An economic assessment model of pension reform transferability: The case of Venezuela

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Abstract Social pension and security systems worldwide are experiencing difficulties in maintaining the financing required to provide promised benefits. Despite their economic and political difficulties, many Latin American countries have arguably been more proactive and innovative with the implementation of social security reform than other regions of the world. Suggestions for reform of the social security system in Venezuela are provided by integrating many of the same concepts found in other restructurings in Latin America. It is the conclusion of this paper that, given the political and economic instability of the region, a major overhaul of the existing system is not politically feasible. An incremental approach with minimal disruption is more attainable given the current circumstances.

Keywords: *pensions, Latin America, social security, regulation, economic conditions and forecasts, international*

Introduction

Social security and pension systems worldwide are experiencing difficulties in maintaining the financing required to provide promised benefits. Reasons for the respective shortfalls vary by region, with some involving actuarial-related matters while others concern public policy issues and the attendant political implications.

Despite their economic and political

difficulties, many Latin American countries have arguably been more proactive and innovative with the implementation of social security reform than other regions of the world. Structural changes of social pension plans in countries such as Chile are providing a laboratory for major developed countries as they consider similar modifications.^{1,2}

By examining the characteristics of the

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public pension policy in an unstable yet asset-rich country, this paper is able to provide a forum for debating international reform in this state of affairs. Because of the unique point in Venezuela's history — the leadership of the government is precarious while the country's economy is heavily dependent on the export of crude oil — this analysis could provide an analogy for resolving similar hardships of pensions in developed countries.

The focus of this study is to examine the extent of social security reform efforts in various Latin American countries. From that foundation the paper extends its analysis to an in-depth description of the system in a specific country — Venezuela. This thorough analysis includes a review of the history of social security in Venezuela, its basic components and principal objectives, and current challenges experienced by the system. Suggestions for social security reform in Venezuela constitute the concluding contribution of the paper.

Pension reform in Latin America

Despite its economic difficulties, South America is considered one of the pioneering areas of the world with regard to a systemic overhaul of its pension collection and delivery systems. There are many different models of reforms utilised, with the most common ones being:

- Reformed public model — this is a public system, supervised by the state, which continues to work in its existing format but with selected modifications. The incremental change for this model is relatively small, which may make it the easiest to implement politically.
- Substitutive private model — under this model the former public

administration forbids new contributors into the old system, and a new mandatory system is created based on total capitalisation (private accounts). Chile was the first Latin American country to implement the substitutive reform in 1981.

- Parallel model — this model does not forbid the entry of new contributors. Instead, it keeps the existing public system and simultaneously introduces a parallel private system. Peru in 1992 and Colombia in 1993 are examples of this model.
- Mixed model — an intermediate reform that develops a system of saving and compulsory individual compounding that complements the public distribution system. Argentina has implemented this mixed model.

The social security systems of Latin America were widely influenced by international organisations at the beginning of the twentieth century. This influence resulted from a change within the structures of exporting societies which evolved from farming and mining activities to urban and industrial ones.

The reformation of the Latin American social security system is a response to a number of factors, which led to a financial imbalance of the systems already in existence. These factors include:

- Demographic changes associated with an aging population.
- Restrictions within a labour market reflected by high unemployment rates and low economical growth, and as the Venezuela case will illustrate, a decrease of real salaries.
- Problems in the reform's design and in the inefficient operation of liable institutions. Such reforms were intended to liberate the Treasury from the responsibility of its constant

disbursements to social security funds. They were also intended to increment the activity of the market and to stimulate the participation of private capital in the supply of collective assets through the privatisation of state companies.

Pension reforms have taken place in over one-third of Latin American countries. The following table summarises the characteristics of reforms in Chile, Peru, Argentina, Colombia, and Mexico.

Social security in Venezuela

Despite its abundance of natural resources, Venezuela has experienced its share of the political and economic turmoil that has troubled many Latin American countries over the past decade. In early 2002, President Hugo Chavez was briefly overthrown by opposition forces, only to return to power less than 48 hours later. The economy is dominated by the petroleum sector — accounting for roughly a third of GDP, around 80 per cent of export earnings, and more than half of government operating revenues.³ Volatility of employment levels and inflation continue due to a variety of factors, including periodic currency crises, the flight of foreign capital, a weak non-oil sector, and the nearly \$20bn cost of a flooding/mudslide catastrophe at the end of 1999.⁴ Even though about two-thirds of its 24 million people live below the poverty line, the literacy rate in Venezuela exceeds 91 per cent.

The national retirement system of Venezuela was implemented in 1967 with the creation of the Venezuelan Institute of Social Insurance (IVSS). This institution is in charge of social security in areas such as health, pensions, and unemployment. One product of market liberalisation in Venezuela was the

creation of the anti-monopoly agency called 'Procompetencia', which managed to survive a change of government and a move toward interventionist, anti-market mechanisms hostile to its survival.⁵

From its beginnings the IVSS has worked as a financial system in which each worker is assigned a fixed percentage of his monthly assessment. These assessments are deducted from the contributor's salary as social security and are distributed as follows: the worker contributes 4 per cent of his/her monthly salary, which covers 25 per cent of the expenses. The employer covers the other 75 per cent, and the percentage contributed varies, depending on the risk factor of each business:

- For a minimum risk of 13 per cent, a contribution of 9 per cent is required.
- For a medium risk of 14 per cent, a contribution of 10 per cent is required.
- For a maximum risk of 15 per cent, a contribution of 11 per cent is required.⁶

For the IVSS to guarantee its contributors a retirement pension to men and women beginning at an age of 55 to 60, the organisation relies on technical and mathematical allowances (reserves) that allow it to respond to people's needs in the expected manner. Addressing these needs is a fundamental element of the system.

In Venezuela, as in most other Latin American countries, the actuarial reserves are also used to finance other activities covered by social security — particularly health insurance, living units, etc. Ideally, technical reserves should represent the present value of future benefits (including accrued benefits).⁷ By the late 1980s, the reserves from this relatively new pension system were already insufficient to provide the mandatory pension payments.

Table 1: Summary of pension plan reforms in Latin America

Country Year of reform	Chile 1981	Peru 1993	Argentina 1994	Colombia 1994	Mexico 1997
Former system	Public system of defined benefits	Public system	Public system	Public system	Public system of defined benefits
Reformed system	Private system of defined contributions for all workers	Mixed system: — Some public support — Some support of defined contributions Continues with some changes Yes	Mixed system: — Some public support — Some support of defined contributions Continues with some changes Yes	Mixed system: — Some public support — Some support of defined contributions Continues with some changes Yes	Private system of defined contributions, only for workers in a formal field Completely eliminated ^a No
What happened to the former system?	Phased out gradually				
Are current workers required to remain in the former system?	Yes	No	No	No	Yes
Are new workers required to enroll in the new system?	Yes	No	No	Yes, every three years	No
Can workers return to the public system?	No	No (After June 1996)	No	Yes ^d	No ^e
Do they provide recognition bonuses (gift vouchers)?	Yes	Yes ^b	Yes ^c		
Profile of a new pension scheme with regard to the role of the state	Provides minimum guaranteed pension (PMG) and social assistance 10%	Provides minimum guaranteed pension (PMG) ^f and social assistance Private: 8% (10% since 1997) Public: 11% (13% maximum) 0.3%	Minimum pension 8%	Provides minimum guaranteed pension (PMG) and social assistance 10%	Provides minimum guaranteed pension (PMG), social fare and social assistance 6.5% = 5% + (1–5.5%) ^g
Contribution rate to the new system:					
— For the elderly					
— Disability, survivor	3%		3%	3.5%	4%
— Public assistance and support	Income in general	1%	16% paid to the employer 27% ^h	1%	Income in general
Total percentage of contributions:	19%	9%	27%	8% (private sector)	15.5%
— Before the reform	13%	13.3%	27%	13.5 – 14.5% ^h	6.5 – 21%
— After the reform					

Notes: ^aContributions to the former system stopped on 31st August, 1997. Workers close to retirement during the transitional period had access to the best benefits of either the former system or the new one; ^bonly workers that have contributed at least 48 months in the last ten years and have been working for at least six months before the new system started; ^cthe compensatory pension is included in the pension, not as a bond, and its value is determined by the years of contribution and the earnings in the last ten years; ^dworkers who have contributed to the system for less than 150 weeks are not eligible for these vouchers; ^eThe future fiscal costs will be calculated on an annual basis; ^fthe minimum pension was introduced to the system in 1995, but its regulation has not been implemented yet; ^gthe social rate is indexed to the IPC (Consumer Price Index) and is estimated using the 1 per cent and the 5.5 per cent, depending on the worker's income and the average rate of 2.2 per cent of the salaries; ^hthis percentage of contribution was for both public and private domains in 1996 and subsequent years. The contribution rate was gradually increased during the 1994–1996 period.

An IVSS audit performed in 1994 revealed that 'the technical reserves should be at a figure of 373 million Bolivars. However, by the end of 1993, the pension fund balance was only 351 million Bolivars, the equivalent of 42 per cent of the gross domestic product (GDP) of that same year'.⁴

Eligibility requirements for a person to claim his/her retirement pension are to be between 55 and 60, and to have made a contribution to the pension system for at least 750 weeks — approximately 15 years. The pension paid is equal to or higher than the urban minimum salary.⁸

Yet as with any sharing system, the IVSS is designed to redistribute its income among all its contributors. Those who worked and contributed for more than 15 years would compensate those that only worked the minimum period.

Ruling principles of the IVSS model

The doctrinal principles that have promoted the historical development of social security in Venezuela include the following:

Universality: This criterion is sustained by the premise that since all citizens of one country contribute directly or indirectly to national productivity, logic dictates that each of these citizens is protected by the system.

Integrity: The beneficiaries of the social security system are protected by the principle of integrity in order to attain improved welfare and to obtain a minimum amount providing a dignified quality of life.

Solidarity: Understanding that financing is the mechanism whereby the resources necessary for social security are

obtained is a consequence of the doctrinal principle of solidarity. This principle is sustained by the criterion that all members of society, despite their income, are obliged to progressively contribute to the system.

Efficiency: This refers to the optimal usage of the administrative, technical, and financial resources of the social security system, which is a way to guarantee the beneficiaries quality service.

Participation: 'Every (fe)male citizen has the right to freely participate in public affairs, directly or through his/her chosen representatives'.⁹ Since social security is a public policy, it is assumed that this principle [of participation] applies to it.

Coverage in Venezuela

This section discusses the distribution of benefits in the retirement or elderly pension, whether or not they have contributed to the system. Using this as the starting point for the distribution underpinnings, we identify two types of system: contribution and non-contribution.

The former refers to the financing system where one institution obtains the economical resources enabling it to make payments, via the state's disbursements to workers' and employers' contributions. The latter system refers to those mechanisms that attempt to protect everybody regardless of their former economic situation, by granting a minimum income or subsistence allowance.

Through the formulation of non-contribution protection, benefits are extended to all citizens. In other words, mechanisms of non-contribution seek to protect everybody, regardless of how long they have contributed to the system

and how much they have paid into it. This concept is supported by the Constitution of the Venezuelan Bolivarian Republic, which states 'The lack of contributory ability would not be a reason to exclude people from the protection [of the state]'.

Financing the Venezuelan social security system

Financing is defined as 'the group of measures adopted by a system with the purpose of gathering the allowance or resources that it needs to work'. It is the financial strategy adopted by a social security system that defines the financing of the system, the mechanisms of profitability, and the modes of distribution of the contributions collected. We can categorise the different financing sources into two main groups: direct and indirect contributions.

Direct contributions

Direct contributions refer to assessments made against affiliated workers and the employer's assessments.

Assessed contributions by affiliated workers

All workers who render their services in a private or public domain are under obligation to make a monthly contribution to the system. Such a contribution is a percentage deducted from their salary and collected by the IVSS, for the purpose of future distribution in the form of benefits.

Assessed contributions by employers

Every company with at least five workers is obligated to make corresponding assessments to social security. The employer's assessment is calculated based on a percentage of worker payroll, and is updated for changes, such as the hiring

of a new worker or an incremental change in basic salaries. In most cases, this occupational liability is transferred to the cost of production and usually ends up being incorporated into the price of goods and services.

Indirect contributions

These contributions include those resources obtained through a tax system, via direct or indirect taxation. Examples include: income taxes on bank debt, and taxes on liquor and cigarettes.

Another source of contributions for the social security system is through the GDP. Obviously, these contributions depend on the development of socio-economic structures of each country. A recent report published by the magazine '*Trabajo En El Mundo*' ('Work Around the World') examined the GDP transferred to the social security system in Latin America. They found that the average percentage transferred is around 4 per cent. Interestingly, neither Cuba nor Venezuela was included in the study as they were considered 'outliers'. Cuba transfers 20 per cent of its GDP to social security and Venezuela only transfers 0.4 per cent. In comparison, European countries typically make contributions of more than 20 per cent.

The choice of the financial system utilised is a critical one with regard to social security, since the method adopted secures the availability of the funds needed to meet its obligations. A financial balance between deposits and disbursements is required. The financial load of the system in Venezuela is distributed in two main ways:

— Distributing the secure financial load among different groups or generations of the contributors via:

Simple or annual distribution. This consists of an annual evaluation of the cost of payments so that the income necessary to grant the payments can be estimated.

General average premium. Also called collective funding, this method fixes from the beginning of the period a pegged-rate contribution that is intended to be sufficient to guarantee the indefinite financial viability of the system.

Stepped premium. This intermediary method consists of a fixed level of contribution adequate to secure equivalence between deposits and disbursements during a balancing period of ten or 15 years. Subsequently, if these resources are not proven to be enough at the end of a given year, the contribution rate is increased to assure the balance in a new period.

Sharing of coverage capital. This method consists of fixing an equivalent annual income to the present value of pensions — either the pensions that are to be granted in that year or the ones already granted. In other words, a technical reserve is accumulated equal to future assessments. To summarise, this method operates with the creation of contingency reserves able to cover eventual unforeseen variations of expenses so that the contribution rates are as stable as possible.

- Distributing the cost of benefits individually. With individual funding each person finances his own benefits through mandatory or voluntary contributions. The state delegates all duties of collection, investment, and granting of benefits for retirement, disablement, and survival to the Administration of Retirement Funds (ARF), an organisation created

exclusively to administer these funds. This system is characterised by the following features:

- The benefits granted by the system are directly proportional to the contributions that the insured individual has made into it.
- The insured person holds all rights to the individual account, which is part of his capital accumulated throughout his active work life.
- The deposited funds cannot be seised.
- The contributions to these funding accounts are deductible from annual income taxes.

Justification for pension system reform

There are a number of reasons necessitating a major restructuring of the social security system in Venezuela. In this section we identify and discuss these factors.

Earlier reference was made to the inadequacy of utilising the minimum average salary in the computation of benefits. Another consideration is the loss of the pension's real value, which was especially eroded during years of high inflation. For comparative purposes, a table matching the rate of inflation in Venezuela, the EU, and the USA during the past decade is shown below.¹⁰

During the mid-1990s, the reigning government recognised a need for reform of the social security system. The purpose of such a reform was to find financially feasible solutions for a system that was failing, as it was becoming increasingly dependent on injections of funding from the national treasury.

Demographic tendencies

Even though the 'population pyramid' shows a considerable portion of younger

Table 2: Rates of inflation

Year	EU %	USA %	Venezuela %
1994	3.0	2.6	60.8
1995	2.9	2.8	59.9
1996	2.5	2.9	99.9
1997	1.8	2.3	50.0
1998	1.5	1.5	35.8
1999	1.4	2.2	23.6
2000	2.3	3.4	16.2
2001	2.6	2.8	12.5

Source: CIA World Factbook

people, the net effect of the birth and death rates in Venezuela is an increase in the age of IVSS contributors.¹¹ This dynamic leads to an incremental increase of the dependence rate (the financial relationship between active workers and retirees). Since the method of distribution is based on the intergenerational system, every time this dependence rate increases, the financial strain on the social security system increases.

IVSS financial imbalance

The technical reserves of the Venezuelan system have been earmarked to finance both the IVSS infrastructure and a health subsystem. Unfortunately, the health subsystem has traditionally operated with a deficit. The actuarial reserves were insufficient to finance the present value of pensions,¹² which was damaged by an aging population and by an increase in the flight of capital.

Problems with the flight of capital

In a sharing system, the loss of capital is normally associated with three factors: the weak relationship between contributions and their benefits; high rates of inflation; and the lack of trust by contributors toward the social security system. In the present system, if the contributor resigns or is fired from one

job and takes up a new one in the formal system, he could lose all his years of quotation.

As referred to previously, the high inflation rate of the 1990s produced a decrease of the real value of salaries, which caused the economical decrease of contributions to the IVSS and an erosion of the real value of pensions. As a result, workers do not attain real benefits corresponding to the value that they have been charged during their working years.

Due to this perceived lack of guarantees relating to their income at retirement, workers become understandably discouraged and sceptical of the system. As a result, the system is perceived as a tax deduction from their salary. 'The percentage of contributors from the active economic population who abandon the system is more than 25 per cent.'

Co-existence of a multiplicity of special interests

Adding to the complexity of the Venezuelan social security system are the different models of retirement and pension plans in both the public and private sectors. The result is that some governments, councils, and other institutions work with similar criteria yet offer different benefits. Examples of these regimes are: retirement funds for

professors serving in the military, banking institutions, and organisations associated with the petroleum industry.

Financial cost

Disbursements from the State Treasury to fund the system are now a regular occurrence, and payments related to pension shortfalls are becoming increasingly substantial. As long as employee and employer contributions are insufficient to cover pension obligations, this situation will continue.

The weak relationship between salary deductions and the future benefits expected, combined with serious uncertainty about the distribution of those benefits, has resulted in a shift of employment and production to the informal or 'underground' economy. The consequences are an increase in tax evasion and muted economical growth.

Because of this financial quagmire and dismal estimations of long-range forecasts, interest is building for the creation of a social security model based on an individual capitalist regime (or private retirement accounts), whereby each worker saves a fraction of his/her salary in an individual savings account, guaranteeing him/her a pension upon retirement.

Suggestion solutions for pension system reform

A number of public policymakers and think tanks have drafted proposals for restructuring the social security system in Venezuela. Among these is the Economic Commission for Latin America (CEPAL), which has extensively examined the most common problems of any given distribution system. Some suggested proposals and tools for implementing reform by CEPAL are mapped out in Table 3.

Fiscal cost of reforming pensions

The fiscal inadequacies of the current system in Venezuela are a primary reason why there is more pressure today to reform this system of pensions. Due diligence mandates examination of the consequences this reform has on the financial status of public social security institutions. The financial status is affected by transferring one contribution system to another, since in the latter, the inability of one individual to contribute to the system does not exclude him from it. This fact will provoke changes in the conventional indicators of public finances of any given country, which will vary, depending on how the financing of the reform is assumed. In the case of Venezuela, either through income attained from petroleum exports or from general taxes.

There are three main kinds of fiscal costs:

- Transitional costs — These originate from the state's assumption that there is an implicit deficit in the pension funding. Since active workers would contribute to the new system and not to the old one, the tax authority would have to increase tax rates in order to finance the added expense of that deficit.
- System supportability — The fiscal costs associated with the supportability of the system are related as much to demographic factors (such as age, life-expectancy, attainment of retirement age) as to macroeconomic variables (such as increment of the GDP, participation of salaries in the national fund, level of unemployment, underground economy robustness, and the increment rate of salaries and interest).
- Long-term viability of the system — Viability is determined by institutional, demographic and

Table 3: Suggested proposals and tools for implementing reform

Problem	Objective	Proposal	Tools
<ul style="list-style-type: none"> System composed of different regimes that exclude one another and affect the mobility of the working force. 	Homogeneity.	Equalise the differences between regimes so that their benefits are the same for workers with similar characteristics.	Equalisation of contributions and eligibility conditions (retirement age) to obtain pensions in a single homogenised system.
<ul style="list-style-type: none"> Few productive jobs with little relation between contributors and beneficiaries. 	Work productivity.	Guide economic policies toward the generation of productive employment.	Investment in human resources, savings, productivity of economical factors, expansion of markets and increase in technical development.
<ul style="list-style-type: none"> Evasion and delays in employer's payments to the retirement system; State's debt. Independent employer's contributions. 	Improve the collection system.	Develop incentives to motivate people to fulfill their obligations to the system. Create sanctions for those not in compliance. Create mechanisms to negotiate the debt of the system.	Computerisation, creation of individual accounts, identification of contributors and beneficiaries, adjustment of fines and real interests, bonds adjusted to the state debt. Simplification of bureaucratic procedures.
<ul style="list-style-type: none"> Low profit of the reserve funds deviated to other governmental programmes. Lack of indexation mechanisms. 	To invest these funds.	Supervise and regulate the investment portfolios. Develop the capital markets.	Create a regulatory organisation; a risk-evaluating commission; forms of financial mediation; periodic publication of balances; preparation of financial reports according to each programme.
<ul style="list-style-type: none"> Systems do not provide complete coverage of the work force; segments of the population fall through cracks in the system. 	Solidarity. Expand public coverage to reach more sectors of the population.	Develop mixed systems of basic and complementary pensions on the basis of personal accounts. Create incentives to appeal to and motivate independent workers to join.	Usage of funds for collateral credit for the participants. Homogeneity of minimum pensions and self-financing of additional pensions. Separation of the pension programme from the fiscal budget.
<ul style="list-style-type: none"> Benefits have no correlation with contributions; indexation of benefits with different criteria of collection and with other sources of income. 	Adequate the benefits to individual efforts and to the capacity of the system.	Guarantee the minimum and complementary pensions, which need to be adequate to cover the contributions of each member during his/her work life.	Fixation of retirement age with regard to life-expectancy and years of contribution to the system. Flexibility of retirement age. Granting minimum and complementary pensions. Development of life insurance companies. Development of mechanisms of indexation adequate to the system. Regulation and supervision of eligible dependants. Elimination of privileges.
<ul style="list-style-type: none"> Excessive administrative spending. Inefficiency of the system. 	Improve administration.	Conduct an administrative reformation of the system.	Rationalisation of major expenses; divide the programmes; legislative reform; computerisation of procedures; improvement of personnel qualifications. Clearly defining: each programme's budget, personnel policies, normalisation, and privatisation.

Source: CEPAL, 'Reformas de los sistemas de pensiones con componentes de capitalización,' Vol. 56, August 1995.

Table 4: Budget impact of coverage at basic levels for a non-contributive regime

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
35% GDP	0.4%	0.5%	0.6%	0.6%	0.7%	0.9%	1%	1.1%	1.3%	1.5%
50% GDP	0.6%	0.7%	0.8%	0.9%	1.1%	1.2%	1.4%	1.6%	1.9%	2.2%
75% GDP	0.9%	1%	1.2%	1.4%	1.6%	1.8%	2.1%	2.4%	2.8%	3.2%
100% GDP	1%	1%	2%	2%	2%	2%	3%	3%	4%	4%

Source: National Institute of Statistics (INE)

economic considerations. Since the institutions are the ones that must be designed in a way that can resolve the demographic and economic factors, new generations will have to absorb the financing charges of the system.

The National Assembly Office for Economic and Financial Consultancy has estimated that using shared funds, and given preliminary projections for social security contribution rates of 9–10 per cent, a deficit will appear in the Venezuelan system around 2030, and the system will be bankrupt around 2050. Furthermore, this office points out that the current cost of this system is estimated to be 3.3 per cent of GDP in decentralised systems, more than the current 0.4 per cent of GDP in university regimes, 0.4 per cent in military regimes, and 0.1 per cent in other special regimes.

In 2001 there were 520,000 people with pensions within the Venezuelan Institute of Social Services, and the charge for each of them was \$4,630 per year. Using these figures and factoring in forecasted demographic growth, the current system would increase its number of beneficiaries to \$1.47m in the year 2025, and to \$2.84m in 2050. Thus, to cover the cost in 2050, the system would need a budget exceeding \$7.456bn per year just to pay pension obligations, not including other administrative expenses.

To calculate the budget impact of this

coverage at a basic level for a non-contributive regime, the National Institute of Statistics (INE) looked at the number of citizens who would reach 65. Participants who would retire and get their pensions from the IVSS and from the projections of special regimes were subtracted from those requiring the minimum pension.

Four different scenarios were considered: 35 per cent of the population with coverage at the basic level, followed by estimations at 50 per cent, 75 per cent, and 100 per cent. The results of the study are shown in Table 4.

The results suggest that if the Venezuela government tries to fulfil Art. 80 of the Venezuelan Constitution, the cost to guarantee the coverage of minimum pensions could climb tenfold to 4 per cent of GDP. The study concludes that 'the reform of the social security system cannot take place without serious fiscal reform, including one that improves revenue collection services by adding new resources and reducing incentives to illegally dodge taxes. These measures are needed to improve the efficiency of public expenditures and guarantee the budgetary allowances for public welfare without neglecting contributor's preferences'.

Finally, the Association of Promoters for the Administration of Pension Funds, referencing the February 2001 preliminary project for the Law on Pensions, has calculated estimations of fiscal expenses from 2001 to 2043 under

Figure 1: Estimates of fiscal expenses 2001–2043

Source: Association of Promoters for the Administration of Pension Funds.

four scenarios, as graphically illustrated in Figure 1.

Conclusion

This paper examined the characteristics of the Venezuelan social security system. As with many other countries, Venezuela is expected to experience a financial shortfall in its projected retirement and social health-care future liabilities. This paper also presented an in-depth discussion of the various reforms implemented in other Latin American countries. Finally, suggestions for reform of the social security system in Venezuela were provided by integrating many of the same concepts found in other restructurings. It is the conclusion of this analysis that, given the political and economic instability of the region, a major overhaul of the existing system is not politically feasible. An incremental approach with minimal disruption is more attainable given the current circumstances.

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- 2 Mesa-Largo, C (2001) 'Structural Reform of Social Security Pensions in Latin America: Models, Characteristics, Results, and Conclusions', *International Social Security Review*, Vol 54, pp 67–92
- 3 CIA World Factbook.
- 4 The Venezuelan Bolivar has an exchange rate of 700 bolvares per US dollar. The exchange rate has deteriorated steadily during the past six years, from 680 in the year 2000, 548 in 1998, and 417 in 1996. Some analysts contend that the Bolivar is still overvalued by as much as 50 per cent
- 5 Kelly, J. and Perera, A (2000) 'Antitrust policy in a hostile environment: Institution building in Venezuela's procompetencia', *International Journal of Public Administration*, No 5–8, pp 1125–1156
- 6 The risk factor is classified by the IVSS, using factors associated with various business operations and activities. For example, companies in the oil industry are rated with maximum risk primarily due to the physical operations involved in that business.
- 7 Gaitan, W J. and Fernandez, A (1998) 'The new Venezuelan social security system', *Benefits and Compensation International*, Vol 27, No 9, May, pp. 7–13.

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- 8 The minimum salary is established by the government partially as a function of a basket of consumer prices known as the Alimentary Basic Basket. Historically, the minimum salary has not been directly linked to inflation. Consequently, the minimum salary is artificially low
- 9 Constitution of the Venezuelan Bolivarian Republic, 1999
- 10 The ten-year average rate of inflation from 1984-93 in the European Union, United States, and Venezuela were 4.4 per cent, 3.8 per cent and 30.8 per cent, respectively.
- 11 As a comparison, the death rate in Venezuela is 4.92 per 1,000; in the United States the death rate is 8.7 per 1,000.
- 12 Present value of pensions is defined as the amount of money needed today to pay pension obligations upon retirement