

# Pension Notes

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## **Eleven proposals for increasing contributory pension coverage in Latin America**



Federación Internacional  
de Administradoras  
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### Executive Summary

Due to the low percentage of workers who actually contribute to contributory pension programs, 60% of adults over the age of 65 in the Latin American region, on average, do not receive a contributory pension.

Given this scenario, we are faced with the challenge of increasing contributory pension coverage. We have highlighted eleven alternatives from among the existing proposals for achieving this objective.

First, sustainable economic development must be promoted through a variety of policies, because this generates greater labor formality. For example, one could consider advancing economic development by reducing bureaucracy, using new technologies to increase efficiency and competition, improving education and training, and boosting infrastructure.

Second, it is essential to promote policies that reduce labor informality. First, for example, through measures aimed at improving the labor market, such as: (i) reducing the costs of formal employment and employment contracts; (ii) promoting formal employment for women, which requires greater labor flexibility and maternity benefits (such as universal day-care centers); (iii) promoting formal employment among the elderly, through greater labor flexibility, while reducing age discrimination, rewarding companies that focus their recruitment on the older segment and investing in technological cooperation training; and (iv) promoting formal employment for young people through greater study/work flexibility, hiring subsidies, policies that reduce school drop-outs and establish a lower minimum wage for them.

Within the same objective of reducing informality, one could also consider policies aimed at improving social security design, such as: (i) adjust

the official retirement ages to reflect the increase in life expectancies on retirement (this influences the effective retirement age and policies for the severance of older people in companies); (ii) take into account the impacts that individually funded pension systems have on coverage, compared to PAYGO systems (greater incentives to contribute granted in the former than in the latter, since contributions are personal savings over which members have ownership rights, and furthermore, in the latter, the right to a pension is forfeited if a minimum number of years of contributions are not met); (iii) provide access to other basic social security benefits when enrolled and contributing to pension programs (for example, health insurance or others); (iv) review the requirements for accessing the benefits of social programs that discourage contribution to contributory pensions; and (v) design a non-contributory pension pillar that does not discourage contributions to contributory programs.

A third alternative is the need to educate and communicate the benefits of the contributory pension system, since if people do not receive them, they do not see the need to increase or improve their pensions.

Fourth, the pension evasion and avoidance issue has to be contained: by increasing the effectiveness of the process for monitoring workers' contribution payments; improving workers' pension information and education; reducing labor costs and reviewing the design and correlation of the existing social programs.

Fifth, further progress must be made in the mandatory incorporation of the self-employed with savings capacity into the pension system.

Sixth, income tax collection and returns should be used to include new groups of workers in the contributory pension system.

Seventh, attempts should be made to take advantage of the contribution formalization procedures in certain modest sectors of the self-employed with some saving capacity (such as for example, artisanal fishermen, taxi drivers, circus workers).

Eighth, incentives for voluntary participation in contributory pension programs should be augmented. This will require promoting the development of the financial system; improving fiscal or tax incentives for voluntary savings (for example, tax incentives for pension contributions made by the self-employed and defining tax incentives for lower-income workers who do not pay taxes); improving the liquidity of voluntary savings, while establishing disincentives for withdrawals; increasing competition in the voluntary pension savings industry, authorizing different entities to manage such plans, without costs or obstacles to transfers; and creating collective voluntary savings mechanisms with automatic enrollment.

On the previous point regarding the promotion of the development of the financial system, it must be emphasized that it would appear to be totally counterproductive to implement public policies that can work against this objective in the long term, for example, through reforms that divert social security contributions to a collective PAYGO fund and establish benefits that mostly end up being financed with resources from the public budget.

Ninth, we must explore contribution collection through the consumption of workers (for example, determining that a percentage of the consumption tax should go to the individual accounts of workers; or establishing default rules that involve allocating a part of the consumption to individual savings through technological applications).

Tenth, simple contribution mechanisms must be defined, using existing technology, so that low-

income and irregular workers can contribute smaller amounts at flexible time intervals that are more suitable to their reality. This can be achieved efficiently through micro-pension applications, which allow their participants to contribute to their savings accounts in small amounts, daily or weekly.

And finally, as an eleventh measure, we must look for ways to provide liquidity to the non-financial savings accumulated by retirees (for example, transforming the value of real estate, while continuing to use it, into a contributory pension flow, commonly known as a “reverse mortgage”).

## I. Introduction

In Latin America and the Caribbean, contributors to mandatory contributory social security systems (including individually funded and PAYGO systems) make up 44% of the Economically Active Population (EAP), while that figure is around 72% in OECD countries. This figure shows that, on average, only 4 out of 10 workers contribute to some kind of pension system, a phenomenon directly related to the degree of economic development and the informality of labor markets in the region. As expected, coverage changes depending on income level: while in the two lowest-income quintiles, only 1 or 2 out of 10 people, on average, contribute to a social security system, whereas in the two highest-income quintiles, 5 or 6 out of 10 people, on average, contribute (see Graph 1).

The region's low contribution coverage has resulted in a serious problem of lack of protection during active working life and in old age. In fact, only 40% of adults over 65 years of age in the region, on average, receive a contributory pension, due to the predominant high informality and the fact that pension systems were designed to rely on a formal wage labor market. When including non-contributory pensions, this

percentage rises to 59% (see Graph 2), which implies that 41% of senior citizens do not receive any kind of income.

In response to the low percentage of workers receiving a contributory pension and the inadequacy of average pension amounts granted by contributory systems as a result of low pension savings and retirement ages, non-contributory pensions have gained traction since 2000, but their implementation entails design and sustainability challenges<sup>1</sup>.

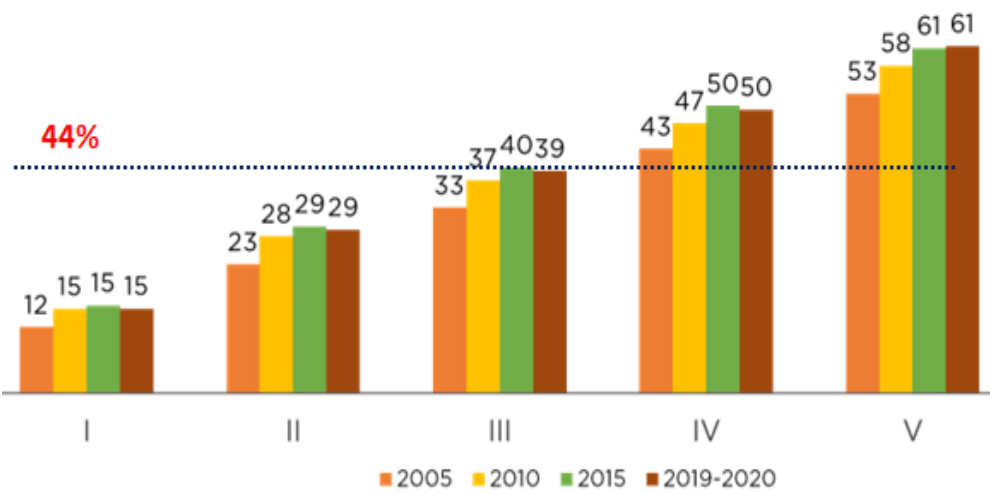
An increase in contributory pension coverage (measured as the percentage of workers who effectively contribute to the contributory pension program) to OECD levels, would imply that pension amounts, on average, would almost double, significantly easing the fiscal pressures of countries associated with the development and/or expansion of non-contributory pension programs. What proposals would allow us to move towards the objective of increasing contributory pension coverage? In this pension note we conduct a review and highlight eleven proposals in this regard.

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<sup>1</sup> For further details on the challenges involved in

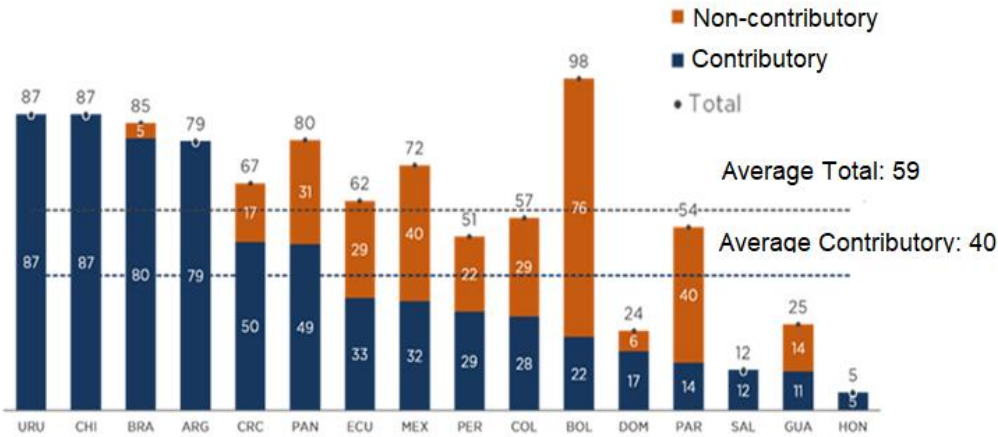
implementing non-contributory pension systems, please see [FIAP Pension Notes No.66](#).

**Graph 1**  
**Active workers contributing to social security in Latin America, by income quintile**  
**(% EAP, 2005-2020)**



Source: Tapia, Waldo (2022).

**Graph 2**  
**% of the population over 65 years of age receiving a pension in Latin America**



Source: Tapia, Waldo (2022).

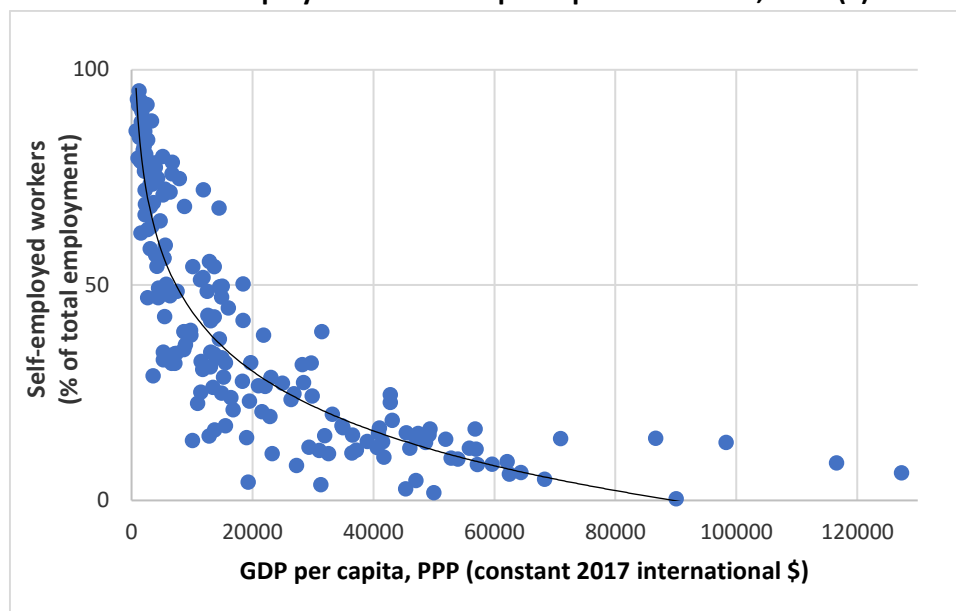
## II. How to increase contributory pension coverage?

On reviewing the literature and international experience, the following eleven alternatives that enable increasing the contributory coverage of pensions, stand out:

1. **Adopt policies that promote sustained economic development.** There is abundant evidence<sup>2</sup> that shows a positive relationship between the degree of economic development of a country and the level of coverage of its pension programs. This is because formal enterprises expand as countries develop, and they become more productive and efficient. This increase in the formality of

the economy translates into an increase in the percentage of workers who pay pension contributions (increase in the contributory coverage of pension systems). This is evident in Graph 3, which shows a strong negative correlation between the country's per capita output and the informal sector of economic activity (as measured by the participation of the self-employed in total employment). Conversely, informality diminishes as an economy develops. Thus, adopting economic policies that promote economic development constitutes the first ingredient of the solution to the problem of low contributory pension coverage, although their effects occur gradually over time and also depend on other factors that affect labor markets.

**Graph 3**  
**Informal employment and GDP per capita worldwide, 2019 (\*)**



Source: FIAP based on World Bank World Development Indicators.

(\*) Ratio considers a set of 176 countries worldwide.

<sup>2</sup> See Holzmann and Packard (1999); Palacios and Pallares-

Miralles (2000); World Bank (2001); Gollin (2008); La Porta and Shleifer (2014); McCaig and Pavcnik (2015).

What kind of economic policies would help us further economic development? There are many options, but to name a few, according to the *Instituto Libertad y Desarrollo*<sup>3</sup>, there are at least four main lines of action that would enable increasing the capacity for growth in a sustainable manner:

- (i) **Reduce bureaucracy.** Optimize Government processes, simplify procedures and eliminate unnecessary requirements, so as to speed up the creation of new ventures and the execution of investment projects through greater efficiency in the management and services provided by the State.
- (ii) **Adapt regulations to allow companies and individuals to use new technologies that enable greater efficiency and competition.** Rules and regulations must be modernized to allow innovation and different business models in the face of the technological transformations occurring worldwide.
- (iii) **Improve education and training.** The technological revolution is changing the way we live, learn and work. However, to truly harness the potential of these tools and integrate technology into production processes, the digital and necessary skills of the population must be honed.
- (iv) **Boost infrastructure.** Infrastructure investment can boost growth and job creation during construction; increase the growth capacity of the long-term economy when the works are in service; and increase productivity (due to greater efficiency of the logistics chain and time saving). It is worth mentioning that one of the major drivers of infrastructure is investment, financed with the resources of long-term institutional investors, such as pension fund managers. In fact, pension fund

investment has contributed to the realization of infrastructure improvement projects (roads and transportation; housing, energy, telecommunications; sanitation and health; among others) in the different countries in which the individually funded systems operate, at a lower capital cost, increasing the standard of living of workers and their families and favoring increases in the efficiency and productivity of the different productive sectors<sup>4</sup>.

<sup>3</sup> See LyD (2020). "[Propuestas seleccionadas de agendas previas para reactivar el crecimiento](#)". Serie Informe Económico N° 286.

<sup>4</sup> See FIAP (2020). "[As Europe advances towards individual capitalization, some in Latin America advocate return to Pay-as-You-Go](#)" page 70.



2. **Adopt policies to reduce labor informality.** We group these policies into 2 broad areas:

**A. Labor Market**

- i) **Reduce the costs of formal employment and employment contracts.** In most countries, the incorporation of companies is discouraged by a wide variety of legal rules and regulations, tax requirements and bureaucratic procedures. At the same time, labor legislation often raises recruitment costs due to the existence of obstacles and high severance costs, inefficient collective bargaining rules, the obligation to adopt wage schemes not associated with productivity, and minimum wages set at levels unrelated to labor market conditions. All these “incentives” to labor informality make it difficult to increase pension coverage. In this regard, we can cite as an example the case of Colombia, which in 2012 implemented a tax reform that reduced payroll deductions other than pension contributions (the so-called “non-wage costs”), but that employers had to pay if they wanted to formalize their workers and have them contribute to pensions. The effect of that reform has been extensively assessed, and all studies indicate that it served to increase formality, although only moderately<sup>5</sup>.
- ii) **Encourage the formal employment of women.** Women have the greatest coverage issues, which is why it is of the utmost importance to promote quality female employment. In this regard, the literature points out that motherhood is a

great barrier to labor formality in women. In fact, there are studies that show that the birth of the first child increases informality among women, an impact that is greater the lower the level of education.<sup>6</sup> What policy design can reduce this barrier? Some public policies that can help to reduce this barrier, are: (i) improve labor flexibility (flexible working hours, telecommuting); and (ii) maternity/paternity aids (nursery or universal nursery regulations; childcare costs that are not absorbed only by the woman; provision of vouchers for kindergarten costs; improving/establishing paternity leave).

- iii) **Encourage formal employment among the elderly.** Among the measures that would enable achieving this objective, we can mention:
- a. **Strengthen or implement the special remote contract.** Working from home is a powerful way to stimulate the participation of various groups, including senior citizens, who may be more willing to work from home or have greater difficulty moving.
- b. **Establish working hour flexibility.** There are certain types of work, in the commercial sector, for example, in which workers can work part-time (senior citizens in the mornings and students in the evenings).
- c. **Implement downward mobility when a senior reaches a certain level in the company.** There will be fewer young people in the labor market in the future, so older people will have to extend their working careers. To this end, companies

<sup>5</sup> See Ministry of Finance and Public Credit. “[Tax reform and labor informality in Colombia: A Dynamic and Stochastic General balance Analysis.](#)”

<sup>6</sup> See study for the case of Chile. Berniell, Inés, Lucía Berniell,

Dolores de la Mata, María Edo, Mariana Marchionni (2020)). “Gender Gaps in Labor Informality: The motherhood effect”. Journal of Development Economics.



should implement a downward mobility system, i.e., make it possible for older professionals to carry on working in lower-ranking positions, with ample training opportunities.

- d. **Strengthen training programs.** There is a need for training programs to teach senior citizens and hone their skills, focusing on technological skills, since the largest generational gap is precisely in this area. Hence, there should be an Information and Communication Technologies (ICT) program to facilitate the entry or reinsertion of this group into the market.
- e. **Raise awareness among the general population about the need to eliminate prejudice and age discrimination against senior citizens.** There are certain organizations whose policies encourage the severance of workers for merely having reached the official retirement age, without considering whether an individual is fit to stay on the job. This is a loss for society, since it entails excluding people who are still fit to work. According to the United Nations<sup>7</sup>. “Ageism” in the elderly is associated with poorer physical and mental health, greater social isolation and loneliness, greater financial insecurity, lower quality of life and higher rates of premature death, which is why it points out that educational activities that improve empathy and combat misconceptions, and intergenerational activities to reduce prejudice, can be helpful. In this regard, two innovative ideas for intergenerational support are:
  - **Establish support programs.** Companies can implement these programs among senior and junior workers, to encourage the intergenerational transmission of knowledge between them.

- **Create arrangements whereby senior citizens can supervise young workers**

doing their practice while they finish their studies. As an example of the aforementioned practices, we can cite Chile’s “Talento Senior” program (in which younger workers provide technological advice to older workers, enabling them to keep up with technological advances); and the Plenus distinction of the Carlos Vial Espantoso Foundation,<sup>8</sup> (which promotes collaborative labor relations within companies).

- f. **Reward companies that focus on hiring senior citizens.**
- iv) **Encourage the formal employment of the youngest.** For example, through the following measures:
  - a. **In periods of lower economic growth, provide subsidies to companies that hire young people.** The effectiveness of these subsidies is partially dependent on:
    - Public finances being reasonably buoyant, so that when a slowdown or recession begins, fiscal expansion can be implemented immediately (before the economic crisis itself causes a worsening of the fiscal budget).
    - Elements that promote the acquisition of skills for employment among young people are incorporated. These programs need to be in place long enough for participants to develop employment-related skills that can be tested in the specific work environment.
    - Grants are generous enough to attract businesses and should be directed to specific groups of young people (for

<sup>7</sup> See: <https://www.who.int/es/news/item/18-03-2021->

[ageism-is-a-global-challenge-un](https://www.who.int/es/news/item/18-03-2021-ageism-is-a-global-challenge-un)

example, those at risk of long-term unemployment)<sup>8</sup>.

- b. **Make working hours more flexible to increase the employment rate of young people**, allowing them to study and work at the same time.
- c. **Eliminate the minimum wage for young people, or failing that, establish a minimum wage for young people that is lower than the general minimum wage**, in order to encourage the employer to hire workers from that age group.
- d. **Establish policies to enable reducing school dropout rates**. Higher levels of schooling increase the likelihood of employment, so it seems pertinent to seek to reduce school dropout rates, for example:
  - By establishing a family allowance for children from lower-income households attending middle school.
  - By improving the quality of primary and secondary education. The decision to educate oneself is strongly influenced by the expected results of this process. Better education that ensures better possibilities of future employment should discourage school dropout.<sup>9</sup>
- e. **Establish measures to reduce ageism towards the youngest**. Just as there is ageism towards the elderly, it also frequently occurs towards the younger sectors (there is a greater tendency to choose someone who has been working for a large number of years). Therefore, here there is also room for improvement in this aspect, through educational activities and intergenerational support programs.

## **B. Social security design**

- i) **Adjust official retirement ages to reflect increased life expectancy on retirement**. The official retirement age is not only important for pension outcomes but is also a relevant reference influencing the effective retirement age of individuals, and policies governing the severance of senior citizens in companies. In this regard, it seems extremely relevant to choose an adequate official retirement age for the design of social security.
- ii) **Consider the impacts of the individually funded pension systems on coverage, compared to the PAYGO systems**. On the one hand, the individually funded systems provide greater incentives to contribute than the PAYGO systems, since contributions are personal savings on which members have ownership rights. On the other hand, in the individually funded systems, all workers with savings in their accounts will be entitled to a pension, or the total withdrawal of their accumulated balances, including the returns obtained. However, in the PAYGO systems, a minimum contribution period is generally required for accessing a pension, and those who fail to meet this condition are deprived of this benefit.
- iii) **Provide access to other basic social security benefits when enrolled and contributing to pension programs (e.g., health or other insurance)**. This

<sup>8</sup> See ILO (2017). "[Rising to the youth employment challenge: New evidence on key policy issues](#)".

<sup>9</sup> See Beyer, Harald (1998). "[Youth unemployment or a school dropout problem?](#)". Estudios Públicos (CEP).

would encourage informal workers to become formal workers.

- iv) **Review the requirements for accessing the benefits of social programs that discourage contribution to contributory pensions.** Countries usually have several social programs that help those most in need and in many cases access to such benefits and their amounts are either lost or reduced when people become formally employed. This affects people's willingness to formalize their employment status and contribute to the pension system. For example, social policy based on subsidies<sup>10</sup> may eventually establish erroneous incentives if it is not carefully designed, since depending on the beneficiary's level of income, it can encourage the underreporting of income (commonly known as "avoidance"), negatively affecting the future pension. A study by the Public Policy Center of the Catholic University of Chile (2012)<sup>11</sup> found that, of the 25 social programs analyzed in Chile, at least 20 generated some degree of lack of interest in contributing. Thus, it would appear to be of the highest priority to carefully design these

social policies to minimize income underreporting and informality.

- v) **Design a non-contributory pension pillar that does not discourage contributions to contributory programs**<sup>12</sup>. The ideal situation would be for non-contributory pensions (whose amounts meet the objective of reducing poverty in old age, are sustainable and can be financed in the long term) to be progressively financed, i.e., with resources mostly from high-income sectors, which distort the economy in general, and the labor market in particular, as little as possible. That is why this financing must come from the public budget (i.e., from taxes applied to both labor and capital income), and not from social security contributions (labor tax), as recommended by international institutions such as the OECD, since in this case the incentives to work in the formal labor market and to contribute to contributory programs are negatively affected. Furthermore, the amount of the non-contributory pension should be such that it does not discourage contribution to the contributory pillar.

<sup>10</sup> Health allowances, pensions, family and housing allowances, women's work bonus and others.

<sup>11</sup> "Pensions and Social Programs: Main Incentives and Disincentives to Pension Behavior." Joint Study by the Social Security Advisory Council and Commission of Users of the Pension System, commissioned by the Chilean Deputy

Secretary of Social Security.

<sup>12</sup> For more details on the proper design of non-contributory pension systems, please review FIAP Pension Note No.66 "[Analysis and evolution of non-contributory old-age pensions in Latin America](#)".

**3. Educate and communicate the benefits of the contributory pension system.** The benefits of the contributory pension system are generally perceived to be insufficient. If these benefits are not evident, people do not see the need to increase or improve their pensions. Hence, improving education and communication regarding the benefits of these systems helps to improve pension coverage. In this case, it would be a good idea to introduce courses in financial and social security education in universities.

Thus, local financial and social security education campaigns, which can be promoted by the industry with the help of the public sector, are particularly relevant. According to the OECD<sup>13</sup>, national pension communication campaigns are effective when designed in accordance with clearly established and measurable objectives. A notable example is the case of Mexico, in which the National Commission for the Retirement Savings System (CONSAR) and the Pension Fund Managers (AFORES) jointly hold the annual Afores Fair (since 2009), thus contributing to financial education and social security culture awareness. To the same end, the AFORES also participate in the National Financial Education Week, organized by the government.

**4. Reduce Social Security evasion and avoidance.** Social Security evasion (non-payment of pension contributions<sup>14</sup>) and Social Security avoidance or under-declaration

(which occurs when the employer pays contributions on part of the salary and not on the total<sup>15</sup>) are important factors that reduce the coverage and collection of contributions, so it is essential to take measures to reduce their effects, such as:

(i) **Improve the effectiveness of the auditing of workers' contribution payments.**

Greater oversight is needed to detect the non-payment of contributions and impose adequate penalties. For example, among the proposals put forward to contribute to this objective<sup>16</sup> in Chile are the strengthening of the oversight activities of the Labor Directorate; the prioritization of oversight in economic sectors, companies and types of workers with greater problems of evasion and avoidance; a better structuring of oversight and coordination between the institutions involved, with an agency clearly responsible for the final results; the review of incentives and penalties for non-payment of contributions; strengthening of the funding and reach of the specialized courts to handle the demand for cases involving pension collection and the judicial collection attributions of the AFPs, allowing them to act jointly in cases against employers by all their workers.<sup>17</sup> Another example is El Salvador, where a Comprehensive Law of the Pension System recently<sup>18</sup> created a public agency to

<sup>13</sup> See OCDE Pensions Outlook (2020). Chapter 7: "[Communicating on investment strategies.](#)"

<sup>14</sup> There are two possible reasons for non-payment of contributions: that the employer discounts the contributions from wages and does not pay them to the corresponding fund manager; or that it keeps the worker as a dependent, but without a formal contract.

<sup>15</sup> This is explained by the fact that agreements are often reached on the non-taxable parts of wages (e.g. transportation and food), in both private and public sectors. The estimates for Chile show that avoidance (non-taxable allocations) in some companies can be up to 18% of salary.

There are important non-taxable components of wages in the public sector.

<sup>16</sup> See Faculty of Economics and Business, University of Chile (2012). "Analysis of evasion and avoidance in the payment of social security contributions and public policy measures to remedy their causes." Joint study of the Pension Advisory Council and the Commission of Users of the Pension System.

<sup>17</sup> See Association of AFPs (Jun3, 2014). "Chilean Pension System: Diagnosis and Proposals for Improvement." Rodrigo Pérez M., Chairman.

<sup>18</sup> <https://www.presidencia.gob.sv/inicia-en-la-asamblea-estudio-de-reforma-de-pensiones-propuesta-por-el->

oversee compliance by all employers with the obligation to send the social security contributions discounted from workers to the AFPs (evasion in this country affects about 100,000 workers).

- (ii) **Improve the information and pension education of workers.** Workers must be the main auditors and be aware that the more they contribute, the better their pensions will be, so the solution partly involves more education and welfare culture (see point 3).
- (iii) **Reduce labor costs** [see point 2.A. i) above]
- (iv) **Review the design and correlation of the different existing social programs,** to avoid or minimize incentives to evade and under-report contributions to pensions, with the aim of improving the benefits received in other social security programs (see point 2.B.ii above).

**5. Mandatory incorporation of self-employed workers with savings capacity<sup>19</sup>.** The existing evidence justifies the obligation to contribute to pension systems, basically because of what is known in the literature as "intertemporal myopia": during the active work stage, individuals are not able to anticipate their requirements in old age, so they do not voluntarily save and have a high preference for present consumption. By forcing them to contribute, pension systems seek to protect them against this unforeseen situation, offering them a sufficient and stable income to

avoid poverty in old age, as well as avoiding or reducing the likelihood that they will be a burden for the State in the passive stage. In the Latin American countries with individually funded programs, only Uruguay and Chile make it mandatory for the self-employed who issue fee ballots to pay pension contributions, in order to guarantee them protection similar to that of salaried workers, as of the 2019 tax campaign. In other countries such as Bolivia, Costa Rica, El Salvador, Mexico and Peru, self-employed workers can only contribute voluntarily to the pension system. In the Dominican Republic, self-employed workers still do not have the option to make pension contributions<sup>20</sup>. However, a recent proposal by the country's Association of AFPs (ADAFP), called for integrating independent workers, freelance professionals and the self-employed, with a contribution on presumptive wages, starting at the minimum wage. Despite the efforts of different countries to incorporate self-employed workers (as in Colombia and Peru), political pressures have made it difficult to legislate and then enforce the rules and regulations that make it mandatory for them to contribute.

**6. Use income tax collection and tax returns to add new groups of workers to the contributory pension system.** For example, the companies that self-employed workers render services to in Chile withhold a percentage of their gross income, which must be paid to the Treasury. Contributions to the different social programs are paid with these withheld amounts<sup>21</sup>. Such measures should be

[gobierno-del-presidente-nayib-bukele/](https://gobierno-del-presidente-nayib-bukele/)

<sup>19</sup> Low-income self-employed workers would best be covered by non-contributory programs financed with resources from general taxes.

<sup>20</sup> This is despite the fact that Law 87-01, which introduced the individually funded system, provided for the mandatory participation of self-employed workers in the Subsidized Tax Regime, which is still not operational to date.

<sup>21</sup> The mandatory contribution for self-employed workers who issue fee slips gives them access to all social security benefits, ensuring them the same protection as dependent workers. Mandatory contributions by self-employed workers began in the 2019 tax campaign, receiving Social Security coverage as of July 1 that year. The amount withheld on fee slips, which was 12.25% in 2022, (and will gradually increase to 17% by 2028), enables the obtainment of pensions and

analyzed very carefully in countries with high levels of informality.

In the case of Chile, some studies<sup>22</sup> propose using the General Treasury of the Republic to collect the contributions of other self-employed workers who, although they do not issue fee slips, also pay income tax (either through activities that benefit from the "presumed income" regime such as transportation, mining and the exploitation of agricultural and non-agricultural real estate; or through activities covered by the "effective income" regime).

**7. Take advantage of formalization to contribute.** For example, in activities requiring municipal permits, the permit may be subject to the payment of social security contributions, or applicants demonstrating a certain number of contributions to the pension system may be awarded higher scores for projects with state subsidies. For certain modest self-employed sectors that have some savings capacity (e.g., artisanal fishermen, taxi drivers, circus workers), an alternative is that the rule should allow for the presumption of a basic income on which to contribute, and that the contribution is a requirement for receiving work permits and State subsidies.

**8. Maximize incentives for voluntary participation in contributory pension programs.** To this end, it is necessary, for example:

- a. **To promote the development of the financial system.** Access to services that meet a secondary function as a savings mechanism is of paramount importance in promoting voluntary contribution to the pension system. Thus, many families prefer to invest in services such as the education of children or health provision, in addition to saving on assets that can provide them with liquidity when required. It follows that for a self-employed worker, the probability of contributing increases with access to bank credit. Hence, the development of the financial system should be one of the main objectives if greater voluntary participation in pension systems is sought<sup>23</sup>. Thus, it would appear to be totally counterproductive to implement public policies that can reduce the depth of the financial market in the long term (for example, policies that divert social security contributions to a collective PAYGO fund and establish benefits that mostly end up being financed with resources from the public budget).
- b. **Improve fiscal or tax incentives for voluntary savings.** For example, tax incentives for social security contributions made by self-employed workers can be improved and tax incentives for lower-income workers who do not pay taxes can be defined, in addition to simplifying effective access to established incentives. In fact, self-employed workers are not allowed to deduct social security contributions from their taxable base income in many Latin American countries. Together with the illiquidity of social security savings, these are sufficient reasons to explain their very low contribution density.

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coverage in health, social security, accident, and occupational disease insurance, among others.

<sup>22</sup> See Martínez, Claudia and Esteban Puentes (2011). "Trabajadores independientes: identificación y características de los distintos grupos y medidas para aumentar su incorporación al sistema de pensiones y densidad de cotizaciones". ("Self-employed workers: identification and characteristics of the different groups and

measures to increase their incorporation into the pension system and contribution density")

<sup>23</sup> See Fuentes, Eduardo (2010). "Incentivizing the voluntary contribution of self-employed workers to pension funds: an approach based on the Chilean case." BBVA Working Papers No.10/11.



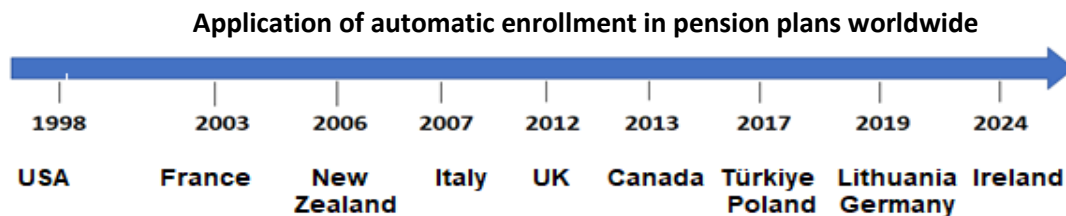
- c. Improve the liquidity of voluntary savings, while establishing disincentives to withdrawals.
- d. Increase competition in the voluntary pension savings industry, allowing different agencies to manage these types of plans, without costs or obstacles to transfers.
- e. Create voluntary collective savings mechanisms with automatic enrollment.

Automatic enrollment in voluntary pension savings plans has been one of the main driving forces of individual funding at an international level, due to its effectiveness in increasing the coverage of this type of savings<sup>24</sup>. By 2024, at least 11 countries will be implementing this mechanism, helping to supplement the sources of income for the retirement of thousands of workers (see Figure 1). In fact,

more than 50% of countries with this mechanism rank in the top 20 of the Mercer 2022 Global Index (Germany; Canada; United States; Ireland<sup>25</sup>; New Zealand; and the United Kingdom).

Given this international experience, it is imperative to be able to advance in the creation of voluntary savings mechanisms with this characteristic. For example, in the Dominican Republic, the country's Association of AFPs (ADAFP) has proposed the creation of such a mechanism, in which employers and workers would contribute a similar percentage, tax-free, and would also have options for early withdrawal and even exclusion of workers themselves from the system if they do not want to be part of it

Figure 1



Source: FIAP based on OECD Pensions Outlook 2022; "Best practices and performance of auto-enrollment mechanisms for pension savings" (European Commission); and <https://irrationalretirement.com/2021/12/16/what-a-shocker-automatic-enrolment-in-retirement-plans-works-how-it-started-and-how-to-make-it-better/>

In addition to automatic enrollment, other default options of voluntary savings plans that help workers make decisions and increase savings are the definition of default portfolios for those who do not choose investment structure and the automatic and gradual increase in the contribution rate over time (often referred to in the literature as "automatic scaling"), which can help members achieve adequate contribution levels throughout their working careers.

9. **Explore the collection of contributions through the consumption of workers.** To this end, different mechanisms can be used, such as, for example, determining that a percentage of the Value Added Tax (VAT) goes to the individual accounts of workers (the estimates for Chile show that pensions could increase between 8% and 30% with 1% of VAT). Another possibility is to establish default rules that involve allocating a part of consumption

<sup>24</sup> Automatic enrollment uses some of the characteristics of individual behavior, such as inertia and procrastination, to keep people in a pension plan, since the default value in such

cases is to participate. At the same time, the opt-out option maintains individual choice.

<sup>25</sup> Since 2024.



to individual savings through technological applications<sup>26</sup>. One of the advantages of these mechanisms is that it would allow contributions to be collected even for informal workers. In this regard, it is noteworthy that the Uruguayan government recently presented a draft reform to the pension system<sup>27</sup>, which, among other things, establishes a voluntary savings plan for consumption.

- 10. Define simple contribution mechanisms using existing technology, so that low-income and irregular workers can contribute smaller amounts, and with flexible time intervals that are more suitable to their reality.** In private pension plans, workers' contributions are usually deducted monthly from their wages. However, as low-income and working groups with irregular income streams are more inclined to make small payments at flexible time intervals, micro-pension applications have recently begun to appear, allowing participants to contribute to their savings accounts in small amounts and on a daily or weekly basis.

An example of micropension application is PinBox Solutions<sup>28</sup>, a fintech dedicated to the digital inclusion of micropensions in Asia, Africa, Latin America, and the Caribbean. This fintech<sup>29</sup> contemplates micropension, liquid savings and insurance components, and a digital payment scheme. The micro-pension component is designed to provide a flexible

“defined contribution” retirement solution. The liquid savings component enables members enrolled in this scheme to access resources to meet financing needs, such as savings for their children's education, marriage and emergencies. The insurance pillar for risks such as health, death, among others, provides the necessary peace of mind for dealing with these types of highly volatile situations. All of this is complemented by a digital payment scheme (initiated through a WhatsApp chat) to save and withdraw funds automatically.

- 11. Look for ways to provide liquidity to non-financial savings accumulated by pensioners.** For example, most older workers' wealth is probably in the form of homes of their own. Systems known as “reverse mortgages”<sup>30</sup> open up the possibility of transforming real estate value into a contributory pension flow (while continuing to occupy the property), representing a very attractive alternative for this sector of the population. Furthermore, by alleviating the lack of income during old age, this type of mechanism, can help reduce poverty levels at this stage (there are studies<sup>31</sup> showing that the poverty rate could be reduced by up to 15%), improving the well-being of people who opt for this alternative. In this regard, it is worth mentioning that this alternative is contemplated in the recent proposal to reform the Uruguayan pension system.<sup>32</sup>

<sup>26</sup> For more details on pension saving mechanisms through consumption, please review Pension Note No.56 “[El ahorro través del consumo como una fuente complementaria para financiar las pensiones](#)”. (“Saving through consumption as a complementary source for financing pensions.”)

<sup>27</sup>[https://medios.presidencia.gub.uy/legal/2022/proyectos/10/cons\\_min\\_661\\_mensaje.pdf](https://medios.presidencia.gub.uy/legal/2022/proyectos/10/cons_min_661_mensaje.pdf)

<sup>28</sup><https://www.pinboxsolutions.com/>

<sup>29</sup> See Gautam, Bhardwaj (2022). “[Making saving for old age and risk management easy and simple. For everyone. Everywhere](#)”. Presentation at the FIAP 2022 International Seminar; and Tuesta,

David (2022). “[Superando las barreras para el desarrollo de micropensiones](#)” (“Overcoming barriers to the development of micropensions.”)

<sup>30</sup> See FIAP (2020). “[The challenges of Reverse Mortgage as a mechanism for supplementing pensions](#)”.

<sup>31</sup> See Ruiz, José Luis et al. (2019). “[The social and economic effects of introducing reverse mortgages in Chile](#)”.

<sup>32</sup>[https://medios.presidencia.gub.uy/legal/2022/proyectos/10/cons\\_min\\_661\\_mensaje.pdf](https://medios.presidencia.gub.uy/legal/2022/proyectos/10/cons_min_661_mensaje.pdf)

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