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Reform of the Pension System Within the Instituto Mexicano del Seguro Social (Mexican Social Security Institute)

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- Four Fundamental Stages in the Development of the Instituto Mexicano del Seguro Social
- Some of its Main Indicators
- Problems that Gave Rise to the Pension System Reform
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- Main Benefits and Costs of the Pension System Reform
- Estimate of the Transition Fiscal Cost
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Four Fundamental Stages in the Development of the Instituto Mexicano del Seguro Social

- 1943, Instituto Mexicano del Seguro Social—IMSS—(Mexican Social Security Institute) is founded.
- 1973, important reforms are made in the Act, to improve the existing benefits, and to incorporate new groups and insurance schemes.
- 1995, the 1973 Act is repealed.

The outstanding feature of the new Act is the setting up of a defined contribution pension system based on individual accounts.
- In 2001, the 1995 Act is reformed. The reforms are focused, basically, on IMSS internal organization.

Some of the Main Indicators

- About 14 million workers are affiliated.
- It provides protection to more than 46 million beneficiaries.
- Pensioned people are about 1.9 million.
- Second fiscal authority of the country, on collecting more than 9 billion USD of worker-employer contributions.

Some of the Main Indicators

- It gives attention to more than 115 thousand children in its child care centers throughout the country.
- One of every three Mexicans is born in IMSS facilities.
- 25% of the nation's medical research is under its responsibility.

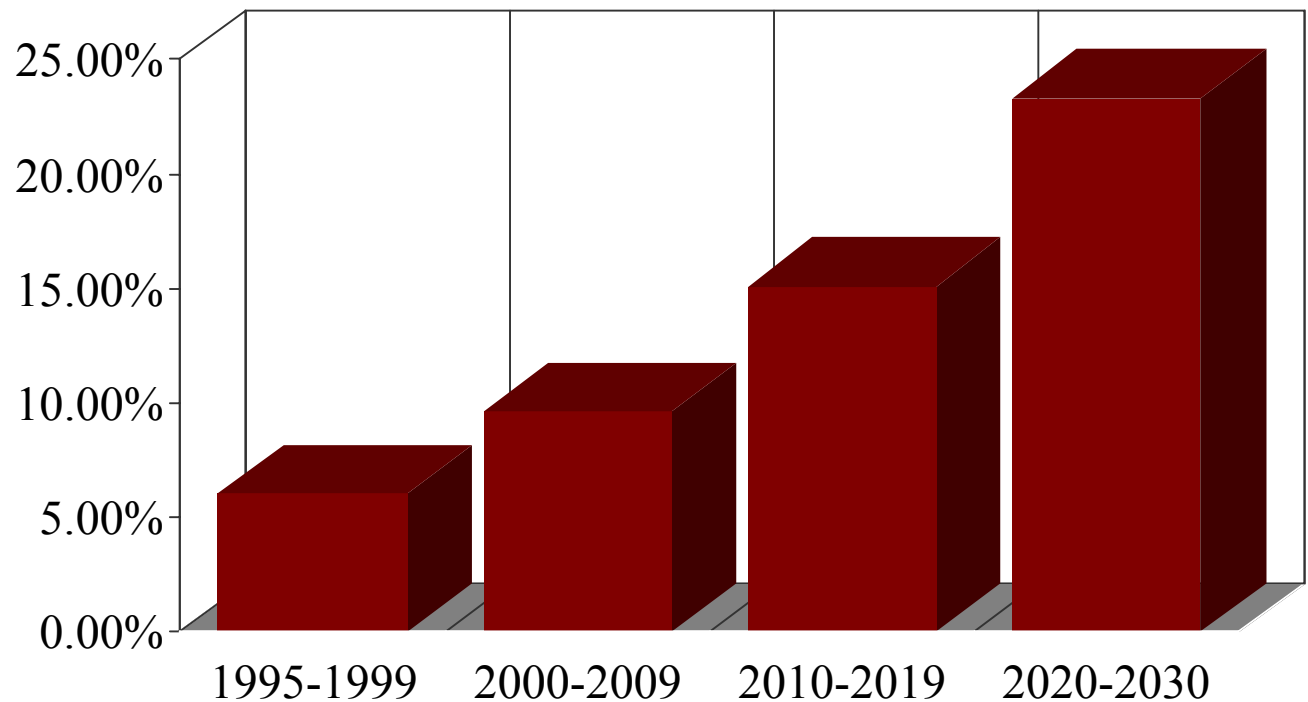
The Problem that Gave Rise to the Pension System Reform

The former pension system included:

- Pension system for Disability, Old Age, Unemployment at Old Age and Death Insurance
- Pension system for Worker's Compensation Insurance
- The Disability, Old Age, Unemployment at Old Age and Death Insurance system used up more than 80% of the pension's total payment. From year 2000, it would have been necessary to increase considerably the level of contributions assigned to cover the pension's expenditure (6.00% of the quotation salaries).

The Problem that Gave Rise to the Pension System Reform

The following chart shows the required increases.



■ Level of contributions as a percentage of the quotation salaries

Main Objectives and Characteristics of the Pension System Reform

Objectives

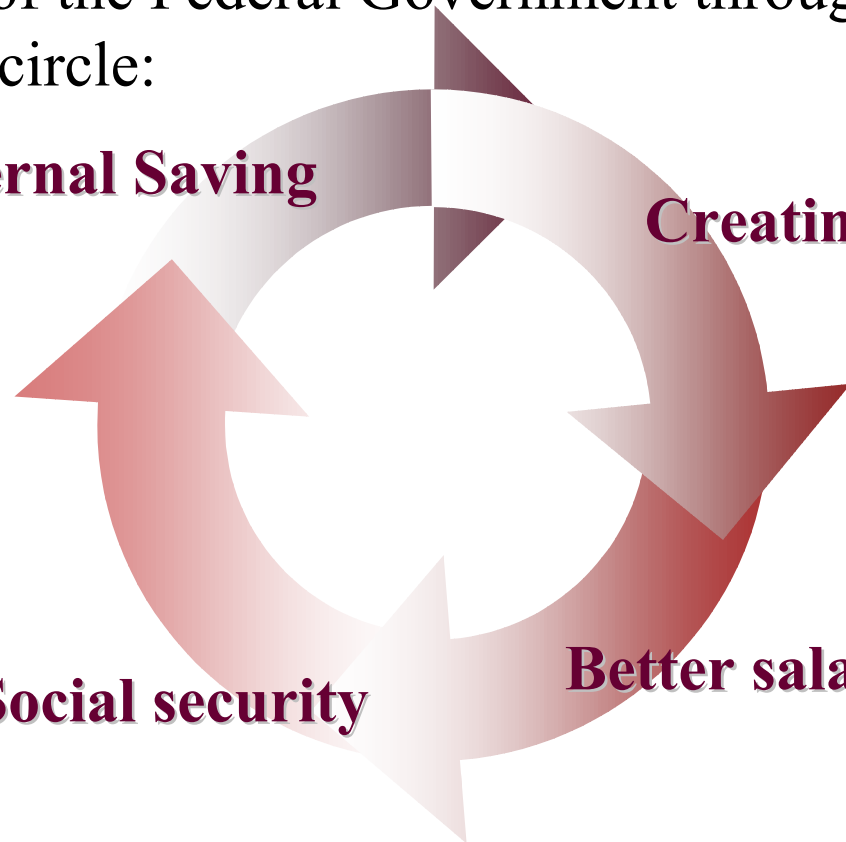
- To help in reaching the social and economic policies of the Federal Government through a virtuous circle:

Internal Saving

Creating of jobs

Better salaries

Social security



Main Objectives and Characteristics of the Pension System Reform

Characteristics of the Pension System in Force

Repealed Act			New Act		
Type of Insurance	Type of Pensions' Scheme	Financial Instrument	Type of Insurance	Type of Pensions' Scheme	Financial Management
Disability, Old Age, Unemployment at Old Age and Death	Defined Benefit	Collective funds	Retirement, Unemployment at Old Age, and Old Age Disability and Life	Defined Contribution Defined Benefit	Individual Accounts Individual accounts complemented with resources administered by the IMSS, when the accounts turn out to be insufficient to finance the benefits.

Main Objectives and Characteristics of the Pension System Reform

Characteristics of the Pension System in Force

Repealed Act			New Act		
Type of Insurance	Type of Pensions' Scheme	Financial Instrument	Type of Insurance	Type of Pensions' Scheme	Financial Management
Worker's Compensations	Defined Benefit	Collective funds	Worker's Compensations	Defined Benefit	Individual accounts complemented with resources administered by the IMSS, when the accounts turn out to be insufficient to finance the benefits.
Retirement (SAR, or Retirement Saving System)	Defined Contribution	Individual Accounts	It is incorporated to the Retirement, Unemployment at Old Age, and Old Age	-	-

Main Objectives and Characteristics of the Pension System Reform

Other features of the new pension scheme:

- Expenditure for pensions in payment in force until June 30, 1997 in Federal Government's charge.

Main Objectives and Characteristics of the Pension System Reform

Other features of the new pension scheme:

- Transition model: The workers affiliated to IMSS until June 30th 1997 (generation in transition) were incorporated immediately to the new pension system; however, at the moment of getting an Old Age or Unemployed at Old Age pension, they are able to choose at their convenience, between the pension derived from the Act repealed and the one derived from the 1995 Act. If they take the first option, the accrued fund in the individual account is transferred to the Federal Government; the missing portion needed to cover the pension is in Federal Government's charge.

Main Objectives and Characteristics of the Pension System Reform

Other features of the new pension scheme:

- Individual accounts administered by the Administradoras de Fondos para el Retiro –AFORES- (Retirement Funds Administrators) and assets invested by the Sociedades de Inversión Especializadas en Fondos para el Retiro -SIEFORES- (Specialized Investment Societies of Retirement Funds) and INFONAVIT (National Institute of the Workers Housing Fund).

Main Objectives and Characteristics of the Pension System Reform

Other features of the new pension scheme:

- Currently, there are 13 AFORES in the market, managing assets on the whole 27.3 billion USD that are equivalent to the 4% of the 2001 GDP and approximately 60% of the international reserves of the Banco de México (central bank).
- Pensions derived from the Disability and Life Insurance and Worker's Compensation Insurance, covered by insurance companies dedicated to the selling of life annuities.
Currently, these kind of institutions manage assets equivalent to 5.9 billion USD.

Main Objectives and Characteristics of the Pension System Reform

Other features of the new pension scheme:

- The guaranteed pension granted cannot be lower than one minimum wage as of July 1st 1997, indexed for inflation. Currently, it is equivalent to 154 USD.

Main Benefits and Costs of the Pension System Reform

To the workers:

Benefits	Costs
Transparency when administering resources assigned to the retirement benefits.	Increase to the maximum quotation salary.
The contributions placed in the individual accounts are never lost.	Uncertainty about the benefit amount that they will receive at old age.
The saving culture is promoted.	High commission rates by the AFORES.
The low-income workers have the opportunity of getting access to the financial system.	Complexity in the system's operation and, therefore, possibility of mistaken decision making.
Guarantee of benefits payment by the Federal Government, in case of payment of benefits derived from the 1973 Act.	Low interests rates gained through the INFONAVIT sub-account in comparison with those gained through SIEFORES sub-account, what causes impact on the benefit amount to be earned.

Main Benefits and Costs of the Pension System Reform

To the employers:

Benefits	Costs
Contributions to the Worker's Compensation Insurance according to the claims ratio.	Increase to the maximum quotation salary.

Main Benefits and Costs of the Pension System Reform

To the IMSS:

Benefits	Costs
A financially viable pension system.	Increase in the amount of resources advocated to pay the complement of Disability and Life Insurance, as well as Worker's Compensation Insurance pensions, whether the expected claims ratio increases and the interest rates gained by the individual accounts decreases dramatically.

Main Benefits and Costs of the Pension System Reform

To the financial system:

Benefits	Costs
Foundation of new institutions (AFORES and Pension Insurers)	Promotion of new services and investments recouping.
Significant increase in the administered financial resources.	

Main Benefits and Costs of the Pension System Reform

To the Federal Government:

Benefits	Costs
Tacit recognition of a problem that would have affected the public finances anyway.	Payment of the fiscal cost of the reform.

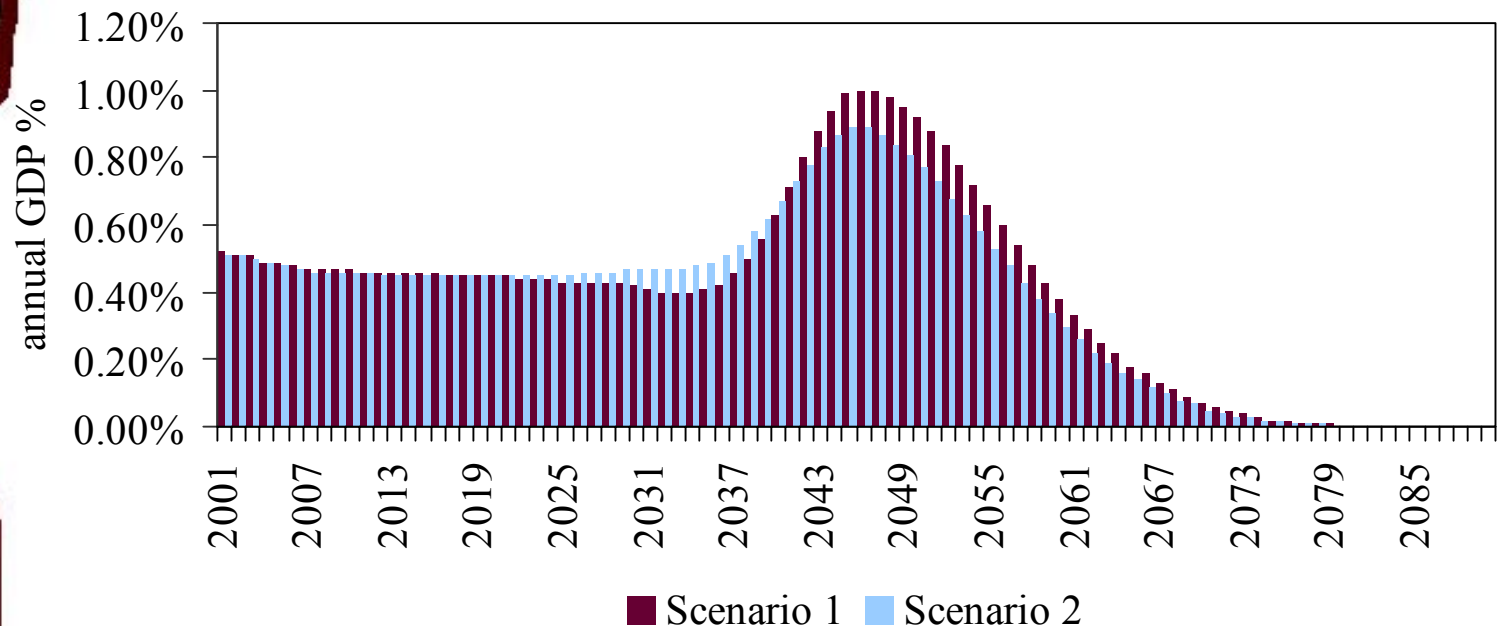
Estimate of the Transition Fiscal Cost

We the exponents want to thank the authorities of the Instituto Mexicano del Seguro Social the for allowing us to use the information required to elaborate this estimate, and our gratitude to the actuaries Mario Arriaga and José Landaverde for their collaboration to make the corresponding actuarial calculations.

Estimate of the Transition Fiscal Cost

- Results

The following chart shows the behavior we estimate the transition fiscal cost will have as a percentage of the GDP



Estimate of the Transition Fiscal Cost

- Present Value of the Transition Cost

Present Value of the Transition Cost	Scenario 1	Scenario 2
% of the GDP for year 2000	22.31%	33.78%

Final Thoughts

- The IMSS and other social security institutions cover around 17 million workers and represent around the 40% of the Labor Force.
- After more than four and a half years of having in force the 1995 Act, we consider as necessary in the pension system:
 - The revision of the INFONAVIT function.
 - The decrease of the commissions collected by the AFORES.

Final Thoughts

- The revision of the high investment percentage of the SIEFORES portfolio in government bonds and the implications on the national economy and public finances.
- The revision of the contributions level to the individual account, if the INFONAVIT stays without modifications in its operation.
- To encourage the private sector to issue long-term debt instruments.

- If we consider the fiscal cost of the IMSS pension reform and the problems of other systems not yet solved, Mexico will need to get additional financial resources in significant amounts. Otherwise, our country could face, once again, recurrent economical crisis during the 21st Century.
- Where are the actuaries?
 - ✓ Social Security \Leftrightarrow Actuary
 - ✓ Evolution: Technician \Rightarrow Participant decision process.