every person—not that of the agencies.

b) Incorporating every approach and vision: economic, actuarial, fiscal, operations research and management.

c) The evaluation should be well structured in the sense that it should include all the steps in the evaluation strategy: identification and key stakeholder participation (not only those responsible for the tool's management), a logical framework design, key indicator identification and a set of goals, defining sources of information, developing evaluation elements and a strategy to disseminate results.

Even though at first lack of information can lead to imperfect supervision, over the years more consistent data will allow coherence in the evaluation. A good evaluation strategy will result in continued improvement; a poor strategy will ruin investment efforts. Ideally, key data should stem directly from transactional systems and surveys should be considered a complement.

There is no direct answer to the question about how much information should be disclosed. Privacy issues are a completely valid restriction on disclosure and too much information can also influence the opinions of interested parties. Revealing all available information might seem like an easy and "transparent" strategy but it should be considered that the degree of openness of information should at all times depend on an agency's capacity to take action and improve low-performing areas. Providing information without having the capacity to change may generate feelings of frustration among agency managers and among the general public.

**CHAPTER VIII**  
**SOCIAL SECURITY FINANCING**



## CHAPTER VIII

# SOCIAL SECURITY FINANCING

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### VIII.1 What is Social Security Financing?

**I**n the world of social security, the term financing is customarily used to refer to a very extensive collection of topics: public finance, the value of benefits, savings (by families, social security agencies, or countries) and investment fund management. In turn, each of these is linked to relevant aspects of social security policy: its solvency, the incentives it establishes to work or to retire, organic integrated or independent government organizations, and the credibility afforded by citizens. Thus, throughout the decade there has been no shortage of debate topics relating to situations and reforms dating back to the eighties, many of them renewed but others definitely innovative.

The topic of financing first appeared in detail in the first two issues of *The Americas Social Security Report 2002* and *2003*. The former described two conditions intrinsic to pension systems. First, higher levels of public spending in social security will eventually result in higher taxes and contributions. Second, if social security contributions are high relative to the value of services provided, unemployment or labor informality would be potentially affected. In addition, this first report presented a discussion on pay-as-you-go and individual capitalization models, largely emanated from the nineties. The topic of health insurance

financing was first addressed in detail in the 2005 Report, which includes an extensive chapter dealing with this subject. Most Reports have included discussions on relevant financing issues. In addition to the topics that were reviewed in those first few years, we can find the following:

- Fiscal aspects of pension system reforms: redistribution and transition costs
  - Social security oriented towards treating HIV/AIDS in countries in the Americas: Financing of high-cost diseases and treatments
  - Portability of health insurance, labor supply and work mobility
  - Coexistence of pension regimes
  - International social security agreements
  - Facing disability in the Americas: legislation, employment programs and insurance mechanisms
  - Globalization and unemployment protection
  - Unemployment insurance: a necessary instrument in contemporary nations
  - Financial crisis and pension systems
  - Projections of health expenditure in the Americas
  - Main characteristics of general old age pension schemes
  - Old-age pension benefit indicators in the Americas

The above list of topics reflects general concerns that were considered particularly relevant in those years. For example, with respect to the 2008 crisis, unemployment and investment fund losses were highly debated, while at the beginning of the first decade of the twenty-first century, the impact of reform on pension systems was the leading topic. In actuality, each of these topics has always been important so in the following section we attempt to make a list of the most relevant.

## VIII.2 Tendencies and Debates

In this section, we present a brief summary of key debates surrounding social security financing that have taken place over the last decade. Actually, the depth of these debates has required that a complete report be dedicated to them so this should only be seen as a guide.

### *Individual Accounts versus Pay-as-you-go*

This has probably been one of the most embittered debates surrounding the organization and financing of social security in the last ten years. In Latin America, debates were virulent and, for some authors, the world was divided into those operating individual account systems and those who still had pay-as-you-go systems. However, the 2010 Report stated that such classification was possibly inappropriate. To this end, it quoted two pairs of authors that symbolize this change, Murphy and Welch (1998) and Barr and Diamond (2008). Each has a different way of dealing with this matter and their political preferences are likely to be different, but their basic conclusions are similar as regards the central issue: the financial structure of the pension system is important, but it is possible to adequately deal with most problems in social security through alternative financing structures. The following have been discussed as topics that should be addressed by reforms:

i) Social security systems were created (mostly between the thirties and the fifties) using a model

that inevitably yields low rates of return on savings, generating a permanent distortion in labor and financial markets.

ii) Privatization is a secondary topic in the solution of most problems faced by social security. Gains from changing to an individual account system can be achieved by reforming the traditional system.

iii) There are significant advantages in providing an adequate framework to encourage work; for example, by avoiding the marginal taxes on work of almost 100% observed in many social security systems. While reforms to individual account systems have dealt more closely with this issue, it can be resolved in a collective system.

iv) Governments must eventually face the issue of unfunded public debt and of promises that cannot be kept. In most cases, it is preferable to do it through taxes on consumption to avoid putting excessive weight on generations of workers and high taxes on work and income.

v) It is not possible to argue that investment of financial funds by private agents will improve returns and reduce the deficit of the pension system.

vi) The social security system is subject to considerable political risk and reforms must work on defining adequate governance regulations to diminish the problem of short-term decisions generating long-term problems.

The 2010 Report thus expressed the need for debates on pension reforms in the years that followed the crisis to switch toward a general understanding of these issues. However, the last topic in the list indicates why these outcomes may not always be easy to achieve. As Professor Gary Becker (2009) expressed: "If there is no obvious gain from allowing most individuals to invest in stocks to help cover their retirement and if there is no fundamental transition problem, what, if any, are the advantages of a funded privatized system? I believe the advantages are mainly political, not 'economic', that privatization helps to separate saving from interest group politics, taxation and government spending."

Expressed differently, there are actually no valid structural reasons why a collective system should not be properly designed, as there are also no reasons why individual capitalization should solve the above-mentioned problems by itself. Most importantly, that the system should avoid establishing excessive disincentives to work or facilitating contribution evasion, that returns on (individual or collective) savings be adequate, that governments avoid laying the burden of large fiscal deficits on several generations of citizens, that fund investment be transparent and include adequate risk management and that the social security system be isolated from political risks.

### ***Centralized or Decentralized Fund Management***

The 2009 Report pointed out that in some developed countries individual retirement accounts are managed through the financial system in general, with functional integration between the financial system and the social security and fiscal systems. On the contrary, in Latin America IRAs were introduced with the creation of new institutions known as pension fund managers, which specialize in this area. The Report argued that the key to defining each model was the capacity of national governments to handle registration and collection processes effectively, which in turn opens the possibility of a national administration that controls collection, tax deductions and registration of funds into pension plans and IRAs. When this can be done, we have the models used in the U.S. and Canada. If this capacity is not available, governments opt for regulatory solutions that place special emphasis on risk management and use third parties (fund managers, collection agencies) to perform the necessary functions; this is the model used in Latin America. Canada and the United States have high tax compliance levels. This allows social security to rely on the general tax administration to assist in worker and employer registration. In turn, the fiscal agency receives regular information on payments made to social security institutions and private pension plans,

either occupational or based on individual accounts. In the model used in the U.S. and Canada, pension plan solvency regulations have reduced the need of having specialized regulatory commissions to supervise them.

This point, which is more of an administrative issue, has not permeated the debates, but, in practice, it is gradually gaining importance. Several countries where the design of income tax legislation is functionally linked to the general pension system have made advances in adopting common mechanisms to collect taxes and social security contribution. Certainly, this issue has no relevance in the United States or Canada because income tax coverage is very high, but it will continue being a difficult problem to solve in Latin America and the Caribbean, where virtually all countries have informal economy problems that prevent them from establishing an adequate link between the fiscal system and the social security system.

### ***Funding versus Pay-as-you-go***

Debates on the convenience of saving to stabilize contribution rates and pension plan benefits—frequently summarized by the terms "capitalize" or "fund"—have been decided in favor of the need to save. In the domain of health plans, this matter has turned out to be more complex than expected and no satisfactory solution has been reached.

For pension plans, demographic and worker behavior in the presence of extremely high taxes have settled the argument. It is necessary for national pension schemes to save in order to face aging; trying to pay benefits under a pure pay-as-you-go program leads to increased payroll contribution rates, those paid by active workers. Demographic cycles in the twentieth century were very marked—and it is not clear they will be over in the 21st century—determining that national pension systems created between the thirties and fifties would end with high dependency rates since the end of the twentieth century.



One of the arguments in favor of reforms toward IRAs is that they are automatically capitalized. The general opinion is that even though this might be true, individual accounts are not necessary to capitalize and that individual accounts do not ensure capitalization. The reason is that social security systems with collective systems can make financial savings to stabilize contributions and benefits. The 2008 Report underlined the importance of the Canada Investment Board because this is probably the country that has developed this strategy more explicitly (see also ISSA 2010). Another striking fact in this discussion is that an individual account system can virtually work as a pay-as-you-go system in the long term if the investment portfolio is excessively concentrated in the State's own debt. In such a case, it is not clear that the advantages of financial savings to reduce future fiscal pressure are being achieved.

Fiscal pressure associated to social security remains a permanent concern. The 2009 Report indicated that public spending in pensions as a percentage of GDP ranged between 0.2 and 15% in LAC countries. One of the exercises was to calculate implicit pension debt in a reform simulation using the same methodology for all countries reviewed in CEPAL (1998). Results are as follows: an extremely high cost (debt) in Uruguay, Brazil and Argentina (between 202 and 305% of GDP); a high cost in Cuba, Panama, Chile and Costa Rica (between 94 and 151% of GDP); a low cost in Peru, Mexico, Venezuela, Paraguay, Colombia, Nicaragua, Bolivia, Guatemala and Dominican Republic (between 22 and 45% of GDP); and an extremely low cost in Ecuador, Honduras, El Salvador and Haiti (between 4 and 19% of GDP). Pension debt depends on the size of the older adult population, social security coverage and the generosity of pension systems. These results are not comparable with studies using different methodologies for different countries.

An aspect of public finances discussed in the 2009 Report was the way liabilities were accounted for in public accounts. In general, governments do not record these liabilities so they may have

considerable hidden debt. To the extent explicit capitalization policies exist, the problem diminishes.

### ***Fund Returns***

The subject of fund returns is of interest to social security to the extent individual benefits are affected. Any scheme, either collective or individual accounts, can calculate the rate of return received by workers, as was done in the 2012 Report.

The 2012 Report also discusses changes in the value of retirement savings, which also affects the rest of the schemes but in different ways. There are two particularly relevant issues regarding finances and the age of retirement. In the first place, the extent to which social security schemes substitute private savings decisions and, in the second place, the extent to which retirement ages are affected by financial risks. Both are different sides of the same coin. The institutional framework can affect their relative importance in each country, but there is no such thing as a risk-free pension system. The extent to which risk affects the age of retirement, individuals modify their savings decisions to compensate for possible value losses stemming from the public pension system and, similarly, change their retirement decisions to adjust for changes in the value of private savings.

Since the 2008 financial crisis, pension systems, even those that had made financial savings, began to face the situation described in Figure VIII.1: interest rates reached historic levels from the mid-seventies to the nineties but in 2013, we will have experienced a five-year period of extremely low rates. Whatever the reason for such low rates and their potential development over the next years may be, there is no doubt that there has been a negative impact on pension fund profitability relative to what had been expected until 2007. Policy analysis and actuarial studies used interest rate levels exceeding the rate of inflation by 3% or more, but probably most will not be able to reach these goals for at least a decade. This means that the present value of future liabilities is higher while investment returns are lower, resulting

in deficits higher than expected. On the other hand, the strong recovery of emerging economies has also meant better investment outlooks. Thus, the 2012 Report points out that fixed income world markets yielded returns exceeding 6% in 2010, so interest rates were not low everywhere. The Report also mentions that investors have noticed that while the debt of developed countries exceeds 100% of GDP—and a lot more in some countries—if we consider social security debt, the average in developing nations is 33%. They have expectations of more rapid economic growth, and have often carried out social security reforms in an attempt to reduce future accidents (particularly Latin America). Thus, rich country pension funds could benefit by investing in LAC country debt, and perhaps pension funds in LAC countries will not suffer great losses.

### ***Worker Choice***

One of the key elements of reforms towards individual accounts was that workers should be able to choose their retirement fund manager. As time has passed, we have observed that these systems have to introduce regulations to prevent this capacity from diverting towards excessive marketing expenses or systematic worker errors. The 2009 Report gave special emphasis to the importance of research on psychology and economics, which indicate the importance of defining an adequate decision-making framework for individuals.

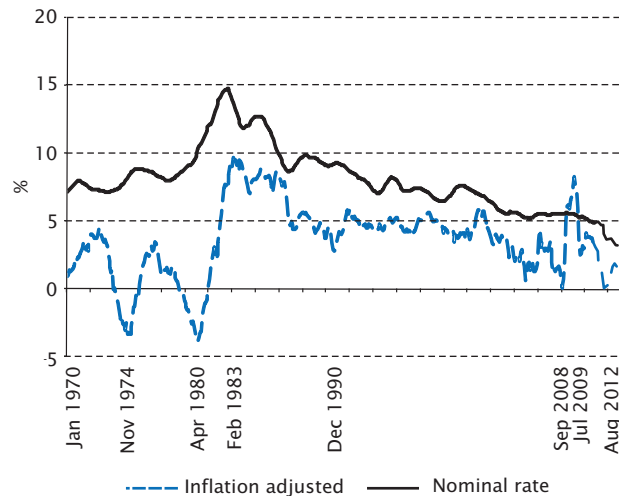
For example, the 2009 Report pointed out that research on pension plans shows that when faced with marginal changes in the selection framework, individuals can change their risk related decisions, so an uninformed choice can end up doing more damage. In fact, one of the chief complaints against IRA based systems concerns high fee charges. To address this problem while clearing the way for individual savings, either mandatory or voluntary, some countries have created individual accounts

controlled by a national social security agency but allow workers to choose from a menu of public and private investment fund managers.

Why is a larger number of choices justified as a policy option? The answer to this question is closely connected to the evaluation of pension systems. Specifically, it is connected to developing more flexible investment choices. Pension systems with individual account components have advanced towards using a "multi-fund" regulation to channel worker savings. This means that Chile and the rest of the countries that moved to capitalized systems are allowing workers to choose among different funds. In the United States and Canada, workers can basically direct their individual retirement savings to a large number of options available in the market. In models where account management is still the responsibility of a national social security agency, but permit individual savings (such as the Swedish model or Panama's new model), several options are allowed; similarly to collective investment funds.

Typically, countries that have adopted the multi-fund strategy allow workers to move from one fund to another within the same fund manager without having to pay a fee. Countries with regulations on minimum returns have been under pressure to extend these rules to several collective investment funds. This relates to behavioral issues regarding the way individuals respond to the complexity of information on pension plans. The purpose of this new trend, which started only a few years ago, is to adopt regulations to set limits to the decisions workers and retirees are allowed to make to reduce the incidence of apparently obvious mistakes systematically made by a large number of people. These regulations include establishing default options and restrictions on investment choices depending on worker age; in general, older workers are forced to invest more in safer assets while younger workers are induced or allowed to invest in riskier assets with better return outlooks in the long-term.

**Figure VIII.1**  
**High-Grade Corporate Bond Average Annual Interest Rates, 1970-2012**  
 (12 month average)



Source: Moody's Yield on Season Corporate Bonds. <http://www.federalreserve.gov/> (2012).

### **Health Financing**

The 2003 Report began to deal with the topic of health insurance reforms. Analyzing in detail the situation of Canada, the United States, Mexico, Colombia and Chile, it alluded to the complicated coverage problems that, with the exception of Canada, remain as challenges in most countries. It discussed two issues that remain key debate issues. First, the way financing is regulated affects the ability to contain expenses. For example, designing prospective payment rules generates better incentives for hospitals to avoid excessive spending compared to reimbursement systems. Second, it indicated that the way funds are consolidated and the health risks of the population are pooled affects the capacity to provide services and underlined the importance of adequately defining financial and organizational functions and purchasing of health services. Even though it commented that different mixes of public and private participation can work in a health system, it pointed out that the State's lack of capacity to make participation mandatory makes it very difficult to accomplish the goals of universality and cost containment.

### **Long-Term Care**

The 2006 Report mentioned the difficulty in financing long-term care programs. LTC programs have existed in the region mainly as welfare programs with limited budgets and capacities, but aging and loneliness are making it more necessary as part of a range of social security programs. These are not health service programs since they provide assistance to persons with limitations in activities of daily life to minimize, restore or compensate for the loss of physical or mental functions.

The 2006 Report presented projections of the demand for LTC that indicated that by 2050, around 16% of the households will have at least one older adult requiring LTC services. Financing solutions for LTC should contemplate assistance to both the person and the caregivers. Benefits for caregivers may include cash payments, but since they are the family caregivers, they should also receive financial support via social security coverage (health insurance and accumulation of length of service in the pension system) and paying substitute caregivers so they can enjoy periods of rest and vacations. Several countries with social security systems have adopted payroll

taxes to finance LTC programs while others are financing them with taxes. LTC programs thus face the dilemma faced by other social security areas: raising contributions generates resources but may leave many out of the system where informal economies exist; and on the other hand, programs financed through taxes usually only make small payments to low-income populations and do not provide a solution to the problem of most families.

### ***Tax Structure***

Several Reports have dealt with fiscal issues and the central message is that the huge size of social security systems determines that the design of the tax system and the design of social security contribution and benefit schemes are not separable. To emphasize this point, it has been mentioned that there are three major tendencies to achieve the goal of providing stable financing for the social security system combined with equitable fiscal treatment. First, governments have strived towards containing or even reducing the "wage gap", defined as the difference between the amount paid by the employer and net cash income received by the worker. Second, the use of general taxes on consumption, notably the value added tax, as a pillar of public finances, has grown. Third, an integral design of income taxes, social security contributions, and subsidy schemes.

The wage gap as defined above is mainly determined by social security contributions, income taxes, and other payroll taxes. In Table VIII.1, we see that the U.S. and Canada have comprehensive policies to reduce the wage gap, something that has not been achieved in Spain (a country that exemplifies the situation of most but not all of Europe), and that Korea presents a gap similar to Mexico while the gap in Chile is definitely lower. It is worth mentioning that these differences are very closely associated with program design and centralization as well as with the degree to which individuals and the State share the responsibility of saving to finance social benefits.

In Table VIII.2, we can see that collection of social security contributions as a percentage of national revenue collection has stabilized or increased since the nineties. Actually, in the whole OECD area, social contributions increase from the sixties to the nineties and stabilize around 25% of national revenue collection, while general taxes on consumption increase 80%, mainly by prevailing over special taxes (Table VIII.3). On their part, the consolidation of the VAT as the most stable tax and the one that affects the wage gap less is clear. In Figure VIII.1, we can see how since its introduction in the seventies, Latin American countries have adjusted their rates around 15% (not shown in the figure) and have made advances in closing the exception mechanisms that reduce the effectiveness of this tax.

**Table VIII.1**  
**Wage Gap for Married Couple with One Single Family Provider and Two Children at 100% of the Average Salary. Income Taxes Plus Employee and Employer Contributions Minus Cash Benefits**  
(percentage of wage costs)

	2000	2005	2010
Spain	32.3	33.4	33.8
Canada	23.9	21.5	17.3
United States	20.6	17.4	16.3
Korea	15.6	16.2	17.5
Mexico	12.6	14.7	15.5
Chile	6.10	6.10	6.20

Source: OECD (2011c).

**Table VIII.2**  
**Social Security Contributions, 1965-2008**  
 (percentage of total taxes)

	1965	1975	1985	1990	1995	2000	2005	2006	2007	2008
Argentina							17.0 <sup>2/</sup>			
Brazil						24.8 <sup>1/</sup>	23.3 <sup>1/</sup>	24.1 <sup>1/</sup>	23.9 <sup>1/</sup>	24.1 <sup>1/</sup>
Canada	5.6	10	13.5	12.1	14	13.6	14.9	14.7	14.5	14.7
Chile				9.0	6.5	7.3	6.5	5.8	5.6	6.4
Korea		0.9	1.5	10.1	12.1	16.7	21.2	21.2	20.7	21.8
Mexico			11.3	13.4	16.6	16.5	15.7	14.9	15.3	12.7
Spain	28.3	47.5	40.8	35.4	36.2	34.9	33.6	32.8	32.3	36.4
United States	13.3	20.5	25.2	25.2	24.9	23.4	24.4	23.5	23.3	25.1

Source: "Social Security Contributions" database, OECD. Available at: [www.oecd.org/ctp/taxdatabase](http://www.oecd.org/ctp/taxdatabase).

Notes: 1/Social security contributions as a percentage of central government revenues, World Bank. Available at: <http://data.worldbank.org/indicator/GC.REV.SOCL.ZS>. 2/Social security contributions as a percentage of central government revenues, World Development Indicators 2007. World Bank. Available at: <http://data.worldbank.org/sites/default/files/wdi07fulltext.pdf>.

**Table VIII.3**  
**Tax Structure in OECD Area**  
 (percentage of total revenue collection)

	1965	1975	1985	1995	2000	2008
Personal income tax	26	30	30	27	25	25
Corporate income tax	9	8	8	8	10	10
Social security contributions	18	22	22	25	24	25
Payroll taxes	1	1	1	1	1	1
Property taxes	8	6	5	6	6	5
General taxes on consumption	12	13	16	19	19	20
Specific taxes on consumption	24	18	16	13	12	10
Other taxes	2	2	2	3	3	3

Source: OECD (2011c).

### VIII.3 Perspectives

The financial crisis of recent years has not been favorable to social security finances worldwide. In addition to the problems of aging, lack of coverage and growth in medical costs, now social security is facing low investment profitability and unemployment, which increases spending and reduces income. On the other hand, social security programs have been the quintessential platform to protect families against the effects of the crisis and to maintain the necessary cohesion to advance in the difficult road governments have had to travel.

Probably the best signs of improvements in social security in the region are associated with the theme of the 2012 Report, which concentrates on the evaluation of pension system benefits. Whatever the organization of the system in each country may be, the main goal is

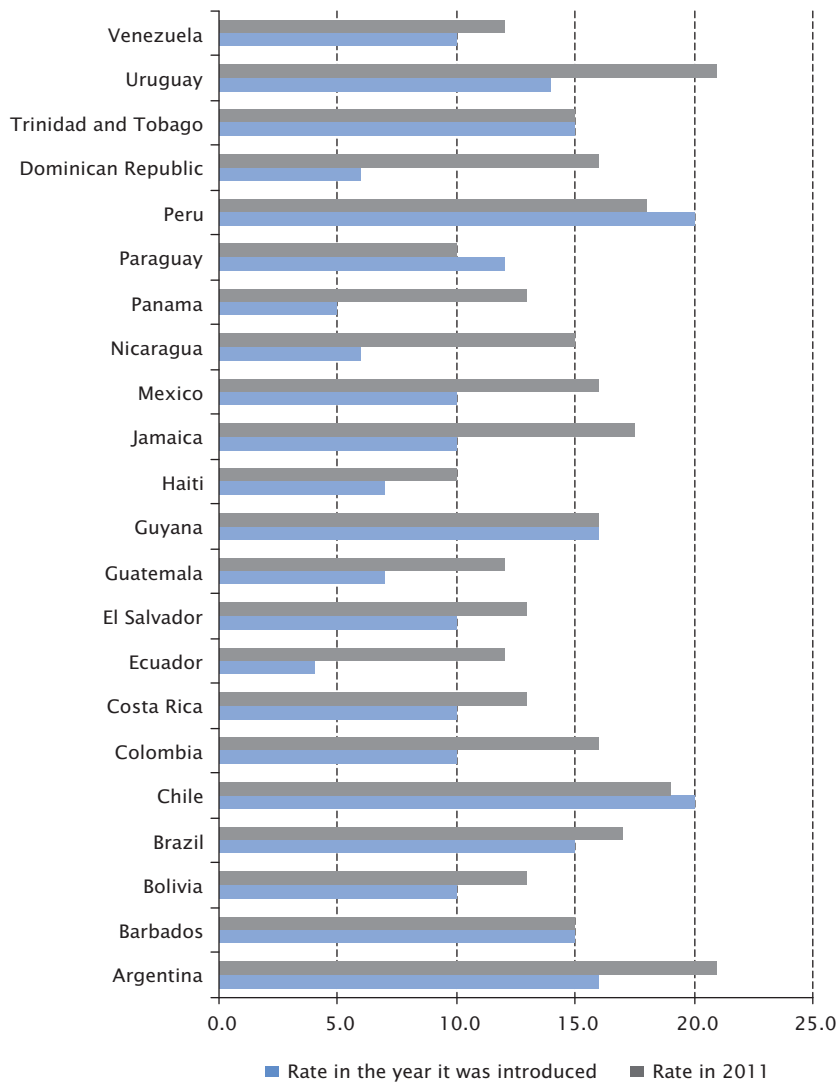
the well-being of individuals and the fact that discussions are beginning to be oriented towards this aspect is encouraging. However, a long unfinished agenda remains. In the field of pensions, an evaluation of the impact on informality on benefits, as well as the scope of disability benefits, is required. There has been less progress in other areas. It is not easy to measure the benefits of health insurance and to analyze the effectiveness of financing and spending. It is not easy either to make an international comparison of outcomes in safety and hygiene programs and insurance against work accidents since evaluations are not very common even within countries.

Paraphrasing the 2010 Report, it is impossible to deny that the global economic crisis has created difficult conditions for workers in the Americas. However, we have to remember that recessions are a

normal characteristic of the economy and that we know much more now than in 1929 about how to confront these episodes. In particular, social security has shown that it can be very helpful in dealing with difficult economic situations. When this Report was being prepared, in mid 2012, for Latin America, the road to stability and economic recovery seemed to be better than in other parts of the world; however this does not guarantee that the instability has ended.

From this crisis we must learn that lack of coverage, management flaws, and segmentation in social security become more evident when the economic situation worsens and that it will always be better to rely on permanent national policies designed under a long-term perspective and based on global risk strategies than on improvised, urgent, disconnected and often contradictory actions.

**Figure VIII.2**  
**Value Added Tax in Latin America and the Caribbean:**  
**Rate in the Year It Was Introduced and Rate in 2011**  
 (percentage)



Source: TMF Group (2012) and Lora (2001).



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