CHILE

Chile: pension system in 2008

The pension system has three components: a redistributive first tier, a second tier of mandatory individual accounts and a voluntary third tier. The individual accounts, introduced in 1981, are of the defined-contribution type. The redistributive first tier was substantially extended in a pension reform in 2008.

Key indicators

		Chile	OECD
Average earnings	CLP (million)	5.83	21.21
	USD	11 200	40 600
Public pension spending	% of GDP	5.2	7.0
Life expectancy	at birth	78.6	78.9
	at age 65	83.7	83.1
Population over age 65	% of working-age population	14.8	23.6

Qualifying conditions

Defined-contribution

Normal retirement age is 65 for men and 60 for women. Pension benefits can be drawn at any point from that age. Individuals are not required to stop working to claim pension.

Basic and supplementary schemes

The basic solidarity pension (PBS) is payable from age 65 on condition that people have lived in the country for at least 20 years and at least four of the five years prior to the claim. The qualifying conditions for the supplementary welfare pension are the same.

Benefit calculation

Defined-contribution

The contribution rate for individual accounts is 10% of earnings. Administrative charges are levied on top of this contribution (not out of the mandatory contribution).

There is a ceiling on contributions, which in 2008 was set at 60 "unidad de fomento" (real, that is inflation adjusted, units), which was CLP 1 287 283 per month, equal to 8 times the minimum wage in December 2008 and 291% of average earnings. From 2009 onwards, the ceiling will be indexed to average earnings.

At retirement, the accumulated capital can be used to buy an immediate life annuity, to get a temporary income with a deferred life annuity, to take programmed withdrawals, or to buy an immediate life annuity with programmed withdrawals. A withdrawal of 15 UFs is made from the individual account to cover for funeral expenses. For comparison with other countries, replacement rates have been calculated assuming an actuarially fair annuity, using sex-specific annuity rates.

Basic

The basic pension (PBS) was CLP 60 000 in 2008-09. This was increased to CLP 75 000 from 1 July 2008 as a result of the 2008 reform. The modelling uses this higher value for the basic pension and assumes it is indexed to wages.

Supplementary

The 2008 reform also introduced a pension-income-tested supplement as a replacement for the previous minimum pension. This is payable to all individuals whose defined-contribution pension is less than a specified amount: the maximum welfare pension threshold (PMaS). This threshold will increase over time as the new system is phased in:

	Maximum welfare pension (PMaS, CLP)	Target coverage of older people (%)
July 2008-June 2009	70 000	40
July-August 2009	120 000	45
September 2009-June 2010	150 000	50
July 2010-June 2001	200 000	55
July 2011 onwards	255 000	60

The supplementary benefit increases, at first, with individual income from the defined-contribution scheme. The increment is 1 – the value of the basic pension (PBS) divided by the maximum welfare pension (PMaS): i.e., 14.3% for the period July 2008-June 2009, when the PBS is CLP 60 000 and the PMaS is CLP 70 000. From 2011, the PBS will be CLP 75 000 and the PMaS CLP 255 000. Thus, the increment in benefits will rise to 70.6% of individual entitlements under the defined-contribution plan. For people with defined-contribution pensions above the value of the basic pension, the value of the supplement is reduced. The benefit is defined as the value of the basic pension (PBS) – the ratio of PBS to the value of the maximum welfare pension (PMaS) multiplied by the value of the defined-contribution pension. The key ratio of PBS to PMaS is 85.7% in 2008-09, falling to just 29.4% from mid-2011 onwards.

The objective of this new supplementary pension is to improve the living standards of low-income workers when they move into retirement. The table above shows that the government expects 40% of the poorest pensioners to benefit from the new programme in 2008-09, increasing to 60% from mid-2011 onwards. The modelling of pension entitlements uses the parameters that will be in place from 2011 (and so will be those applicable to a new labour-market entrant in 2008). The modelling assumes the value of the supplementary pension will be indexed in line with wages from 2011 onwards.

Variant careers

Early retirement

Early retirement is allowed at any age in the defined-contribution scheme as long as the capital accumulated in the account is sufficient to finance a pension above particular thresholds. The first condition is that the benefit must be worth 150% of the minimum pension under the old system. From July 2012 onwards, this will change to 80% of the maximum welfare pension, PMaS. The second condition is that a certain replacement rate is reached, relative to earnings in the 10 years prior to drawing the pension. This replacement-rate threshold is increasing: from 64% in 2008-09 to 67% in 2009-10 and 70% from August 2010 onwards.

The normal retirement age is reduced by 1 or 2 years for each 5 years of work under arduous conditions in specified occupations. The maximum reduction of the normal retirement age is 10 years.

Late retirement

It is possible to defer pension claiming after normal retirement age.

Childcare

A pension voucher is given to women for each child that they have had when they reach 65 years of age. The voucher is equivalent to 10% of 18 months' minimum wages at the time of birth plus the average net rate of return on defined-contribution pension plans from the birth until the pension claim. The average interest rate is calculated for "fund C" of the private pensions: the middle one in terms of the risk-return trade-off. This is transformed into a pension flow when the woman claims her pension.

Unemployment

No credits are given. A separate unemployment insurance system has existed since 2002.

Personal income tax and social security contributions

Taxation of pensioners

When claiming a pension individuals are allowed to obtain the "Free Purpose Surplus" if the remaining balance is enough to finance a pension that is at least 150% of the minimum pension and yields a replacement rate of at least 70%. The surplus can be obtained in tax-free annual installments up to a maximum of 200 UTM per year and a total tax-free amount of 1200 UTM. If obtained as a lump-sum, the maximum exempt amount is 800 UTM[1].

Taxation of pension income

Same rates as general income tax rates apply. Structure of Income tax is progressive:

Income bracket (UTM)		Marginal tax rate
From	To (inclusive)	
-.-	13.5	0%
13.5	30	5%
30	50	10%
50	70	15%
70	90	25%
90	120	32%
120	150	37%
150+		40%

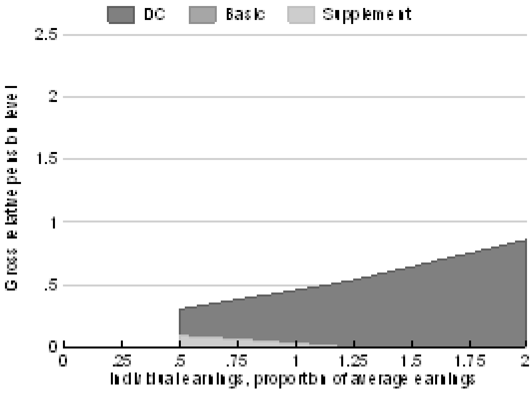
Social security contributions paid by pensioners

Pensioners pay 7% of pension income for health coverage.

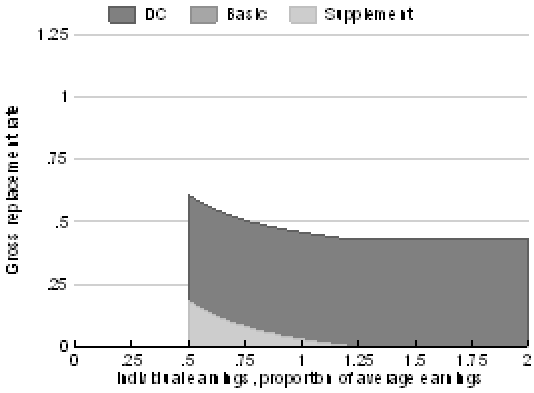
[1] UTM is the Monthly Taxing Monetary Unit. It is adjusted each month according to inflation. In December 2008 its value was cl$37,652.68 or us$58 (using the exchange rate for the same period: us$1= cl$649.32).

Pension modelling results: Chile

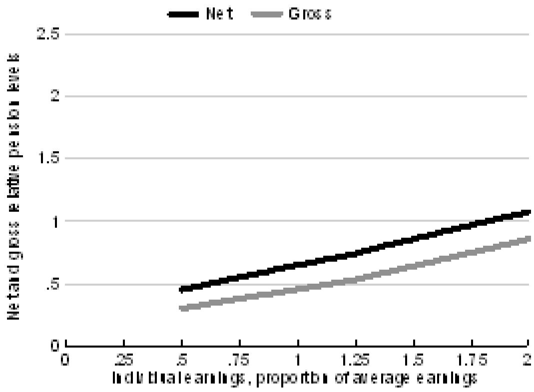
Gross relative pension level



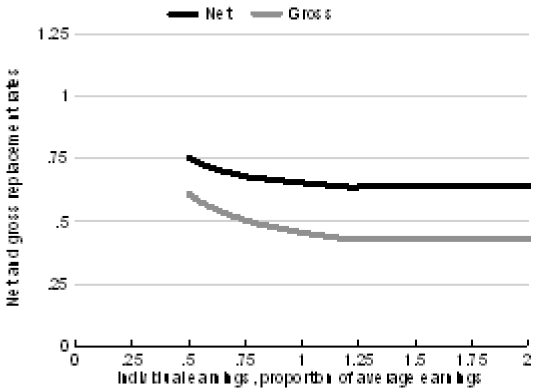
Gross replacement rate



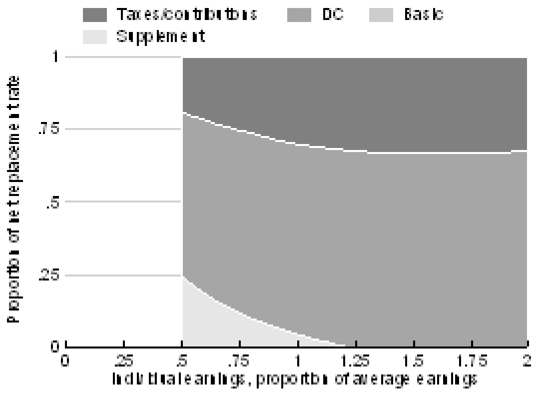
Net and gross relative pension levels



Net and gross replacement rates



Sources of net replacement rate



Taxes paid by pensioners and workers

Men *Women (where different)*	*Median earner*	*Individual earnings, multiple of average*				
		0.5	*0.75*	*1*	*1.5*	*2*
Gross relative pension level	39.2	30.0	37.4	44.9	62.7	83.7
(% average gross earnings)	30.4	24.6	29.3	34.0	43.3	52.7
Net relative pension level	56.9	44.5	54.5	64.3	84.3	105.5
(% net average earnings)	45.1	36.9	43.5	49.9	62.3	73.4
Gross replacement rate	48.4	60.0	49.9	44.9	41.8	41.8
(% individual gross earnings)	37.5	49.2	39.1	34.0	28.9	26.4
Net replacement rate	66.0	74.4	66.9	64.3	62.7	62.5
(% individual net earnings)	52.4	61.7	53.4	49.9	46.3	43.5
Gross pension wealth	7.4	9.2	7.6	6.9	6.4	6.4
(multiple of average gross earnings)	7.8	10.2	8.1	7.0	6.0	5.5
Net pension wealth	6.3	8.1	6.6	5.8	5.1	4.8
(multiple of average net earnings)	6.8	9.0	7.1	6.1	5.1	4.5