Private firms to assume Chile's old-age pensions

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Santiago pensioner

SANTIAGO, Chile — In a daring experiment effective May 1, the military government of Chile will begin dismantling Latin America's oldest social security system and turning the pension business over to private enterprise.

The reform is controversial front-page news here — as it would be anywhere it were tried. In effect, President Augusto Pinochet has decreed the demise of a public pension system that is more than half a century old and covers nearly three-fourths of all Chilean workers.

The U.S. equivalent would be to phase out the federal Social Security Administration and let bankers, financiers and others compete for the management of billions of dollars in mandatory payroll deductions.

The Chilean goal is to transform a costly, red-tape-ridden government obligation into a competitive industry that will make profits by serving clients well.

As the May 1 startup date approaches, Chilean bankers and financiers are straining eagerly at the harness. New pension fund administration companies, called AFPs, are busily setting up shop and plotting a multimillion-dollar advertising "war" to win clients.

Most of the 10 AFPs forming so far are controlled by industrial and financial conglomerates that have grown rich and powerful under the free-market policies of Gen. Pinochet's regime.

The two biggest financial groups, known as the "Piranhas" and the "Crocodiles," are starting AFPs with initial capital in the range of $40 million each.

Union opposition

Chilean officials say that the profit motive will make the private companies administer the pensions more efficiently than the government ever could. They also predict that in private hands, the pension money will generate a surge of growth in the Chilean economy, bring more jobs, better pay and more profits.

To hear some union leaders tell it, however, the government is ripping up the collective security blanket of the workers and throwing it into the capitalist maw.

"We have noted a total consensus among workers to reject the new pension plan," said one Santiago labor leader. "The financial groups are going to enrich themselves with the money of the workers."

The Santiago newspaper La Segunda reported last week that some of the AFPs had tried to organize a cartel for fixing their commissions at a uniform level. Cartels are illegal in Chile.

La Segunda said the "dynamics of the marketplace" foiled the cartel scheme when three AFPs decided at the last minute to set competitive commission rates.

It was the government's hope that labor organizations, professional associations and other groups, and not just financial conglomerates, would form AFPs to give the new industry a broader and more competitive composition. So far, however, they have appeared reluctant to venture into unknown waters with the Piranhas and Crocodiles.

In a study published last year, before the new pension system was decreed, Chilean economist Jose Pablo Arellano said that putting the public funds in private hands "could produce a greater concentration of ownership, permitting the main economic groups to make important increases in their power and control."

No redistribution

The pension money, Arellano said, would give the conglomerates capital for purchasing stock control over increasing numbers of Chilean companies.

The main criticism of privately run pension funds is that they will eliminate the element of "social solidarity" in the social security system.

Like U.S. Social Security, the Chilean Seguridad Social has been a system of redistribution. Contributions from workers are distributed almost immediately to the retired, disabled and widowed. Only a small portion of the contributions are invested — in fact, the Chilean government subsidizes nearly one-third of the system's cost.

In Chile, as in the United States, some pensioners receive more for what they have put into the system than do others. Low-income pensioners get a break at the expense of high-income contributors and taxpayers at large.

Under the new system, each contributor will have an account with an AFP. On retirement, his pension will be based on what he alone has put in, plus interest, less the AFP's commission.

Law requires three-fourths of the Chilean labor force to make regular contributions to one of about three dozen government or semi-public social security funds called *cajas*. Only the self-employed are exempt.

Like the new plan, the old system is much criticized.

"Social security in Chile is shameful, because you put so much in and you get so little," said a withered septuagenarian after collecting his pension in cash at a pay station on Santiago's Santo Domingo Street.

The old man said he retired in 1969 after making social security contributions for more than 30 years. His pension is a modest $83 a month. "It doesn't buy anything."

Not enough money

The National Pensioners Union, a new organization, says studies show that the 1.1 million Chileans who receive social security checks do not get enough money collectively to cover even one-third of their total needs for food, shelter, clothes and health care. Despite cost-of-living adjustments, inflation shrank the dollar value of the average pension by one-third between 1970 and 1978, according to official statistics.

"A pension system of a clearly socialist cut has produced poverty and discrimination for millions of Chilean workers," said former Labor Minister Jose Pinera in announcing the pension reform last November.

Pinera, a Harvard-educated civilian who now is minister of mining, said the reform is a key part of the regime's larger design for reducing the role of government in the economy and letting free-market forces dominate.

Workers' contributions under the new system will be lower, Pinera said, "because, among other reasons, of the greater efficiency of private administration, less possibilities for fraud and less incentive for evasion" of payments. He said the new system "will undoubtedly produce an increase in demand for manpower, which will translate into higher pay as well as less unemployment."

Chile's most widely circulated newspaper, La Tercera, has been running a series of articles in which the new system is explained in popular language to a character named *Flaco Alegria* — Slim Happiness.

"Although deductions will be smaller, the pension reform guarantees minimum benefits at least equal to what you get in the current system," a knowledgeable friend tells Slim. "And the government guarantees that."

Slim: "That sounds like something from Mandrake the Magician, *compadre*."

Friend: "There's no magic. What happens is that the system is going to work more efficiently, without so much red tape and bureaucracy. The funds are going to be invested so that they don't lose value. They are going to grow."

Slim: "Then my decision is, 'I'm changing.'"

Time to decide

Workers already participating in the old social security system have five years to decide whether to

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etired Chileans line up in Santiago to collect their monthly pensions.

ransfer their accummulated contri-utions — in the form of govern-nent bonds — to a private fund. If hey do not, they may continue nder the old system until retire-nent at age 65 for men and 60 for vomen.

The government eliminated em-loyer contributions to social secu-ity in March. At the same time, sal-ry raises were decreed to cover a orresponding increase in employe contributions.

Workers who switch to the new ystem will get a sweetener — a re-duction in their payroll deductions equal to as much as 15 per cent of their pay.

The minimum payroll deduction for the new system is 17 per cent. Ten per cent goes into the privately run pension fund, and 7 per cent into disability and health insurance. The social security medical system will continue to be run by the government for the time being.

Workers joining the labor force after next year must go into the new pension system. Thus, the old system will wither away and eventually disappear.

Self-employed Chileans who have had no access to social security will be permitted to open pension fund accounts under the new system.

The only major groups that will be excluded are the armed forces and police. Their government-run pension plan, one of the most generous in the old system, will continue.

Servicemen and policemen retire after 30 years active duty, and their pensions are more than three times the national average.