ILO CONTRIBUTION TO
PENSION REFORM IN CHILE

ILO Subregional Office for the Southern Cone of Latin America
Chile - Paraguay - Uruguay
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Foreword

Briefly covered in the following text are the main ILO actions and initiatives in support of the 2008 Pension Reform proposed by the Government of Chile and unanimously approved by National Congress.

Long before the political consensus necessary to initiate Pension Reform was achieved, the ILO was already supporting and accompanying its constituents to achieve this major social transformation. This publication is an account of the process and provides a summary view of the main activities and studies carried out. It is therefore a kind of accountability report for tripartite constituents: government, employers and workers, within the ILO’s historical concern for social security to be available for everyone in need of it.

This publication updates and extends a previous version titled Pension Reform in Chile and the Contribution of the ILO (ILO, 2008) and is part of the Support for Pension Reform in Chile Project (Proyecto Apoyo a la Reforma Previsional en Chile). Its aim is to more completely document ILO contribution to the process, including the activities carried out until March 2010, as well as a short presentation of the Pension Reform and its first results.

The specific characteristics of Chile’s pension system mean it cannot be easily replicated in other countries of the region or the world. Nonetheless, the aims set out by the process are currently applicable to other latitudes and the reform process experience, including political economy and management, may serve as a significant international benchmark on how to transform a pension system.

Chilean Pension Reform pursues a set of aims that are consistent with the strategy proposed by the ILO for adoption in countries in order to advance towards achieving the goal of decent work: increase social protection coverage, achieve greater gender equity, and combat poverty. Such aims are in line with recommendations by the 2001 International Labour Conference, when the issue of social security was addressed,
including the most recent aim of constructing a social protection floor. Similarly, these activities are part of ILO commitment to support countries in extending social security for all social groups, improving their working conditions and income security.

Guillermo Miranda
Director
ILO Subregional Office for the
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Santiago, June 2010
ILO contribution to Pension Reform in Chile¹

1. A historical reform

The Pension Reform began providing benefits on 1 July 2008—the most significant social transformation attempted in Chile since democracy was recovered in 1990, both in terms of its consequences in configuring a social protection system and its effect on the welfare of current and future generations, and also the scale of fiscal resources committed in the long-term. Enacted by Law 20 255, the pension system reform bill signed by President Michelle Bachelet on 11 March 2008 and unanimously approved by Congress on 16 January 2008 after an intense year of parliamentary debate, aroused interest beyond national borders due to the influence gained in other countries by the individual fully-funded regime set up in Chile in 1981.

It is a pioneering transformation which, as described by Bachelet on national television on the eve of the debut of the Pension Reform, represents a historical achievement and “an indispensable act of justice in a country that wants to advance towards modernity”, thereby taking “a giant step to end poverty and indigence among the elderly [moving] towards levels of greater equity and social justice” (Bachelet, 2008).

The Pension Reform proposes a set of aims that in general terms coincide with International Labour Organization global guidelines for social security, such as increased coverage—in this case for self-employed workers and young workers—, improved benefits and gender equity, by strengthening the solidarity pillar and by improving the contributory pillars of the system, both mandatory and voluntary. Its architecture highlights the creation of an extensive system of solidarity pensions, which on the one hand provide a basic solidarity pension to individuals in poverty aged 65 and over, and also provides an additional solidarity benefit to individuals receiving low pensions, and includes benefits for disabled people. The content of the

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reform addresses most of the main shortcomings affecting the individual fully-funded system since it was created: new social security institutionality, integrating agencies of the system of pension fund administrators (AFPs) and others inherited from the previous pay-as-you-go system, and strengthening conditions that allow for greater competition in the pension industry. And in recent decades the ILO reported this in various papers and studies.

In spite of the major burden imposed by this endeavour on fiscal accounts, estimated at 1.03% of GDP by 2015, in its first two years (2008 and 2009) the Pension Reform did not imply a disruption of fiscal discipline nor of the macroeconomic balance, thanks to sustainable long-term funding (Arenas de Mesa, 2010). In addition, the process to implement Law 20 255 was exemplary, smoothly materialising public policy through widespread and previously unheard-of inter-institutional collaboration and the effort and commitment of Government workers and authorities, resulting in successful change management (Delano, 2010).

The reform process began when President Bachelet took office and in March 2006 formed the Presidential Advisory Council for Reform of the Pension System, also known as the Marcel Commission. In July of that same year, the Commission submitted a report which served as the basis for an Inter-Ministerial Committee to draft the bill, and the content was announced by the President in December 2006 when it was sent to Congress. The bill took a year to be passed by Congress, a short time for a bill of such significance, facilitated by the preceding work of technicians, politicians, and social players. The bill was finally enacted in March 2008 and began granting benefits in July of that same year.

The Pension Reform made its debut in an unexpected scenario. Three months after the first benefits were granted, in September 2008, a global financial crisis broke out in developed countries, the greatest in recent decades, stemming from years of imbalances and deficient practices in the financial sector, and which quickly spread to the countries of Latin America. In spite of the intense impact of the crisis, since GDP growth dropped and unemployment rose, Chile had resources to cushion the social effects of recession and had a sound financial system which allowed it to react on time and raise social expenditure. The pension system reform became one of the tools that allowed the Government to provide additional assistance to lower-income sectors.

Within the context of the ILO’s constant concern for everyone in need of social security to have access to these benefits –something which in the process of globalization has become more necessary as the liberalization
of markets also introduced greater risk and uncertainty— is that the Organization, through its Subregional Office for the Southern Cone of Latin America, supported the Pension Reform put into effect by Chile in 2008. This was done even before political and social players achieved the necessary consensus to move ahead with the process, through working with constituents and technical teams that discussed and prepared proposals for such a transformation. This support for the reform continued during the first two years of its application, systematizing the experience and the lessons learned in the process (ILO, 2008; Délano, 2010).

Across-the-board work carried out by the ILO with workers, employers, and government has modestly—but continuously—contributed to spread ideas and explore opportunities for consensus in carrying out a wide-reaching and ample reform. It was precisely the need for a systematic approach to pensions, capable of integrating the contributory and non-contributory aspects, one of the features underscored by the ILO well in advance as the most appropriate overall approach for the reform process. Other dimensions to which the ILO contributed with studies and criteria to achieve greater visibility and define priorities for the process, were those related to increased coverage, the improvement of benefits, and gender equity. In some cases the process was followed through visible outputs, such as studies and publications, whereas in other cases the contribution was less visible, such as forming technical teams that helped pave the way for the reform (ILO, 2008).

Briefly covered in the following text are the contributions made by the ILO to Pension Reform in Chile. The account is divided into three sections, including the introduction. The second section presents the history of ILO contribution to the process, and the third section provides a concise description of the Pension Reform and its first results.

2. Five stages of ILO activities and contributions to Pension Reform

ILO activities and contributions to Pension Reform can be divided into five stages. The first stage, from 1981 to 2001, covers the first 20 years existence of the individual fully-funded regime, when the ILO maintained a critical view of the system. The second stage, from 2001 to 2003,
when recommendations to the resolution about social security at the 89th International Labour Conference of 2001 were put into action; followed by a third stage from 2004 to 2006, when the ILO actively supported consensus-building regarding the need to begin a reform of the pension system; and a fourth period from 2006 to 2008, when the Government of Michelle Bachelet began discussions preceding the bill, through the Marcel Commission, and sent the legal initiative to Congress, that passed the Pension Reform in January 2008; and finally, the fifth stage, since that moment and March 2010, comprising management and application of the Pension Reform.

The following section provides a concise view of ILO activities and contributions in these five stages.

**a) 1981-2001: Critical view of individual fully-funded accounts**

The ILO has historically held a critical view of the privatizing pension reform implemented in Chile in 1981 introducing the individual fully-funded system. This new system, although it contributed together with other institutional and economic reforms to the development of a capital market that was necessary to drive economic growth, and thus enabled other modernizing reforms, it violated basic principles of the social security systems promoted by the ILO in a tripartite manner. Lack of solidarity, persistent gaps in coverage, creation of new gender equities, and absence of representation of the insured, were all aspects that made it impossible to legitimize socially.

The critical view of the ILO stemmed from the nature of the political regime that put into effect the change in pension system, devoid of liberties and without respect for individual and collective rights of workers, and lack of participation by social players in the reform as such. It was based, above all, on that changing from the pay-as-you-go system to the fully-funded system involved payments by workers going to the pension fund administrators, and this violated the principles and rights of social security at national and international levels and, especially, those set forth by the ILO through Convention 102 of 1952, which assigned the State a predominant role in the pension regime (Rodgers, Lee, Swespston and Van Daele, 2009).

The ILO received and processed claims of violation of current regulations. The government of General Augusto Pinochet that put into practice this transformation, as well as the successive democratic governments since 1990 onwards, had to defend the individual fully-funded system. “Essentially,
aside from the system's lack of solidarity, claims were also on account of its exclusive dependence on the individual capacity of workers to save in order to finance their pensions, and the administration of such funds by private agents”, pointed out Victor E. Tokman\(^3\) former Director of the ILO Regional Office for the Americas.

In 1992, ILO officials published in the International Social Security Review one of the first articles critical of the pension fund administration regime (AFP)\(^4\) –as the individual fully-funded regime is called on account of the name of institutions that receive and administer worker contributions. This article had great technical repercussion because of its argumentation regarding the shortcomings of the AFP regime in terms of the quality and scope of the benefits.

Although criticisms have persisted, the tendency has been towards convening in that, on the one hand, it is recognized that private administration has contributed greater efficiency and yields to worker funds and, on the other, that different pillars can coexist and overall guarantee pensions, either by supplementing sources of funding or contributing the fiscal funds necessary to attain universal coverage.

**b) 2001-2003: On the path of the 2001 International Labour Conference**

According to guidelines of the resolution on social security at the 2001 International Labour Conference (ILO, 2002), studies performed at this stage as part of technical cooperation activities allowed identifying priority aspects for the reform. In this way, three studies anticipated fundamental content areas for the 2008 reform by showing, from the perspective of international comparison, the strengths and weaknesses of the pension system in Chile: in 2001, a study on pension coverage in three countries of the region (Bertranou, 2001); in 2002, an analysis of non-contributory and welfare pension benefits in five countries of Latin America (Bertranou, Solorio and Van Ginneken, 2002); and in 2003, an examination of gender aspects in three Latin American countries (Bertranou and Arenas de Mesa, 2003).

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3 Quoted by Délano (2010)
4 Gillion and Bonilla (1992)
In the sphere of technical cooperation, in 2002 the Department of Social Security in Geneva, together with the ILO Office for the Southern Cone of Latin America, negotiated and began operating a significant project with the Budget Office (Dirección de Presupuestos - DIPRES) at the Finance Ministry. Titled “Development of a model for financial forecasting of pension systems in Chile” (Desarrollo de un modelo para la proyección financiera de los sistemas de pensiones de Chile), the project allowed preparing a model, adapted to Chilean pension reality, to estimate the fiscal commitment implied by various components of the pension system: Instituto de Normalización Previsional (INP), recognition bonds, minimum pension, disability welfare pension, and survival pension (PASIS)⁵. Additionally, the project allowed training a group of Budget Office technicians in actuarial matters.

Also in the sphere of technical cooperation, in 2003, and after two years of work, the book Protección social en Chile: financiamiento, cobertura y desempeño, 1990-2000 (Arenas de Mesa and Benavides, 2003) was published. This book joined a series of publications by the ILO to assess the main dimensions of social protection system performance in various countries of the world using the so-called Social Protection Expenditure Review (SPER), developed by the ILO Social Security Department in Geneva. One of the most significant aspects detected by the study was the

⁵ These components arose in the context of the privatizing reform of 1981. The INP, that with the Pension Reform of 2008 was divided into two different agencies, administered the old pay-as-you-go regime pension funds; the recognition bonus represents pension savings prior to this reform, awarded by the State when a worker is disabled, reaches retirement age or dies; in addition, the State determined by law and awarded minimum and welfare pensions for disability and survival.
level of fragmentation of social security and of cash transfers, together with their impact on insurance performance.

c) 2004-2006: Contribution to consensus-building

In April 2004 the ILO organized jointly with the Ministry of Labour and Social Security and Fundación Chile 21, an important international seminar on the future of social security in Chile (ILO, 2004) highlighting two aspects. In technical terms, it included discussion of key aspects that would later be part of the agenda proposed by President Bachelet: pension coverage, gender equity, fiscal sustainability, and the high cost of the system motivated by restrictions to competition in the sector industry. In political terms, it allowed bringing together authorities, technicians, and stakeholders in one same forum, including the participation of experts involved in many pension reforms in different countries, such as Professor Carmelo Mesa Lago (University of Pittsburgh) and Nicholas Barr (London School of Economics). And among the social players were leading representatives of employers and workers, including members of Parliament who explained their views on the pension system (Box 1).
An Incomplete pension system

One of the most important milestones in ILO support for stakeholders in the Chilean pension system prior to the reform was to organize the international seminar “The Chilean pension system in the context of Latin America and the World: Evaluation and Challenges”, a joint technical cooperation initiative carried out with the Ministry of Labour and Social Security and Fundación Chile in April 2004. The meeting brought together several of the most outstanding experts in the field from Chile and the rest of the world, to examine the pension system in Chile 23 years after its creation.

Nicholas Barr
Helmut Schwarzer
Emmanuel Reynaud
Fabio Bertranou
Carmelo Mesa-Lago

International Seminar
The Chilean Pension System in the Context of Latin America and the World: Evaluation and Challenges
Santiago, April 2004

The opening presentation by Professor Nicholas Barr from the London School of Economics broke away from the usual approach to examining pension systems, surprising the audience with an innovative angle, analyzing on the basis of the purposes of the systems. Professor Barr recalled that from the point of view of individuals, pensions fulfill two purposes: first, to smooth consumption; that is, allow individuals to redistribute their income from youth to seniority. Second, it is insurance; because as people do not know how long they will live, they risk savings made during their labour-active stage being insufficient for their old-age. From the government perspective, pension systems may have additional aims, the most important of these being alleviating poverty, which is necessary both from the point of view that upholds equity as well as another which procures to maintain political stability. Additionally it may have redistributive aims for workers receiving lower wages.

Professor Barr analyzed the performance of the Chilean pension system in the light of these objectives. In his view, aiming to smooth consumption had been partially achieved, since the system had stood in place for 23 years, “stability of a set

*Délano (2010), ILO (2008)*

*Continues next page*
of institutions that are not easy to manage” (Barr, 2004). However, Barr highlighted four problems in the system: a) the risk and uncertainty of the level of future pensions; b) incomplete coverage (although greater than in other parts of Latin America); c) “considerable” administrative costs; and d) consumption is smoothed only for those who contribute over the guaranteed minimum pension level.

All these problems “restrict people’s capacity to decide if to consume during their working life or consume during their retirement” (Barr, 2004). As to the insurance, it is offered by the system for the longevity risk, but there is little protection against other uncertainties.

With respect to the government aim to alleviate poverty, it remains incomplete due to factors such as coverage. Several causes explain this diagnosis by the British professor. First, the guaranteed minimum pension does not resolve non-compliance, loopholes, or an incomplete history of contributions. Next, whoever contributes for less than 20 years has no right to any guarantee. The third problem noted is the concentration of poverty among women, of which on average three out of four do not contribute sufficiently to receive a minimum pension. The fourth problem is the shortage of social welfare, both in terms of benefits as well as coverage, and significant when considering the fiscal cost of pensions. Finally, outcomes in terms of redistribution are restricted to alleviating poverty, because equity has been –and still is– an issue still pending in the Chilean development model.

In sum, and at risk of over-simplifying, as Professor Barr said, “Pensions in Chile are an important part of the pension system, but as it stands at this moment, the system is not complete” (Barr, 2004).

During his intervention in the panel discussion at the same seminar on “The Chilean pension system and social policy”, the expert in social security at the ILO Subregional Office, Fabio Bertranou, expanded on the same approach as Professor Barr. Clarity of the aims of each pension system is fundamental, said Bertranou, so as not to expect from those systems what has not been previously defined among their objectives. He recalled that after the pioneering Chilean reform in 1981, greater emphasis was placed in Latin America during the 90s to advance in pension systems to achieve individual aims (smoothing consumption and insurance), whereas social aims were relegated to second place, as the responsibility of governments (alleviating poverty and redistribution). Chile headed this trend in the region. This meant the system began to mature on the basis of the so-called second pillar, contributory and mandatory, involving contributions for old-age, and not the first pillar, basic and redistributive by nature (Bertranou, 2004a).

According to this diagnosis, although the Chilean pension system responded quite well to World Bank (1994) recommendations made in the report Averting...
the old age crisis: policies to protect the old and promote growth, lacked a structure that may define it as a “system” and was rather a set of programmes and components lacking articulation and consistency.

Although Chile is characterized by having the labour market with least incidence of informality in Latin America, its ability to increase coverage—in extension and in depth—is limited by the characteristics of employment as such and the distribution of waged income.

Bertranou (2004a) at the seminar put forwards four challenges to be addressed by the system. The first was the paradox that workers enjoying greatest protection were the least vulnerable. For this he proposed redesigning the first pillar, in order to offset its conceptual bias, focusing discussion on access to insurance by self-employed workers and exploring interactions between protection subsystems that provide coverage and short-term benefits (health and family subsidies) and long-term (pensions). The second challenge was adapting regulation to avoid inequality and discrimination, particularly in the field of gender. The third was to improve competition in the system in order to reduce its costs, and the fourth was the fiscal cost implied by these systems.

In the view of Bertranou (2004a), Chile is in a privileged position to reflect and discuss the future of the pension system, since it has a stable economic and political context, and also institutional, technical, and financial capacity. The greatest restrictions therefore lie in its ability to achieve political agreement, for which “strengthening mechanisms for social dialogue seems essential”.

Technical cooperation with DIPRES was resumed and deepened during this period with the “Support to the Budget Office for the Pension Reform process” project. In view of the guidelines of key aspects for the creation of a new pension model in Chile, the ILO collaborated in the formulation of an actuarial model (ILO, 2005). Similarly, studies aiming to reveal more precisely the interactions between labour market dynamics and social security performance continued at this time (Bertranou, 2004a). One important input for this analysis was the First Social Protection Survey conducted by the University of Chile and the Ministry of Labour and Social Security.

d) From 2006 to January 2008: Contributions to the reform project

This period of project discussion and preparation began with the creation of a Presidential Advisory Council for Reform of the Pension System, known as the Marcel Commission. The ILO was one of the six international agencies
invited to speak, and participated in the Commission’s hearings, focusing presentations on the principles of social security promoted by the organization and highlighting three elements requiring special attention in public policy on pensions: coverage, solidarity and financial sustainability (Box 2).

**BOX 2**

**ILO proposal to the Marcel Commission: “Rebalancing” risks and including solidarity**

The ILO wants to contribute to discussion about pension reform, contributing evidence, international experience, and technical aspects. The ILO does not promote a specific model of reform, since this is for government and social players to decide, rather a set of basic principles stemming from the International Labour Conference. The report to the Marcel Commission on 24 April 2006 covered three areas.

The ILO suggested it would be advisable for Chile to “rebalance” individual and social risks, reshaping the pension system so that it may, in turn, continue to enjoy the advantages and positive effects of the fully-funded system, while adding a solidarity component to articulate contributory and non-contributory components.

In terms of coverage, the ILO recommended a strategy that combines contributory and non-contributory instruments, making mandates more extensive, introducing incentives, and better administration. Strengthening and modernizing semi-contributory and non-contributory instruments was suggested, extending the programme of disability and survival assistance benefits (PASIS), and reformulating around concepts of basic rights and citizenship.

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*a* Délano (2010), ILO (2008)
Regarding the cost of administering the system, the proposal maintained that centralizing collection mechanisms would provide several advantages, not least the economy of scale, improving integration of contributory and non-contributory components, as well as gradual linking to other social protection subsystems and the tax system.

With respect to the solidarity component, the ILO proposed the Chilean set of pension programmes could not be considered a system, on account of its low level of articulation. Pointing out that no developed country with a high standard of living and social integration lacks a solidarity component, the ILO proposed the reform may be redesigned around solidarity as the key component articulating other components, and funding should not be based solely on tax resources but also solidarity wage contributions.

In terms of reducing inequality and gender inequity, it was suggested these may be addressed through the solidarity component, by means of a set of policies and instruments, thereby inhibiting the channels through which the system multiplies the disparities faced by women in the labour market. Policies and instruments may include the implementation of unique life tables or other similarly effective mechanisms for benefits provided by the capitalization component, contributory credits for maternity, adapting retirement age to greater longevity, and adapting regulation to consider separation and divorce.

The ILO informed the Marcel Commission of the technical assistance provided to DIPRES in terms of financial sustainability, providing a financial/actuarial forecasting model to estimate fiscal responsibilities deriving from the pension system.

Mention was also made of the importance of including discussions on the role of the pension mechanism in relation to the medium- and long-term aim to reduce income inequality. Pension systems influence the distribution of income and the system for benefit indexation may contribute to this by being neutral, progressive, or regressive in distributive terms. For example, in the last 15 years PASIS and the minimum pension show a slight real increase, whereas benefits paid by the INP and the AFPs have increased more in real terms, reflecting the higher incomes of new generations retiring. The minimum wage also increases more than inflation in this period. This has progressively created a gap between various types of beneficiaries, and thus it is worth discussing if the gap is to be reverted or at least not widened.

In May 2006, the Marcel Commission organized an international seminar on pension systems, where the ILO gave a presentation on “Coverage and solidarity in pension systems.” As in its hearing with the Commission, the ILO proposed: (a) the expansion of contributory components through a
combination of mandates and incentives, along with strategies to steadily expand coverage; (b) the introduction and expansion of non-contributory components; (c) the standardization of different schemes; and (d) the introduction of solidarity mechanisms in financing and risk coverage. Thus, it proposed establishing a pension system –that is, moving from a set of weakly connected programs toward their effective and efficient articulation, through reforms and reinforcement of the public component. At this seminar, the ILO also contributed international perspectives and its own views, through the presence of its Geneva-based Social Security Department Director, Michael Cichon, and by facilitating the participation of social security secretaries from Argentina, Brazil and Uruguay.

Similarly, in May 2006, the ILO delivered a report on “Pension Reforms in Latin America, Experiences and Challenges” at a hearing of the Chamber of Deputies Commission on Labour and Social Security. Congress was soon to receive the pension reform draft bill and was interested in preparing for an informed discussion.
ILO contribution to Pension Reform in Chile

BOX 3

ILO report to Chamber of Deputies
Commission on Labour and Social Security
Pension reforms in Latin America:
Experiences and Challenges

On 9 May 2008, before the Chamber of Deputies Commission on Labour and Social Security, the ILO reported first on the key importance of labour market problems affecting social security in countries of Latin America, resulting in unequal coverage (Table A).

Second, the ILO recalled that in the last three decades there had been nine structural pension system reforms in Latin America. Four of these followed the substitution model (Chile, 1981; Bolivia, 1997; El Salvador, 1998 and Dominican Republic, 2003); two followed the parallel model (Peru, 1993 and Colombia, 1994) and three followed the mixed model (Argentina, 1993; Uruguay, 1996; Costa Rica, 2001). In turn, non-structural (parametric) reforms had been conducted in another two countries of the region (Brazil, 1998/1999 and 2003/2004, and Panama, 2005); and in Paraguay the 2004 reform affected only the Public Employee Fund.

ILO diagnosis of the structural reform of pension systems before the Commission on Labour and Social Security was critical. Examination of experiences showed problems such as stable or declining coverage; absence of significant impact on efficiency in the labour market; lack of institutional capacity to face the complexities of a more sophisticated system; persistent fiscal problems; high cost of private administration; difficulties in introducing competition to the pension fund administration industry; and that the impact of aging had not been avoided. Recognizing positive aspects, the ILO highlighted the standardization of programmes and conditions to obtain pensions; creation of new institutionality; greater transparency; in some cases better rates of return for contributions when workers had contributed for few years; and, in the case of Chile, development and deepening of the financial and insurance markets.

The ILO reported to the Commission on Labour and Social Security that underestimating institutional requirements and the necessary institutional capacity to make changes rank high among problems in applying these reforms in Latin America. Similarly, privatizing the pension system does not resolve the political risk or the informality of the labour market. Insufficient priority was given to reducing poverty among the aims of a social protection system, whereas public policy paid excessive attention to the second and not the first pillar. In the case of reforms in Chile, the question was posed whether policies were in the right direction or if the performance of a private pension system was because of a favourable economic setting.

Continues next page
As to future challenges, the ILO spoke to the Commission on Labour and Social Security of the need to restructure the social protection matrix in terms of access conditions and financing; paying attention to the feminization of old-age, and the gender dimension in pension systems, as well as the situation of the elderly in the labour market.

### Table A

**Latin America (14 countries): Pension Coverage**

<table>
<thead>
<tr>
<th>Countries</th>
<th>Coverage in employment</th>
<th>Coverage in employment 1st Quintile</th>
<th>Coverage in employment 5th Quintile</th>
<th>Coverage in employment 5th to 1st Quintile</th>
<th>Senior citizen coverage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Argentina (2003)</td>
<td>40.3</td>
<td>4.0</td>
<td>71.6</td>
<td>17.9</td>
<td>68.3</td>
</tr>
<tr>
<td>Bolivia (2002) a/</td>
<td>10.9</td>
<td>0.3</td>
<td>34.0</td>
<td>113.3</td>
<td>14.7</td>
</tr>
<tr>
<td>Brazil (2002)</td>
<td>48.3</td>
<td>13.7</td>
<td>72.7</td>
<td>5.3</td>
<td>85.9</td>
</tr>
<tr>
<td>Chile (2003)</td>
<td>63.4</td>
<td>29.9</td>
<td>72.8</td>
<td>2.4</td>
<td>63.8</td>
</tr>
<tr>
<td>Colombia (1999/2002)</td>
<td>26.9</td>
<td>3.2</td>
<td>59.5</td>
<td>18.5</td>
<td>18.6</td>
</tr>
<tr>
<td>Costa Rica (2002)</td>
<td>52.1</td>
<td>15.9</td>
<td>62.4</td>
<td>3.9</td>
<td>36.6</td>
</tr>
<tr>
<td>Ecuador (2003)</td>
<td>23.3</td>
<td>6.8</td>
<td>45.0</td>
<td>6.6</td>
<td>15.2</td>
</tr>
<tr>
<td>Guatemala (2000)</td>
<td>19.9</td>
<td>4.0</td>
<td>47.4</td>
<td>11.9</td>
<td>11.3</td>
</tr>
<tr>
<td>Mexico (2002)</td>
<td>28.4</td>
<td>1.4</td>
<td>53.1</td>
<td>37.9</td>
<td>19.2</td>
</tr>
<tr>
<td>Nicaragua (2001)</td>
<td>19.4</td>
<td>3.8</td>
<td>31.7</td>
<td>8.3</td>
<td>4.7</td>
</tr>
<tr>
<td>Paraguay (2001)</td>
<td>14.8</td>
<td>0.1</td>
<td>35.0</td>
<td>350.0</td>
<td>19.6</td>
</tr>
<tr>
<td>Peru (2002)</td>
<td>14.4</td>
<td>2.0</td>
<td>46.8</td>
<td>23.4</td>
<td>23.7</td>
</tr>
<tr>
<td>Uruguay (2004)</td>
<td>57.3</td>
<td>13.7</td>
<td>78.9</td>
<td>584</td>
<td>87.1</td>
</tr>
</tbody>
</table>

Source: Prepared on the basis of Rofman (2005), Rofman and Lucetti (2005), and other sources

\( a/ \) Only contributory regime
During the first half of 2006, the ILO also contributed technical notes dealing with aspects such as international labour standards, coverage of self-employed workers, the importance of non-contributory and social assistance pensions, and the relationship between demography and pension systems. (Bravo and Bertranou, 2006; Bertranou, Gana and Vásquez, 2006; Bertranou and Pérez, 2006; Bertranou and Vásquez, 2006).

Once the draft pension reform bill went to Congress in December 2006, the ILO took part in the hearings held in 2007 by the Chamber of Deputies Commission on Labour and Social Security in April; in the Chamber of Deputies Commission on Finance in July; and lastly, in the United Commissions on Finance and Labour of the Senate, in October. The bill was approved by Congress on 16 January 2008, and Law 20 255 came into effect on 11 March 2008.

On 4 June 2007, while the Pension Reform bill was discussed in Congress, during the 96th International Labour Conference the ILO Director General presented President Bachelet, who spoke of the importance of social protection vis-à-vis the aim of Decent Work. In this way the President explicitly recognized the priority of social protection in public policy, a requirement for decent work (Table 4).
BOX 4

Michelle Bachelet at the ILO: “Decent work in an ever more uncertain world”

Before a full plenary at the 96th International Labour Conference in Geneva, Michelle Bachelet, President of Chile, reaffirmed her government’s commitment to social protection as “an essential tool for responding to the challenge of decent work in an ever more uncertain world”, while addressing government, employer and worker delegates on 4 June 2007 at the third session meeting.

President Bachelet said she aspired for her government to be remembered “because it was able to make a qualitative leap in terms of social rights and lay the grounds for a social protection system” explaining to delegates the proposals for reform of the pension system. She explained the aim is to go from a system based almost solely on a fully-funded individual account for each worker, to a mixed system, with a solidarity pillar, another pillar of individual fully-funded accounts (contributory), and a third pillar of voluntary savings, safeguarding the balance and combining incentives with care.

Michelle Bachelet, President of Chile and Juan Somavia
ILO Director General

96th International Labour Conference

Geneva, June 2007

a Délano (2010)
The Pension Reform is supplemented by transformations in health, seeking to ensure quality and timely access; education, where the State also aspires to achieve quality and access; and in other fields. The old social security arrangements were designed for waged workers, but today, with a more diverse and dynamic labour market, social protection must be seen in this perspective. “It is about protecting everyone, which is true, but especially –and although it may sound obvious– protect the most unprotected” she said.

Juan Somavía: “There is no growth without social justice”

Juan Somavía, ILO Director General, presented President Bachelet as someone “whose life has been marked by the struggle for social justice”, adding “fights against the violation of human rights for that tragedy to never again tear national souls. Fights for democracy, for every Chilean be able to decide national political directions. But also fights for national reconciliation (…) Fights for gender equality and non-discrimination”.

Somavía said Bachelet “is driving Pension Reform in Chile to build a sound social base to cover, first, the most unprotected Chileans”, and explained to delegates that social protection is the hallmark of the President’s leadership. He recalled that in her national address on 21 May that year, she had requested “to make decent work an ethical imperative, as a society, and we must strengthen corporate social responsibility”.

The ILO Director-General said “Chile has enjoyed economic success and must now achieve appropriate social success”, and called President Bachelet “a leader with a global vision as her priorities are the ones on the agenda of people around the world”.

Recognizing his emotion as Chilean Director General, Somavía added: “Today I have the honour to introduce a President who transformed an essential truth into concrete policy measures: there is no sustainable economic growth without social justice”.

Furthermore, between August 2007 and June 2008, within the context of the ILO Quantitative Training for the Americas Programme (QUATRAIN-Amercas) a training course on actuarial and financial techniques was organized, with the participation of a select group of government staff, including personnel from the Ministry of Labour, DIPRES, the Superintendence of AFPs and the Instituto de Normalización Previsional (INP). The aim was to extend training, which started with, Budget Office
staff, to other public agencies and to build a common language within the government structure, along with the critical mass necessary to monitor and supervise key financial variables within the social protection system. The Organización Iberoamericana de Seguridad Social (OISS) also collaborated with the activity.

And in December 2007, the ILO held a Regional Tripartite Meeting on Social Security with participation by ten Latin American countries. This important meeting set the agenda for priorities and activities for the ILO and constituents in coming years, based on best practices, international evidence and international labour standards. With ongoing debate on pension reform in Chile, combined with other regional changes in areas such as cash transfers, health care, and provisions for unemployment protection, the meeting became an excellent scenario for stimulating the exchange of ideas and aspirations for social protection throughout the Latin American region, including one of the first debates on the “social protection floor” as a key strategy to extend social security coverage.
e) From January 2008 to March 2010: Support for the ongoing reform

ILO technical support accompanying the process continued after the Pension Reform was enacted, both in the period prior to its start-up (March-June 2008) and after 1 July of the same year, in the application stage when it began granting new rights and benefits to Chileans. ILO officials and consultants collaborated with policy makers and technical teams throughout the process.

At the beginning of November 2008 the government, the Central Unitaria de Trabajadores (CUT) (workers’ union), and the Confederación de la Producción y del Comercio (CPC) (enterprises’ association) signed a Tripartite Agreement aiming to address the challenge of decent work as a political and social priority in the country.

The agreement was signed at La Moneda Palace by the President of the Republic, Michelle Bachelet; the Minister for Labour and Social Security, Osvaldo Andrade;
One of the five areas prioritized in this Agreement was the “implementation of a tripartite programme for education, communications, and training in issues of the Pension Reform”.

In addition, the ILO and the Office of the Undersecretary for Social Security signed a Technical Assistance Agreement aiming to increase social security coverage through deepening social security education. This materialized especially through training monitors in techniques to transmit knowledge linked to empowering all citizens in pension rights and duties. The Practical Guidelines for Pension Reform Facilitators were published for this purpose, drafted to contribute in training these facilitators, providing them with tools for working with various beneficiaries so they may act as multiplier agents capable of carrying out a social transformation through education. In this way, through its International Training Centre in Turin, the ILO held two workshops in Santiago for 40 Reform monitors from all over the country to acquire teaching and methodological skills.

The seminar “Pension Education: the International Experience” was held towards the end of November 2008 and involved analyzing initiatives carried out by leading countries of the world in pension education, as a way of contributing to create public policy in this area.

The foreign experts that participated in this event were Mary Hutch, Director of the Pensions Regulations Board in Ireland; Mike Buckley, member of the UK Royal Society of Arts; Renata Silva Melo, from the Instituto Nacional de Seguro Social in Brazil; Rafael Rofman, World Bank; Ernesto Murro, President of Banco de Previsión Social, Uruguay; and Fabio Bertranou, Expert in Social Security, ILO Subregional Office.
Similarly, as part of ILO support for the Pension Education Fund (Fondo de Educación Previsional - FEP) and in line with the Tripartite Agreement for Decent Work signed the previous year, in 2009 two training courses were held for monitors from 34 projects to acquire skills. These were projects resulting from the first tender carried out by the FEP and to which 247 initiatives were submitted.

This effort represented a remarkable contribution to the skills with which public agents relate to the community, in this case Pension Reform beneficiaries. Technical skills to communicate knowledge, form teams and networks, and mainly to strengthen citizens and their organizations—as the protagonists of rights and performers of duties—are essential skills for the success of public policy in a State that is modernizing.

In turn, through consultants the ILO supported projects winning the tender and sponsored by the Central Unitaria de Trabajadores (CUT) and by the Confederación de la Producción y el Comercio (CPC), respectively, the greatest union and enterprise associations in the country. The aim of the CUT project receiving technical support from the ILO was to create a “Union Network for Pension Education” and was put forward by the Fundación Institución de Estudios Laborales. In addition, one of the winning projects sponsored by the CPC was “Training and Assistance in Pensions for Micro-businessmen”, carried out by the Asociación Gremial de Administradoras de Fondos de Pensiones, and another on “Education and Promotion of the Pension System for Small-Scale Mining”, carried out by Fundación Sociedad Nacional de Minería.

Such activities were carried out in the context of the Programme for Tripartite Education in Pensions conducted by the ILO to contribute to the success of the second phase of Pension Reform, which extends coverage to include self-employed, independent, young workers, and to fully include domestic workers and also the bipartite voluntary savings agreed through collective bargaining. Through this type of action involving permanent cooperation, and which may be tripartite or bipartite, this Programme contributes to
pension education greatly based on knowledge and empowering in pension rights and duties.

In addition, the ILO provided support to DIPRES to create a new targeting mechanism for solidarity pensions (non-contributory and partially contributory benefits), through consultancy by Professor Nicholas Barr, from the London School of Economics, on international experience in this regard. A workshop was held to present and discuss the new pension system with authorities and officials.

Similarly, given the Pension Reform gave rise to the Institute for Occupational Safety (Instituto de Salud Laboral - ISL) stemming from the preceding INP, and as part of collaboration for institutional strengthening, technical collaboration was provided to create a financial and actuarial forecasting model and training about insurance for occupational accidents and occupational disease for officials of DIPRES, the Office of the Undersecretary for Social Security, the Superintendence for Social Security, and the Institute for Occupational Safety⁶. Activities included drafting a report about the institutional challenges facing the system for worker protection in relation to occupational accidents and occupational disease.

Other ILO activities in support of the institutionality created with the reform was financing grants for officials to participate in the Extension of Social Security course, offered by the ILO International Training Centre in Turin; a report for systemization of Chile’s horizontal technical cooperation supply in social security linked to the Pension Reform, and support for the Superintendence of Pensions to analyze social protection coverage of the unemployed.

In parallel, efforts were made to provide testimony and document experience with this reform and management process with the protagonists themselves. This resulted in the publication of two books in 2010, Historia de la Reforma Previsional chilena. Una experiencia exitosa de política pública en democracia (Arenas de Mesa, 2010) and Protección social para todos. Reforma Previsional en Chile (Délano, 2010). Similarly, this text, ILO contribution to Pension Reform in Chile (ILO, 2010), is part of efforts to give testimony, in this case of institutional support for the process.

⁶ New institution created with the Pension Reform to administer public components of the occupational hazard system.
Collaboration activities by the ILO will conclude by drafting a paper on “Challenges for Social Protection in Chile in the Bicentenary”, identifying main advances in the country in this regard in the last 20 years, and outlining challenges still ahead for this decade.
### BOX 5

**Main ILO books and documents related to pensions in Chile**

<table>
<thead>
<tr>
<th>Year</th>
<th>Title</th>
<th>Author(s)</th>
<th>Publisher</th>
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<td>2010</td>
<td>La contribución de la OIT a la Reforma Previsional en Chile</td>
<td>ILO, Santiago, Chile</td>
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<td>2010</td>
<td>Historia de la reforma previsional chilena. Una experiencia exitosa</td>
<td>Manuel Délano, ILO, Santiago, Chile</td>
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<td>de política pública en democracia</td>
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<td>Fabio Bertranou, ILO, Santiago, Chile</td>
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<td>La reforma previsional en Chile y la contribución de la OIT</td>
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<td>Jorge Bravo and Fabio Bertranou, OIT Notas N° 4, June</td>
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<td>Pensiones no contributivas. Su relevancia para la reforma previsional</td>
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<td>2005</td>
<td>Modelling the fiscal implications of the Chilean pension system</td>
<td>ILO/TF/Chile/R.15. Social Security Department, August, Geneva</td>
<td>OIT</td>
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<td>2004</td>
<td>El sistema de pensiones en Chile en el contexto mundial y de América</td>
<td>ILO, Santiago, Chile</td>
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<td>Latina: Evaluación y desafíos. Ponencias del Seminario Internacional</td>
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<td>Santiago, 22 y 23 de abril de 2004</td>
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<td>2004</td>
<td>Protección social y mercado laboral</td>
<td>ILO, Santiago, Chile</td>
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<td>2003</td>
<td>Protección Social en Chile: Financiamiento, Cobertura y Desempeño</td>
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<td></td>
<td>1990-2000. OIT, Santiago, Chile (Alberto Arenas de Mesa and Paula</td>
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<td>Benavides Salazar).</td>
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<td>Protección social, pensiones y género en Argentina, Brasil y Chile</td>
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<td>Arenas de Mesa)</td>
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<td>2002</td>
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<td>Costa Rica y Uruguay</td>
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<td>Chile (Published by: Fabio Bertranou)</td>
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<td>1992</td>
<td>“Analysis of a national private pension scheme: The case of Chile”</td>
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<td>(Gillion, C. and A. Bonilla), in *International Social Security</td>
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3. Pension Reform: Social protection for everyone

The consensus which began taking shape in the 90s and materialized in work by the Marcel Commission in 2006 about problems in quality and the extension of coverage, gender inequity, and industry performance in the Chilean individual fully-funded system, paved the way for rapid approval of the Pension Reform in Congress. Diagnosis by the Marcel Commission of the system founded in 1981 pointed to a majority of workers achieving “a pension significantly lower than their remuneration, either because they had not paid-in with the regularity needed or because the yield of their contributions was insufficient to correct this. They estimated that in another 20 years only half of all adults would have a pension higher than the minimum, less than 5% would access a minimum pension, and the remainder would have a lower pension, a welfare pension, survival pension, or no pension. Those in greater risk of being left in this situation were the most vulnerable: low-income workers, seasonal workers, self-employed workers, and a significant proportion of women (Advisory Council for Pension Reform, 2006).

Response to this diagnosis was given by Law 20 255 on pension system reform which, as explained, seeks to extend social protection, address
problems of gender equity, and overcome poverty, by adopting a solidarity pillar in the system and strengthening contributory and voluntary pillars. The main benefits of the Pension Reform are structured around three strands: return of the State to a preponderant role in the pension system; increased pension coverage for vulnerable groups; and improvement of the individual fully-funded system (Arenas de Mesa, 2010).

The first of these strands, the State returning to a preponderant role in the pension system, highlights the creation of a **solidarity pension system**, State-financed, which rests on the solidarity pillar to provide or supplement coverage for individuals who did not save sufficiently during their working life to finance a decent pension. This system involves four types of new rights:

- **Solidarity Basic Old-Age Pension**, awarded by the State to individuals aged 65 and over, among the poorest 60% of the population and with 20 years residence in the country since the age of 20, including four of the last five years.

- **Solidarity Basic Disability Pension**, awarded by the State to individuals classified as disabled by the Medical Disability Commissions and aged 18 to 65, among the poorest 60% of the population and resident in the country for no less than five of the last six years prior to submitting the application.

- **Solidarity Disability Pension Supplement**, a State contribution to supplement pensions lower than the maximum solidarity pension. To be eligible it is necessary to be 65 years of age or over and be among the poorest 60% of the population under the regime.

- **Solidarity Old-age Pension Supplement**. A variable monthly amount awarded by the State to individuals who, classified as disabled by the Medical Disability Commissions, have a pension lower than the basic disability solidarity pension and fulfil requirements of being 18 to 65 years of age, among the poorest 60% of the population and resident in the country for no less than five of the last six years prior to submitting the application.

Transition to operation of the new system, designed for the year 2012 was brought forwards by one year by the Government of Bachelet to 2011, within the context of the international crisis, to relieve the situation of lower-income families.

The system of solidarity pensions in practice implies universalizing social protection coverage guarantees for old-age. By considering these benefits for the three lowest-income quintiles, the solidarity pillar has allowed extending
ILO contribution to Pension Reform in Chile

social security in poor sectors, but also in other insufficiently covered middle- and low-income sectors. It is estimated that old-age coverage with the solidarity pillar under the Pension Reform increased in Chile from 23.9% in June 2008, the month prior to entering into effect of Law 20 255, to 30.3% in December 2008, after six months of operation, and 51.1% in 2009 (Arenas de Mesa, 2010).

Measures adopted for women, young people, and self-employed workers were highlighted in the second strand, increased pension coverage for vulnerable groups. To face the gender-inequity bias of the previous system, the reform adopted a set of measures to benefit women, highlighting among these a bonus for each live-born child, including children adopted, for all women retiring as of 1 July 2009, conceived in recognition of maternity by society. Another device which allows closing gender gaps is separation of the disability insurance premiums among men and women, returning to the latter the greatest amount applicable because of less claims, through a deposit in their individual account. A third instrument which operates in the same direction is the division of pension savings balances in case of divorce or annulment.

As to young workers, the Pension Reform provided two mechanisms for State subsidy to foster employment, encourage formalization, and increase coverage and the accumulation of pension funds. The first, already in effect, is a subsidy for hiring young people and which is given to the employer paying up to 50% of the first 24 contributions for each worker hired aged 18 to 35 and earning up to 1.5 minimum wages. In 2011 another instrument will come into effect, a State addition to the contributions paid by young people under the same conditions as above, paid directly into the individual fully-funded accounts.

For a third vulnerable group, self-employed workers, of which less than 5% save in the pension system for their old-age, the Reform determined their registration and contributions for the total taxable income, by means of a schedule ending January 2018, and that includes health contributions. This implies equalling their rights with those of dependent workers, gaining access to disability and survival insurance, receiving family benefit, affiliation to a Caja de Compensación and occupational accident and occupational disease insurance.

Regarding the third strand of the Pension Reform, improvement of the individual fully-funded system, changes aimed to improve the regime created in 1981 and which required adaptation to operate with the other three pillars –contributory and mandatory, solidarity and voluntary– and, especially, to raise standards of operation in the industry, in order to control costs, raise competition, and increase fund yields, which will result in
higher income and pensions for individuals affiliated. It was estimated that if by increasing efficiency the Pension Reform increases by 0.5% the yield of individual accounts, next generation pensions should increase by 10% (Arenas de Mesa, 2010).

The Reform embarked on a broad menu of transformations in this regard. Among these, particularly noteworthy are the extension of investment alternatives for AFPs; tenders among AFPs for the administration of accounts for new workers; subcontracting some of the services provided by the administrators, such as customer service and the administration of accounts and of funds; improvement of AFP corporate governance; creation of pension advisors; separation of the disability and survival insurance from AFP administration; improved control and inspection, protection of the interests of the individuals affiliated, and transparency of the system; establishing restrictions in case of conflict of interest and tied sales; discontinuation of the AFP fixed fee; and creating ways for individuals affiliated to participate. Additionally, to strengthen the voluntary pillar, new incentives were created as well as ways to save voluntarily, addressing middle- and low-income sectors (Arenas de Mesa, 2010; Délan, 2010).

Due to the magnitude and the number of changes introduced, as well as the need for their appropriate administration, and also the weakness of some agencies in the sector, the Pension Reform designed a new public institutionality adapted to these transformations and considering the three pillars. It is probably the greatest State institutional change in two decades, aiming to clearly differentiate at sector level the role of public policy design, regulation, and standards, as well as administration of the system, avoiding the duplication of tasks, unifying control and inspection, and making information more accessible (Arenas de Mesa, 2010).

The new institutionality leaves supervision, planning, and conduction of the system as a whole in the hands of the Office of the Undersecretary for Social Security, where technical capabilities were strengthened. In terms of regulation, the new Superintendence for Pensions, successor to the Superintendence of AFPs, concentrates control and inspection of the three pillars, whereas the recently created Instituto de Previsión Social (Institute of Social Security) absorbed most of the functions and attributions previously in the hands of the INP, and is responsible for administration of the system. The functions previously of the INP related to occupational accident and

7 The Pension Reform includes 100 measures aiming to improve pension levels (Arenas de Mesa, 2010)
occupational disease insurance are now the responsibility of the new *Instituto de Seguridad Laboral* (Institute for Occupational Safety) (Chart 1).

The Office of the Undersecretary for Social Security provides technical and administrative assistance to the new Users’ Committee which institutionalizes user participation in the pension system, involving all sector players. In turn, it administers the new Pension Education Fund, which contributes to projects and initiatives to encourage creation of a social security culture in the country. The Superintendence of Pensions contributes to the operation of the new Technical Council for Investments, which convenes representatives from the Executive branch, the Board of Governors of the Central Bank, the AFP industry, and the academic world, to draft reports and proposals regarding the investments made by pension funds.

**Chart 1**

**New pension system public institutionality**

Source: Budget Office (2008)
On the anniversary of its second year of life in March 2010, the Pension Reform is operating with most of its mechanisms. There are indicators showing coverage is increasing, as mentioned earlier, and headway can also be seen in terms of gender equity: 65% of basic solidarity pension beneficiaries (old-age and disability) and solidarity pension supplements (old-age and disability) recorded until July 2009 are women (Délano, 2010). As to the impact of the Pension Reform on income, expectations among State authorities who directed these changes were that by the year 2013 they would allow ending poverty among the elderly and the disabled. In any case, the decisive stress test for this social transformation is being applied by the individuals who receive the benefits each month and exercise the rights awarded by the Pension Reform.

“Social security is very important for the well-being of workers, their families and the entire community. It is a basic human right and a fundamental means for creating social cohesion, thereby helping to ensure social peace and social inclusion. It is an indispensable part of government social policy and an important tool to prevent and alleviate poverty. It can, through national solidarity and fair burden sharing, contribute to human dignity, equity and social justice. It is also important for political inclusion, empowerment and the development of democracy”.

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