SOCIETY OF ACTUARIES®

Article from

Retirement News

February 2019

Issue 97

International Pensions Spotlight: Chile

By Josh Bank with Octavio Rojas

This piece is the result of a joint effort begun when Josh Bank recruited Octavio Rojas, a seasoned Venezuelan actuary and one of the speakers in session 85PD of the 2018 Society of Actuaries (SOA) Annual Meeting and Exhibit, for his deep knowledge of national pension schemes in Latin America. Part of Octavio's assignment was to provide an update on the status of Chile's watershed mandatory defined-contribution scheme, installed in 1981. The program was part of Augusto Pinochet's overhaul of that country's economy following the failure of previous government-run programs. The main change Pinochet's program brought about is the requirement of all workers to put 10 percent of their income into private savings accounts.

As the date of the 85PD session (Oct. 26, 2018) approached, there was a lot of buzz about impending changes to the famous national DC plan. Although imitated in one form or another by many other countries in the region and worldwide starting around the year 2000, it was found to be overly simplistic and naive in its conception.

Octavio, through his extensive network of Latin American contacts, learned from a highly placed individual that a major development was imminent, but details were as yet unavailable. Therefore, his talk on the Chilean system was not completely up-to-date, though it was still well received.

Just two days after that session, Chile's president, Sebastián Piñera (son of José Piñera, the minister of labor and social security under Pinochet and presumptive father of the national DC plan), took to the airwaves to present a bill proposing to realign the pension scheme with current economic and demographic reality. Octavio obtained the text of President Piñera's speech, which was published as a press release of the national government. Josh then prepared the following translation. To our knowledge, it is the only (American) English translation of the Chilean president's pension reform bill.

NATIONAL PRESS RELEASE: 28 OCTOBER [2018]—PENSIONS

From His Excellency the President of the Republic, Sebastián Piñera Echenique, announcing Pension Reform Bill.

Dear Fellow Citizens:

The priorities of our administration are the priorities of all Chileans: public security, employment, salaries, health care, education and a new and better deal for our children, our middle class, our regions and our older adults, in such a way that better times will be enjoyed by all Chilean households.

A new and better deal for our older citizens is the objective and the central motivation for this pension reform legislation, which we share with all of our fellow citizens.

This mission becomes all the more important as we account for the fact that our population is aging, because fewer children are born each day, and we need to promote higher birth rates, and because each day we live longer, and we need to improve the quality of life during those additional years of life.

Today in Chile, there are already 3 million elderly adults who, for the first time, outnumber our children and youths under 15 years of age.

And today this third age has ceased to be merely the near future entry point to the other world, and we need to transform it into a new and fruitful stage of our lives, in which our older folks, who perhaps have stopped working but who certainly haven't stopped living, may reap with dignity the seeds that they planted during their earlier years: their children, grandchildren, family, friends, affections and loves.

We know that today's pensions are very low and insufficient to meet the expectations of our older adults. We currently have 2.8 million retirees, of whom 1.5 million have such low pensions that they need to rely on the Solidarity Pillar, through the Basic Solidarity Pension and the Solidarity Pension Allowance. Among those who depend on these bare subsistence-level programs, 62 percent are women.

WHY ARE PENSIONS SO LOW IN CHILE?

There are basically three reasons:

- *First, the mandatory level of retirement savings, at 10 percent of our salaries, is clearly insufficient.*
- *Second, due to unemployment and the lack of economic development, there exist too many and too extensive gaps in pension programs, and salaries are too low.*
- *And third, given the increase in life expectancies, the longer periods of retirement consistently outpace our ability to finance them through our current retirement savings program.*

This emphasizes the great importance of concentrating our efforts with greater energy, to create more and better jobs and to improve salaries and opportunities, and in so doing to improve future retirement pensions.

But also, the importance and urgency to provide a new and better deal for our elderly adults requires us to promote a new culture of respect, dignity, affection and inclusiveness of our elderly in our society. This requires closer relationships with their own families, better health care, better public transportation and better opportunities for work, sports, culture and recreation. Because our older citizens have much to teach us, and we have much to learn from them.

Our retirement system is based on two great Pillars: the Contributory Pillar, through which all workers make monthly contributions that finance their future pensions, and the Solidarity Pillar, to which the state contributes public resources to provide or top off pensions for the most needy and vulnerable groups.

The reform bill that we present today is designed to strengthen both pillars: contributory and solidarity. Its central objective is to improve current and future pensions, but with a special urgency and compassion for the most vulnerable groups, for the middle class, for women and for those who voluntarily extend their working lives. In so doing, it allows all of our elderly adults to overcome and leave behind situations of poverty and vulnerability and to live out their lives with better quality, better security and more dignity.

CHILEAN WOMEN AND MEN

Which are the fundamental pillars of this pension reform?

- **First:** *Raise the retirement savings of workers, through an additional monthly contribution of 4 percent of each worker's salary, which will be financed by their employers. This higher contribution will grow gradually so as not to affect our ability to create new and good jobs. It will over time mean a 40 percent increase in all workers' pensions.*

- ***Second:*** *Strengthen the Solidarity Pillar, which will grow gradually until reaching 40 percent, will evolve from today's 0.8 percent of GDP to 1.12 percent. This requires an increase in public spending to strengthen this Solidarity Pillar, eventually to close to U.S. $1 billion, financed through greater state funding. This strengthened Solidarity Pillar will allow us to immediately improve the Basic Solidarity Pension and the Solidarity Pension subsidy by 10 percent. These will continue growing relative to the retiree's age, up to 50 percent for the Basic Solidarity Pension and more than 70 percent for the Solidarity Pension subsidy.*

- ***Third:*** *In addition, the state will contribute additional resources to finance a new payment to middle-class retirees who contribute more than the minimum, which will increase along with the workers' contributory years.*

- ***Fourth:*** *This additional funding for middle-class retirees will be greater for women, to partially compensate for their lower participation in the workforce and their lower salaries, often due to child rearing or family care.*

- ***Fifth:*** *The state will also make additional payments to those who voluntarily extend their time of employment and defer their retirement age. In fact, an extension of five years in the workplace could increase their pension by more than 40 percent.*

Half of this additional savings from delaying retirement will go toward financing future pensions, and the other half may be freely drawn by such persons once they retire, in accordance with their individual preferences or necessities.

In summary, the strengthening of the Solidarity Pillar and the higher funding by the state will preferentially benefit those who are most vulnerable, the middle class, women, and those who voluntarily extend their working years past the statutory retirement age.

This retirement reform will also add to workers' options, so they may freely choose who will administer this 4 percent increase, through the creation of new institutions, whether for profit or not for profit, as well as affiliates of compensation funds, savings and loan cooperatives, pension savings administrators (AFPs), life insurance companies, etc., which will be permitted to manage these higher pension savings subject to the investment and operations rules that the Superintendent of Pensions will establish.

At the same time, this reform will promote competition in the pension fund administration industry, improving information to workers and quotes for new affiliates, leading to commission discounts based on the size of groups that join a given administrator and their commitment to staying with said administrator, with a single objective: reducing costs, minimizing commissions and improving their pensions.

As we see it, retirement savings belong to the workers, and therefore, they and only they have the right to choose who administers their retirement savings, and how. This right is not only recognized but also respected and strengthened by this pension reform.

This reform will improve pensions as soon as it becomes effective. But given its gradual application, this improvement will grow with time, always favoring, in terms of both priority and speed, retirees with lower pensions, those who are credited with more contributions, those who are older, women, the middle class and those who voluntarily extend their time in the active labor force.

In addition, this pension reform contemplates a Solidarity Insurance, which will be financed by an additional employer-paid payroll tax of 0.2 percent. The insurance will fund an additional pension, indexed to older ages, for elderly adults who are not ambulatory due to severe mental or physical dependency and may require support and special help.

Dear compatriots:

We are convinced that this retirement reform is just, is urgent and necessary, and requires a greater effort, gradual and incremental, from both the employer, who will need to finance an additional 4 percent of covered payroll, and the state, which will need to make a great effort to provide additional resources to the retirement world on the order of U.S. $3.5 billion.

This reform not only will increase pensions for a majority of retirees but also represents an important component of our commitment to a new and better deal for our older adults, which will materialize through policies and initiatives such as Positive Aging and Better Adult. Further, it will afford all of our older adults a silver age that is more integrated, fuller and happier, next to their loved ones.

In this way, in a responsible and sustainable manner vis-à-vis public finances, complementing the reform of the year 2008 and collecting many proposals from different sectors, we are meeting our commitment, our duty to help our older adults to fulfill their dreams, to mitigate their fears, to be able to develop their talents and achieve a third stage of life that is of better quality, with greater security and more dignity. It is fair and wise that we treat our older adults today as we want to be treated ourselves tomorrow.

I make a passionate call to all parliamentarians, both government and opposition, to add to the discussion in a constructive way, but also with a sense of urgency, to this noble and fine mission of improving the quality of life for all of our older adults.

Thank you very much. Have a good night, and may God bless Chile and all Chileans.

*****

Santiago, 28 October 2018
LFS
13:07

Josh Bank, ASA, is a retired international benefits actuary. He is an appointed member of the SOA Retirement Section Council and formerly served on the International Section Council.

Octavio Rojas is an accredited actuary in Caracas, Venezuela. He has a BSc in actuarial science from Universidad Central de Venezuela and studied stochastic methods in Edinburgh, Scotland.