

The Political Economy of Unemployment Insurance Individual Savings Accounts:

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Abstract:	<p>In recent years, unemployment protection systems based on individual savings have been instituted in several developing countries. Chile was one of the first countries to establish such a system, which at the time was widely referred to as a model for other countries. This paper discusses the very particular political context in which the Chilean system was created before examining how it works in terms of coverage and levels of benefits received by unemployed workers. We undertake a detailed analysis of the administrative data produced by the system, and conclude that the insurance covers only a very small proportion of the unemployed as these workers generally had precarious jobs that did not allow them to contribute to the system consistently. The Chilean case illustrates how difficult it is to establish functioning unemployment insurance in developing countries with precarious labour markets. Based on the interaction between employment characteristics and the conditions imposed by the benefit system, we assess its efficacy and analyse whether the UISA can indeed serve as a model for other developing countries.</p>

The Political Economy of Unemployment Insurance based on Individual Savings Accounts: Lessons for other Developing Countries from Chile

INTRODUCTION

In recent years, several middle income developing countries have implemented unemployment insurance systems based on a financing mechanism which relies principally on individual savings accounts (ISAs). In some cases, these savings accounts are complemented by a minimal shared funding mechanism (a ‘solidarity pillar’) that aims to even out the risk of unemployment among the insured. These unemployment compensation systems have been much lauded and promoted by multilateral international institutions because they are considered to be easy to establish and administer, have low fiscal funding requirements, and limit the risk of moral hazard associated with more traditional insurance systems.¹

The literature on unemployment insurance systems in the developing world generally expresses concern that the risk of moral hazard is higher in countries where the institutional capacity to monitor the job search behaviour of the unemployed is more limited (Holzmann and Vodopivec, 2012). Systems based on ISAs, such as the Chilean one, are therefore expected to lower the risk of moral hazard, thus constituting a more feasible solution to the dilemma of unemployment in developing countries.

The Chilean unemployment insurance savings account (UISA) system provides us with an excellent case study for Latin America, and also for other developing countries. It was the first system to have been implemented that combined ISAs with a ‘Solidarity Fund’ designed to provide minimum levels of coverage to workers who had not been able to accumulate enough savings in their individual accounts. We must also consider that Chile has historically had an exceptional status in the Latin American region as a ‘pioneer’ of privatised Social Security systems to which so-called ‘solidarity pillars’ have been added over time, and which provide basic social protection floors for those not covered by their own savings.² In the same way that Chile’s pension system was once regarded as a model for other developing countries, its unemployment insurance has now also been copied elsewhere. For example, Colombia,

¹ In 2001, the International Labour Organization (ILO) described the Chilean unemployment insurance system as ‘new legislation that could lead to a new generation of reforms in unemployment insurance matters’ (ILO, 2001:50). See also Vodopivec (2013) for a succinct summary of this literature.

² See Contreras and Sehnbruch (2013) for a detailed discussion of how Chilean social security systems developed between 1990 and 2010.

legislated in 2013 to institute a system based on ISAs, while Mexico has legislated that it will implement such a system in the near future. Other countries, such as Mauritius implemented a similar system in 2009 ('Workfare Programme'), while Sri Lanka is still debating the precise form of the unemployment insurance system they wish to institute (Vodopivec, 2013). As we now have enough administrative data to examine how well the system is working, it is important to analyse whether the Chilean system can indeed serve as a model for other developing countries.

It is for this reason that this article dedicates an extensive part of the discussion to an analysis of the political circumstances that led to the implementation of the Chilean UISA system. As will be discussed below, the system's design responds to a very particular constellation of concerns about labour market flexibilisation and the potential for abuse of social protection systems, as well as the limited institutional capacity prevalent in Chile during the 1990s.

This article uses administrative data to examine the extent to which unemployed workers benefit from the Chilean UISA system. It is the first article on the insurance system to use data from a period when the system can be considered to have 'matured' rather than still being in a process of being implemented gradually through the incorporation of new contracts.³ Our data show that the functioning of the system is highly dependent on the employment conditions prevalent in the labour market in which it operates. In developing countries with a high proportion of temporary contracts and high levels of job rotation among workers with formal jobs, an ISA based system is unlikely to provide much protection against unemployment, especially because the unemployed tend to come from the more precarious segments of the labour market. This means that other Latin American countries with similarly poor employment conditions are therefore unlikely to benefit much from copying the Chilean system.

This article proceeds as follows: we begin by explaining the particular historical and theoretical context of ISA based unemployment insurance systems in Latin America generally, and in Chile more specifically. Section 3 then describes how the Chilean UISA system works, while section 4 uses administrative data to analyse its coverage. The article concludes by discussing to which extent the Chilean UISA system can serve as a model for other countries before closing with more general observations on the relationship between employment conditions and social protection systems in developing countries. The article's conclusions are highly relevant for future research on welfare states in developing countries, which tends to ignore the important

³ This point is discussed in more detail in section 4 of this article and is based on Table 2 in that section.

link between social protection systems and the labour markets on which they are based (Huber, 1996).

Before beginning, we must, however, draw attention to two issues. The first is that like all unemployment insurance systems in the world, the Chilean UISAs only cover salaried workers and not informal workers, who do not contribute to the system, and therefore cannot claim benefits either.⁴ This manuscript therefore does not discuss informality and its relationship with unemployment as this is a highly complex subject in its own right, which cannot be covered here.

Second, this article deliberately uses the term ‘unemployment insurance savings account system’ even though it is a cumbersome expression to illustrate that the Chilean system is not really an ‘unemployment insurance’ in the traditional sense. As we will see from the analysis that follows, the system can better be described as a mandatory savings system based on individual accounts with an unemployment insurance component.

THE CONTEXT OF UNEMPLOYMENT INSURANCE SYSTEMS IN LATIN AMERICA

Historical context

Of all the social protection mechanisms that have been instituted in developed and developing countries over the course of history, unemployment insurance is the most complicated (and often ideologically contentious) as there are no easily identifiable characteristics that make a person eligible for a potential benefit, such as an age limit (as with pensions), household structure or income levels (as with benefit payments), or a health condition (disability insurance). By contrast, in the case of the unemployed, the state has to monitor whether a worker is legitimately unemployed, looking for a new job, and available to take advantage of a potential job opportunity. Monitoring the behaviour of the unemployed is particularly difficult in developing countries, where many workers are employed informally or frequently switch between different (and sometimes multiple) precarious jobs.⁵ This also explains why most developing countries, even those in the higher middle income bracket, do not establish fully fledged unemployment insurance systems, and instead prefer to focus on other social

⁴ Evidence from panel surveys in Chile show that informal workers rarely become unemployed, but instead adjust to economic fluctuations through lower income levels.

⁵ The difficulties faced by developing countries in the establishment of functioning unemployment insurance systems mirror those experienced by developed countries during the late 19th and early 20th century, when insurance systems suffered from problems of low coverage, financing issues (sometimes bankruptcies), and fragmentation (some groups of workers were excluded ex-ante from the new systems) (Berg and Salerno, 2008: 88).

programmes such as health insurance, pension systems, or conditional cash transfer programmes. Most importantly, the perception that European unemployment insurance benefits were overly generous and had created undue moral hazard significantly shaped the theoretical and political debates on the subject in Latin America during the 1990s and 2000s, as will be discussed below.

Having said this, the problem of unemployment has always been an important subject for policymakers in the Latin American region, where historically frequent economic crises have led to bouts of high unemployment. Governments therefore began to consider implementing mechanisms that would protect workers against unemployment almost as soon as they began instituting basic labour market legislation in the 1920s. The logic of protecting workers against unemployment is enshrined in dismissal clauses, which generally require employers to give at least one month's notice, and in severance pay mechanisms that require employers to pay one monthly wage (generally) per year of service if the worker is made redundant.⁶

However, aside from debates on whether or to what extent severance pay legislation distorts the functions of labour markets in developing countries, it is clear that it does not work well as an unemployment 'insurance' mechanism.⁷ First, it does not cover workers who have worked informally or for short periods of time under fixed term contracts. Second, it is difficult to enforce severance pay legislation, and we know little about the extent to which it is actually paid in Latin America.⁸ Critics contend that employers use flexible, informal or precarious hiring mechanisms to avoid this legislation, which probably leads to unnecessarily high levels of job rotation. In addition, we know that severance pay is rarely paid in full as employers gamble that workers are unable to face the lengthy and expensive legal process required to enforce their rights. Finally, the right to severance payments evidently does not apply if a worker resigns voluntarily, or is fired for any form of misconduct.

Given the limited use of severance pay as a protection mechanism in the case of unemployment, some countries in Latin America oblige employers to contribute to an ISA to make a provision for potential future rights to severance pay. In this case, the worker has the right to withdraw funds from the account under any circumstance of job loss. This is the case, for example, of the Fundo de Garantia do Tempo e Serviço (FGTS) in Brazil and the Cuenta Individual de

⁶ A similar logic applies in Asian countries, although the amounts stipulated by severance pay legislation vary. See Asami (2013: 28).

⁷ For a debate on the disadvantages of severance pay, see for example Heckman and Pagès, 2000; and Holzmann and Vodopivec (2012).

⁸ More information is available on Asian countries, where payment levels are also low. See Asami (2013: 31).

Indemnización (CII) in Ecuador⁹ or the severance pay contributions paid by employers for domestic service workers in Chile. In fact, these mandatory savings accounts have been operating for many decades, and actually form the basis of the idea that unemployment insurance can be funded through ISAs. However, these savings account systems were instituted as a form of severance pay. They do not contain a ‘Solidarity Fund’ that pools risk between the unemployed. What was innovative about the Chilean system when it was instituted in 2002 was that it combined savings accounts with a solidarity pillar. (For a more detailed discussion of these subtle differences, see Sehnbruch, 2006 and Holzmann and Vodopivec, 2012).

Other countries in Latin America have also established limited traditional unemployment insurance systems in the past. They include Argentina, Brazil, Uruguay, and Venezuela.¹⁰ However, their coverage often excludes entire groups of workers from the insurance (such as construction workers, domestic or public-sector employees in Argentina), and their benefits are limited, both in terms of replacement rates and number of payments (Mazza, 2000 and Velazquez, 2010). It is the perceived limitation and unworkability of these traditional unemployment insurance systems in developing countries with weak institutions and largely informal labour markets that have led policymakers in Latin America and elsewhere to look for alternative insurance models.

Recent political context and theoretical debates in Latin America

The origin of the modern theoretical debate on unemployment insurance in Latin America lies both in the historical experiences described above as well as in the recommendations made by the Washington Consensus to flexibilise labour markets in the region, in particular by reducing or abolishing severance pay mechanisms to boost the creation of more and better jobs, especially for low income workers, women, and young people (Heckman and Pages, 2004). However, such reforms are politically difficult to implement, as illustrated by the fact that severance pay mechanisms have not been reformed or eliminated from Latin American labour legislation.¹¹ Its persistence has therefore led to the recommendation that severance pay be replaced by functioning unemployment insurance mechanisms based on ISAs, which could then

⁹ Employee Indemnity Guarantee Fund and Individual Compensation Account respectively.

¹⁰ A Chilean unemployment benefit scheme also existed prior to 2002, but its benefits were so limited that few unemployed workers bothered to claim them (Sehnbruch, 2006).

¹¹ A discussion of why not can be found in Sehnbruch (2012) and Carnes (2014).

function as a kind of ‘provision’ against severance pay, and be deducted from any final severance payment made.¹²

Furthermore, unemployment insurance is also a part of the ‘second generation’ of reforms recommended by the Washington Consensus institutions that advocate improving active labour market policies in developing countries, by establishing vocational training programs and institutions that can better match workers and jobs (Inter-American Development Bank, 2004 and World Bank, 2013). Unemployment insurance is part of this recommended package.

In this context, the existing literature often begins by explaining that unemployment insurance constitutes ‘a legitimate space for public policy action’ because, as historical experience in both Europe and Latin America has shown, such an insurance cannot be provided through voluntary mechanisms or by private providers, as imperfect information systems and adverse selection criteria make the systems unworkable (Chetty and Finkelstein, 2012: 2; quoted in Vodopivec, 2013).

However, this raises the question of how unemployment insurance can be optimally designed in developing countries, where unemployment is not a ‘discrete’ event and where job search effort cannot be monitored.¹³ Workers, for example, can receive benefits from unemployment insurance systems while either working informally, or not bothering to look for a job at all. This raises the spectre of ‘moral hazard’ as studies from developed countries are often extrapolated to developing countries even though analysts recognise that unemployment in developing countries is a completely different phenomenon (Vodopivec, 2013). Yet, repeatedly, analysts working on optimal social insurance design in developed countries are quoted in the literature on developing countries. Espino and Sanchez (2013), for example, quote Hansen and Imrohoroglu, (1992: 2), who are referring to a general equilibrium model based on the United States economy, when they say that ‘if there is moral hazard, and the replacement ratio is not set optimally, the economy can be much worse off than it would be without unemployment insurance.’¹⁴

¹² See Ferrer and Riddell in Holzman and Vodopivec (2012)

¹³ Vodopivec (2013: 3) uses the term ‘discrete event’ to reflect the fact that in an industrial and urbanised society, workers either work or do not work. He contrasts this with developing countries well workers can ‘resort to self- or home production, because they are divorced from ownership of means of production.’

¹⁴ Similarly, papers by Feldstein and Altman (1998); Orszag and Snower (2002); and Parsons (2003) are frequently cited by the development literature on unemployment insurance.

Political context and theoretical debates in Chile

Concerns about moral hazard such as these have profoundly shaped the debate about unemployment insurance in Latin America from a theoretical perspective and have been incorporated by the Chilean literature on the subject. They led policy makers to search for a new balance between fiscal cost, social insurance and potential mechanisms of abuse by combining insurance contributions with ISAs (Acevedo 2002 and 2006; Calvo, 2002; Ministerio del Trabajo, 2000; Solari 2002; Velasquez, 1998).

In addition to the profound influence of the international literature on Chilean policymakers, we must also consider Chile's role as a pioneer of privatised social insurance.¹⁵ Its pension system based on ISAs was instituted in 1981, and health insurance based on individual insurance plans was established in 1983. Any funding mechanism for unemployment insurance based on sharing risk among workers, was therefore viewed with suspicion during the intensely neoliberal public policy atmosphere of the 1980s and 1990s, which had not yet fully analysed or understood the failings of individualised and privatised social insurance.¹⁶ In this context, traditional unemployment insurance as it existed at the time in Europe, was viewed very negatively, especially by employers' associations and the political right, as is illustrated by the following quotation, from an interview with the president of one of them in 1993:

The experience has been extraordinarily negative. The majority of these countries – Spain, England, and other nations of Europe, and including the USA, are having great trouble reversing these systems, which only tend to encourage leisure There is an increasingly larger group of people that makes arrangements to live off these benefits without any interest whatsoever of working in the formal economy. Moreover, many continue working informally and earning a double income....it would be foolish on our part if we should wish to apply a system in Chile that has been proven, by other countries that came before us, to be wrong and negative.¹⁷

Another influential Chilean labour market analyst, for example, wrote at the time: 'it is well-known that unemployment insurance systems in Europe have failed' (Beyer, 2000). This illustrates the simplistic arguments into which complex problems were distilled.

¹⁵ See Chapters 8-12 in Sehnbruch and Siavelis (2013) for background information on this subject.

¹⁶ Although a national health insurance does exist in Chile, financed by contributions from lower income workers and the state, even to this day there is little shared funding between public and private insurers. See Infante and Paraje (2010) for details.

¹⁷ Interview with José Antonio Guzmán, President of the Confederación de la Producción y del Comercio (CPC), Chile's principal employer organization, between 1990 and 1996 in *El Diario Financiero*, 19th April, 1993. Quoted in Haagh (2004).

The idea of instituting unemployment insurance to protect the unemployed, and positive arguments in favour of unemployment insurance, such as theories related to job – skill matching and counter cyclical expenditure, therefore rivalled with a political economy consensus that was intensely suspicious of any form of state intervention in markets (especially in the labour markets), and of risk sharing. This explains why the Chilean literature on the subject begins by explaining that there is a legitimate role for public policy and the State in the provision of unemployment insurance, as it cannot be provided by a private insurance system (Acevedo, 2002 and 2006; Solari, 2002, Velazquez, 2010).

Initial proposals to establish unemployment insurance in Chile were based purely on ISAs, and contemplated only an additional fiscal subsidy for those who did not qualify for the insurance payments.¹⁸ Until the 1999 economic crisis, legislative proposals languished on the political backburner. But when the unemployment rate in Chile almost doubled within the space of one year to over 10 per cent, and clearly affected the most vulnerable workers most, unemployment insurance became a political priority. Due to lack of data issues, policymakers at the time did not, however, realise the extent to which the formal sector of the Chilean labour market had become flexibilised through non-traditional contractual mechanisms, such as short-term, subcontracted, or freelance contracts, or simply through open-ended traditional contracts with short durations.¹⁹ This fact was therefore not taken into account when the system was originally designed.

The structure of the Chilean UISA discussed in the following section was born out of a political ideology particular to Chile during the late 1990s, out of a Washington Consensus recommendation to flexibilise labour markets (by replacing severance pay with a more flexible structure of unemployment insurance), and out of an almost complete lack of information on the state of the Chilean labour market. The objective of preventing moral hazard thus outweighed the objective of protecting workers who lost their jobs, and led to a system which imposed such stringent conditions of eligibility on workers claiming benefits that its coverage of the unemployed turned out to be negligible. This is how a system that was only instituted in 2002 already had to undergo a first reform in 2009 in response to the realisation that its real coverage

¹⁸ See Ministerio del Trabajo (2000) and Velasquez (1998 and 2010).

¹⁹ For more detail see Sehnbruch, 2006. The UISA was, in fact, designed, without any reliable information on the types of contracts used, the duration of these contracts or of the characteristics of workers who became unemployed. The official Chilean labour market survey (Encuesta Nacional del Empleo) included questions on the type of contract and on employment duration in 2010. Before then, the Chilean national household survey (Caracterización Socioeconómica de Hogares, CASEN) asked about contracts and duration in 1996. However, the results from this survey show that the survey information and the administrative data are very different.

was minimal.²⁰ It was then reformed again in 2015, in an effort to make the Solidarity Fund more accessible to the unemployed.

THE STRUCTURE OF THE CHILEAN UISA: GENERAL CONDITIONS, FUNDING AND BENEFITS

Funding

The Chilean UISA is a mixed system which is financed by all three social actors (government, employers, and workers). The system generates two principal funding mechanisms: individual savings accounts (ISAs) for each worker financed by contributions from the worker and employer in the case of open-ended contracts, and only by employers in the case of workers with fixed-term contracts. In addition, the system generates a Solidarity Fund (Fondo de Cesantía Solidario – Unemployment Solidarity Fund), financed by employers and fiscal contributions (see Table 1 below for details).

The contributions each worker makes to her ISA constitute the worker's personal savings, withdrawable only in the case of unemployment, termination of contract, retirement or any other event in which the worker leaves or loses her job. The UISA system establishes different methods of financial contributions depending on the type of contract held by a worker. In the case of workers with open-ended contracts, employers pay 1.6 per cent of gross wages into the ISAs of their workers, while workers pay an additional 0.6 per cent of their gross wages into their ISAs. Over the course of one calendar year, these contributions add up to one quarter of a worker's monthly wage. In addition employers contribute 0.8 per cent of their total gross payroll into the Solidarity Fund, which also receives fiscal contributions. Finally, both the ISAs and the Solidarity Fund are administered by the Sociedad Administradora de Fondos de Cesantía (AFC Chile) – Administration for Unemployment Funds.

For workers with fixed term contracts the contributions to the UISA system are made only by employers, and amount to 2.8 per cent of a worker's gross wage. An additional contribution of 0.2 per cent is paid into the Solidarity Fund.

All of these payments are limited to a maximum of 11 years. If a worker stays in the same job for more than 11 years, contributions to the UISA system cease as it is assumed that 11 years allow for a sufficient accumulation of resources in the ISAs to cover the eventuality of

²⁰ In an interview undertaken on 8th September 2016, a senior official of the Ministry of Labour who participated in the discussions leading up to the 2009 reform of the UISA confirmed that even during this reform the concern of experts over the possibility of generating undue moral hazard by making this insurance system more generous was predominant and outweighed other considerations.

unemployment (Beyer, 2000; Acevedo et al., 2006).²¹ Nevertheless, the employer's obligation to contribute to the Solidarity Fund remains until the end of the working relationship.

(Insert Table 1. Structure of the Chilean Unemployment Insurance Savings Account System, including 2015 reform here)

Benefits paid by the UISA

To withdraw money from the UISA system, workers have to have contributed to it (not necessarily continuously) for 12 months in the case of workers with open-ended contracts, and for six months in the case of workers with short-term contracts over the course of the last 24 months. In either case, the last three contributions have to have been continuous and from the same employer. Also, workers have to be between 18 and 65 years of age, and have to have been unemployed for at least 30 days. The amount and number of payments that can be withdrawn from the individual savings account therefore depends on the type of contract held by a worker prior to becoming unemployed, on the amount accumulated in the worker's ISA, and, on the cause of dismissal.

Prior to 2016, replacement rates decreased in increments of 5 percentage points from 50 per cent to 20 per cent over a maximum period of seven months. As of 2016, replacement rates were set at 70 per cent, and then decrease at the same rate of 5 per cent until a minimum of 30 per cent. If a worker has sufficient savings the number of withdrawals that can be made is unlimited, although after the seventh month of unemployment the replacement rate is maintained constant at 30 per cent. If the funds accumulated in a worker's individual savings account are insufficient to fund a period of unemployment and the worker was dismissed for economic reasons (i.e. through no fault of his or her own), he or she has the right to obtain additional benefits from the system's Solidarity Fund. The amount and number of payments made by the Solidarity Fund provide replacement rates for up to five months that are equal to what a worker would obtain from his or her ISA. However, these payments are subject to legal minimum and maximum amounts (See Table 1 above).

If a worker changes jobs without passing through a period of unemployment in between, his or her status in the UISA system is reset. Funds can then be either withdrawn from the savings account or left in the account for future use. In either case this does not affect the obligation of the new employer to contribute to the insurance system.

²¹ In addition, the limitation of unemployment insurance payments to 11 years is related to the structure of severance pay in Chile, which is set at one month's wage per year of service with a limit of 11 months wages. Since accumulated savings from the unemployment insurance system are deducted from severance pay liability, the insurance legislation matched this time period.

Unemployed workers thus only receive payments from the Solidarity Fund if their own savings are insufficient to cover their period of unemployment. Workers who resign from their job only have the right to receive payments from their ISA, but not from the Solidarity Fund. It is this inclusion of a Solidarity Fund that distinguishes the Chilean UISA system from other unemployment insurance systems in Latin America and that led to its description as a model for other developing countries.

Beneficiaries of the UISA system are also automatically registered with municipal employment offices (Oficina Municipal de Intermediación Laboral (OMIL) – Municipal Labour Intermediation Office). For this purpose a national employment exchange was created (Bolsa Nacional de Empleo), which facilitates the process of employment placement services of municipal administrations, thus contributing to a better match between employment demand and supply. Unemployed workers receiving insurance payments and made redundant for economic reasons have preferential access to vocational training programs offered by Chile's national training and employment service, the Servicio Nacional de Capacitación y Empleo (SENCE) – National Training and Employment Service. Unemployment insurance payments cease if a worker refuses a place on a vocational training program offered and financed by the SENCE. Similarly, insurance payments are suspended if a worker without justification rejects an employment opportunity (with a salary equal or superior to the minimum wage or at least 50 per cent of the worker's former salary) offered by a local municipal employment intermediation service.

This UISA system operates in parallel to the severance pay legislation, which entitles workers with open-ended contracts made redundant to one month's wage per year of employment duration with a maximum limit of 11 months' wages. The UISA system does not affect severance pay entitlements, except for the fact that contributions made by the employer to a worker's ISA are deducted from them. UISA contributions can therefore be regarded by employers as a provision for future severance payment costs.

The four main factors that determine benefits received from the UISA are the reason for unemployment, the duration of the previous job and its wage level, and the contractual status the worker had prior to becoming unemployed (open-ended or fixed-term contracts). These are therefore the conditions that we have to take into account when analysing the empirical evidence that relates to the functioning of the Chilean unemployment insurance system.

EMPIRICAL EVIDENCE FROM THE CHILEAN UISA

The Coverage of the Chilean UISA (real usage)

The question of how many workers benefit from the system and under what conditions is, of course, crucial to understanding how the Chilean UISA system works, and whether it should serve as a model for other developing countries. In this section, we first examine the real usage that is made of the system in terms how many workers contribute and actually receive benefits from the system. As the level of benefits claimed are low, we then proceed to simulate the hypothetical coverage of the UISA, i.e. how many workers are theoretically covered even if they do not make a claim when becoming unemployed.

Since the UISA system was instituted in 2002, only formal employment contracts that entered into effect after November 2002 become part of the UISA. As we can see from Table 2 below, which is based on the annual reports published by the Superintendent of Pensions in Chile, the insurance now covers 52 per cent of the total labour force, and over 75 per cent of the eligible salaried labour force.²² Workers not covered by the insurance are the self-employed, public sector employees (including the military and police), who are subject to a different Labour Code, as well as domestic service workers (who have a severance pay system to which employers contribute).

(Insert Table 2. Proportion of total work force and unemployment covered by the unemployment insurance system (in thousands and per cent))

In terms of methodology, this article uses a random 5 per cent sample of all workers affiliated to the system, who number 4,4 million contributors for the year 2015.²³ The available database follows individuals from the moment they make their first contribution to the system and includes their monthly contribution histories until December 2015. To analyse this data, we constructed two different databases from the sample: the first (sample 1) uses cross-sectional data from the month of November²⁴ for each year and the second (sample 2) compiles data on all of the employment relationships that terminated in a given year. The second sample therefore allows us to analyse the employment conditions of workers who subsequently become unemployed or stop contributing to the system. All the tables that follow specify whether they are using the full database or one of the two samples.

²² Note that this calculation relates the administrative data from the UISA to data from Chile's official labour force survey, the *Nueva Encuesta Nacional de Empleo (NENE)* to arrive at an approximate calculation of real coverage.

²³ This random sample of administrative data is provided in anonymised form by the Chilean Supervisory Agency of the pension system (Superintendencia de Pensiones).

²⁴ We have chosen the month of November rather than the year end month of December as December employment data in Chile is affected by the entrance of seasonal workers into the labour market, which positively distorts participation rates and negatively distorts the distribution of contracts as seasonal workers are overwhelmingly hired on a short-term basis.

Table 3 below shows that due to this gradual process of incorporating new contracts, the proportion of fixed-term contracts (which rotate more frequently) initially outweighed the proportion of open-ended contracts. However, by 2005, these proportions inverted, and open-ended contracts became the majority. By 2015, 70 per cent of workers had an open-ended contract, while 30 per cent were hired on a fixed-term basis. The data shows that the characteristics of contributors to the UISA stabilised after 2009, with few significant changes in the composition of the data since then. This is an important point to bear in mind, as it means that studies undertaken of the UISA which use data from prior years may be significantly biased due to the evolving nature of the insurance system.²⁵

Table 3 also shows that the employment conditions of workers with open-ended and fixed-term contracts can vary significantly. On average, fixed-term contracts earn only 62 per cent of the average wages of open-ended contracts or 69 per cent of their median earnings (2015). Similarly, the duration of fixed-term contracts is much lower, at 10 months on average compared to the average duration of almost 40 months for open-ended contracts.

Table 3 also shows differences between the average duration of periods of non-contribution for workers who had open-ended or fixed-term contracts. In this context, we must note that we cannot assume that workers are necessarily unemployed while they are not contributing to the UISA. Since we have no information on what they are actually doing while they are not contributing, we have to consider that they may be unemployed, working informally or are inactive. It is important to emphasise this point as those studies of this UISA that analyse whether the system generates moral hazard or not simply assume that workers are unemployed while they are not contributing.²⁶ From Table 3 we can see that fixed-term workers on average spend around six months not contributing to the UISA, and over 50 per cent of them do not contribute to the UISA for longer than three months. Workers with open-ended contracts, on the other hand, spend an average of just under two months not contributing between jobs, and only 16.6 per cent of them take longer than three months to start contributing again from a new job. Unfortunately, it is impossible to analyse these differences in more detail as we do not know whether workers are genuinely unemployed while they are not contributing.

²⁵ Studies by Huneus et al. (2012) or Reyes et al. (2010), for example, use data from prior years.

²⁶ See for example Huneus et al. (2012), Fajnzylber and Poblete (2011), and Reyes et al. (2011). The fact that we do not know what workers are doing while not contributing to the UISA system also extends to those workers who may be claiming benefits from the system. This is also true for workers claiming benefits from the Solidarity Fund, who, theoretically, must be actively looking for work, and who must accept job offers with particular criteria (see details in Table 1 of this article). These conditions do not, however, preclude workers from working informally elsewhere.

(Insert Table 3. Development of the UISA (In thousands and per cent)

(Insert Table 4. Payments of Unemployment Insurance Benefits)

Table 4 above shows that of all the workers who stop contributing to the system²⁷ (either due to unemployment, informal work or inactivity), only 28 per cent actually made an insurance claim in 2015, almost all of which were approved.²⁸ Of these workers 62.5 per cent had fixed-term contracts, while 37.5 per cent had open-ended ones prior to becoming unemployed. Of these beneficiaries, 15.3 per cent receive some form of payout from the Solidarity Fund once they have used up savings accumulated in their ISAs. This proportion is higher for workers who had open-ended contracts (20.4 per cent) but lower for workers who had fixed term contracts (9.4 per cent). Table 4 also shows that on average workers received 2.2 payments from the UISA system with an average replacement rate of 44.4 per cent.

From Table 4 we can see that few workers who stop contributing to the UISA system actually apply for and receive benefits (just over 25 per cent). If we then look at how many of these workers actually receive payouts from the Solidarity Fund, this proportion decreases to 15.3 per cent. The data further indicate that the 2009 reform of the UISA system neither significantly increases its level of payouts, nor the proportion of workers benefiting from the Solidarity Fund.

In part, this figure is so low because 43 per cent of workers who are entitled to payments from the Solidarity Fund do not claim these benefits (Huneeus et al., 2012). This data is consistent with reports from other experts (Fajnzylber and Poblete, 2011; and Reyes et al., 2011) and with survey data (Consejo Asesor, 2008). The reasons for this low coverage are not clear. Although the Ministry of Labour tried to research this question through a survey that was applied to contributors in the system, the response rate to this survey was rather low so that the survey's conclusions are not considered to be conclusive, and have not been made public.²⁹

²⁷ Defined as workers who stopped contributing to the system for longer than one month during a given year.

²⁸ 8.2 per cent of the benefits requested are rejected because workers are still in a current employment relationship at the time they make their claim (i.e. they are not unemployed according to the register of contributions); 4.4 per cent are rejected because the job for which the worker is claiming benefits is not the last job registered by the UISA database; and 2.5 per cent are rejected because the system shows that previous claims made are still outstanding. There are other reasons for which claims are also rejected, such as the claimant never contributed to the UISA or the employer is not registered in the system, but these reasons add up to less than 1 per cent of total claims.

²⁹ Interview with senior official from Ministry of Labour, September 2016.

Again, and as discussed above, one possible explanation for the low take-up rate is that workers are not actually unemployed when they do not contribute to the system. It also seems that workers on average expect to spend only two months without contributing to the system (Consejo Asesor, 2008) so may therefore not bother to make a claim. Lack of information about the UISA system and how to make a claim may also be a problem. Similarly, low replacement rates (38-44 per cent according to Table 4 above) and the conditions requiring workers to register with employment offices (and potentially accept jobs offered) may put workers off. In addition, Huneus et al. (2012) present strong evidence that workers who decide not to claim UISA benefits despite having the right to do so have a higher probability of finding a new job.³⁰

The hypothetical Coverage of the Chilean UISA

Given that the levels of benefit claims of the Chilean UISA are so low, it is important to ask whether workers are at least hypothetically covered by the system, even if they chose not to claim benefits. In this section, we therefore analyse these low levels of usage from two perspectives: first, we examine how the history of the workers' contributions relates to the conditions imposed by the UISA system under which workers may benefit from its insurance component (Table 5). Second, we look at other characteristics of workers, such as their age, sex, or level of education, to analyse which workers are more likely to benefit from the system (Table 6).

Table 5 simulates the potential coverage of the UISA system of those people who stop contributing to the insurance system in a given year (the potentially 'unemployed'), and who should therefore be entitled to receive some form of benefit, provided they have accumulated enough savings in their individual accounts, either from their prior job or from previous jobs. This means that we simulate the level of benefits that workers would receive if everybody who stops contributing to the system actually made a claim. By contrast, Table 4 only looked at actual claims made in the system.

We constructed Table 5 by examining the relationship between the different types of contracts that workers had before ceasing their contributions to the UISA system, the reasons why their employment relationship ended, and the level of contributions that must be made to the system before being able to claim benefits. We find that if all workers who stopped contributing to the insurance system during 2015 made a claim, only half of these workers would actually receive a payment from the system. Of this universe of potential claimants, 51 per cent would receive a benefit from the Solidarity Fund, while the remaining beneficiaries would have accumulated

³⁰ See also Fajnzylber and Poblete (2011) for details on these arguments.

enough savings in their ISAs to receive payments from these accounts. The other 50 per cent of the workers who stop contributing to the system do not accumulate enough contributions in their ISAs to be entitled to a payout. This result can be explained by the fact that a high percentage of those workers who do become ‘unemployed’ had fixed-term contracts in their previous jobs during which they did not accumulate sufficient contributions in their ISAs to be able to claim benefits. This fact is supported by the evidence presented in Table 3, which showed that 50 per cent of fixed-term contracts do not even last three months. One potential reason why the administrative data presented in Table 4 shows that a significant proportion of ‘unemployed’ workers never claim benefits may therefore be that these workers know when they leave a job that they do not have sufficient savings accumulated in their ISAs to make a worthwhile claim.

(Insert Table 5. Coverage of the UISA of all unemployed workers)

The results on Table 5 are different from the results presented in Table 4, because our simulation uses the entire universe of potentially unemployed workers and examines their rights to benefits, rather than just looking at those workers who actually receive benefits. It is important to examine the data from this perspective, because these results eliminate the self-selection bias included in Table 4 that is introduced by the fact that the real payments made by the system are only made to people who actually claim benefits. Overall, the combined results of Table 4 and Table 5 show that few ‘unemployed’ workers actually benefit from the ‘insurance component’ of the UISA system, i.e. from some form of payment from the Solidarity Fund. This prompts the question of whether there are other characteristics particular to the worker that might explain who receives benefits from the system.

In Table 6, we examine the characteristics of the different groups of workers with particular levels of coverage that were defined in Table 5. The first thing we can observe is that there are significant differences between these groups: Around a third of all workers are women, but workers with open-ended contracts and with access to the Solidarity Fund show a higher concentration of women, while only 25 per cent of fixed-term workers without access are women. As expected, people who have enough savings in their ISAs and who therefore do not need the Solidarity Fund are older, more educated, with higher wages and more stable jobs. This is particularly true for workers who had open-ended contracts. In terms of economic sectors, the workers least protected by the UISA can be found in the agricultural, construction and real estate sectors, which are known for hiring workers on a fixed-term basis.

(Insert Table 6. The Characteristics of workers with at least one month pause of contribution to UISA in 2015)

Finally, Table 7 uses a probit regression to study the relationship between the variables described in Table 6 and the probability of actually using the UISA further. Table 7 includes three regressions: for all workers, only workers who have enough savings to fund a period of unemployment, and workers with rights to Solidarity Fund payments.³¹ As expected, having an open-ended contract is positively related with using the UISA. The same is true for older workers and higher levels of income. When considering the whole sample, having a higher level of education is related to a lower probability of using the UISA, but once a worker has the right to the Solidarity Fund, having higher education is positively related to using the system. In terms of economic sectors, among workers with the right to use the Solidarity Fund, there is a higher relative presence of the fisheries and construction sectors, and a lower presence of teachers. The duration of the employment relationship has a positive impact, as does a longer duration of the most recent period of non-contributions, which has a stronger relationship among people with right to the Solidarity Fund.

At first glance, these results seem counterintuitive, as one would expect workers with lower levels of income to be more likely to claim benefits from the UISA. The data, however, makes sense if we relate them to Table 5 above, which shows that many of the ‘unemployed’ (workers, who cease to contribute to the system) do not accumulate enough contributions in their ISAs to be able to receive benefits from the system.³² The regression analysis thus confirms that workers who had precarious jobs prior to becoming unemployed are also the least protected by the UISA.

(Insert Table 7. The Characteristics of Employed and ‘Unemployed’ Workers here)

³¹The results show the point estimate for each regression. Marginal effects are available on request.

³² We need a longer period of data from the unemployment insurance database after 2009 to be able to determine more specific details about how contribution trajectories influence the potential use of the UISA system.

CONCLUSIONS

The Chilean case illustrates how difficult it is to establish a functioning unemployment insurance in developing countries that guarantees appropriate levels of coverage and benefits, has low administrative costs, and provides the right balance of incentives between protecting the income levels of the unemployed and avoiding moral hazard. To establish which lessons other developing countries can learn from the Chilean case, in particular from its hybrid nature that combines both ISAs with a risk sharing mechanism, we must consider several aspects.

First, we must question whether the system genuinely succeeds in avoiding moral hazard in the way it was expected to do. As discussed throughout the text, examining this issue is difficult as we do not know whether people who stop contributing to the system are genuinely unemployed or not. Initial studies carried out by experts suggest that some degree of moral hazard is operating among users of the Solidarity Fund (Huneus, 2012; Reyes *et al.* 2011). This finding would suggest that moral hazard can never be entirely avoided in unemployment insurance systems, even when the actual insurance component of the system (the Solidarity Fund) is quite limited. Whether this finding is, however, conclusive is doubtful, mainly because we know so little about why the vast majority of potential beneficiaries from the system never claim benefits. Further research on the behaviour of those workers who stop contributing is needed to be able to come to more reliable conclusions.³³ While the question about moral hazard is therefore theoretically interesting, it is not relevant in the context of a UISA system in which only 1.5 per cent of the ‘unemployed’ receive a benefit from its insurance component.

The second important lesson that developing countries can learn from the Chilean case is how difficult it is to construct functioning social protection systems based on contributions from formal employment in a labour market that is highly precarious. The Chilean government has recognised and responded to this difficulty by twice reforming a system, which has only been operational since 2002 and initially provided even more limited coverage.

The Chilean UISA system would probably work quite well in a labour market in which long-term, stable employment relationships predominate. However, the reality of most developing countries is that even their formal labour markets are relatively precarious. The high proportion of short-term contracts prevalent in the Chilean labour market combined with high levels of job

³³ Once the 2015 reform of the UISA system has been operating for at least a year and a more recent database becomes available, we will be able to undertake a sequential differential and differential analysis.

rotation of all contracts, but especially of short-term contracts means that those workers who are most likely to become unemployed are the least likely to accumulate sufficient benefits to cover an extended period of unemployment. Given current job rotation levels in Chile, it would therefore be difficult for any unemployment insurance (traditional or otherwise) to provide adequate coverage. Whether other countries should copy the Chilean model or not therefore depends on the characteristics of their own labour markets.

While the current UISA system could probably be improved further by reducing contribution requirements and increasing potential benefit levels, the current system is neither particularly onerous in terms of its eligibility criteria, nor particularly stingy in terms of its replacement rates if compared with other systems in developing countries. Furthermore, making the Chilean UISA more generous is unlikely to solve the fundamental problem generated by the high levels of job rotation in the Chilean labour market. As it seems that other developing countries, especially in the Latin American region, have similar problems with job turnover (Banco Central de Chile, 2016: 27) we must therefore emphasise that more traditional mechanisms of social protection such as emergency employment programmes or conditional cash transfer programmes are still essential to preventing families from falling below the poverty line when household members become unemployed, especially during times of high unemployment rates or economic crisis.

Finally, policymakers attempting to copy the Chilean UISA system in other developing countries must also remember that it was established in a very particular political economy context. As section 2 of this article highlighted, the historical moment during which the system was designed meant that policymakers were more concerned with whether an insurance system would generate moral hazard rather than whether it would protect the unemployed from significant drops in income levels.

Overall, the Chilean case illustrates how important the interrelationship is between the conditions of a social security system and the employment conditions on which it is based. If employment conditions are too precarious, social security systems cannot function appropriately. This means that contribution-based systems without sufficient risk-sharing components between potential beneficiaries can significantly increase the need for fiscal contributions from governments in developing countries with limited resources, especially during periods of high unemployment when governments must focus on preventing significant increases in poverty levels.

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Table 1. Structure of the Chilean Unemployment Insurance Savings Account System, including 2015 reform

		Pre 2015 reform (2009-2015)		Post 2015 reform	
Conditions of the UISA: Contributions and Benefits		Workers with open-ended contracts	Workers with fixed-term contracts	Workers with open-ended contracts	Workers with fixed-term contracts
Conditions relating to Contributions to the UISA system	General Conditions	Age range of workers: 18 - 65 years Had a formal written contract			
	Contribution to ISAs	Total contribution 2.2%: 1.6% from employers 0.6% from workers	2.8% only from employers	No change	No change
	Employer Contribution to Solidarity Fund	0.8%	0.2%	No change	No change
	Government Contribution to Solidarity Fund	225,792 monthly tax units (<i>Unidad Tributaria Mensual</i>)* per year (around 16 million USD)			
Conditions relating to Benefits paid by the UISA system	General Conditions	Benefits from ISAs can be applied for under any circumstance of job loss, including voluntary resignation, mutual agreement, redundancy, or end of fixed-term contract. The level of benefits, however, varies depending on the cause of job loss.			
Benefits receivable from ISAs	Contributions to UISA required before being able to withdraw funds	12 not necessarily continuous contributions since last UI payment	6 not necessarily continuous contributions since last UI payment	No change	No change
	Number of payments receivable from ISA	As many payments as individual funds can provide based on the replacement rates established below.			
	Monthly replacement rates	50%, 45%, 40%, 35%, 30%, 25% and 20% until funds run out (there is no time limit to these payments)		70%, 55%, 45%, 40%, 35% and 30% until funds run out (there is no time limit to these payments)	

		Pre 2015 reform (2009-2015)		Post 2015 reform		
		Workers with open-ended contracts	Workers with fixed-term contracts	Workers with open-ended contracts	Workers with fixed-term contracts	
Conditions relating to Access to the Solidarity Fund		Contributions required before being able to receive payments from Solidarity Fund				
		12 contributions over a 24 month period, with the last 3 contributions being continuous and from the same employer				
		When the Solidarity Fund becomes accessible				
		Funds from ISA are unable to provide minimum replacement rates stipulated below				
		Replacement rates covered by Solidarity Fund	5 payments over 5 months @ 50%, 45%, 40%, 35%, 30% (with legal maximum and minimum amounts that are stipulated by the law and adjusted each year with inflation).	2 payments over 2 months @ 35% and 30% (with legal maximum and minimum amounts that are stipulated by the law and adjusted each year with inflation).	5 payments over 5 months @ 70%, 55%, 45%, 40%, 35% (with legal maximum and minimum amounts that are stipulated by the law and adjusted each year with inflation). In addition, a maximum of 10 SF payments can be made over a period of 5 years.	3 payments over 3 months @ 50%, 40%, 35% (with legal maximum and minimum amounts that are stipulated by the law and adjusted each year with inflation).
Emergency payments from Solidarity Fund that become available when the national unemployment rate reaches levels that exceed the rolling average of the last 4 years by 1 %		2 more payments over two months @ 25%			2 more payments over two months @ 30%	
Other Conditions that must be fulfilled when receiving Solidarity Fund benefits		Beneficiaries must search for a job “in an effective way” (i.e. register with local employment offices and labour market exchange website, attend interviews for job offers, not reject any job offer at least equivalent to 50% of the last received wage). Beneficiaries also have to attend vocational training courses if these are offered by the local employment office.				

Souce: Authors’ summary based on the analysis of unemployment insurance legislation.

* The Monthly Tax Unit is a currency unit established for fiscal use in Chile that is adjusted for inflation on a monthly basis.

Table 2. Proportion of total work force and unemployment covered by the unemployment insurance system (in thousands and per cent)

	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Number of open-ended contracts	94.5	353.4	730.6	1,054.6	1359.4	1657.0	1931.2	2135.1	2243.8	2480.1	2666.8	2861.9	2,942.4	3,113.0
Number of fixed-term contracts	335.0	686.0	857.6	1,013.3	1112.2	1199.9	1234.7	1099.9	1262.1	1335.4	1436.0	1409.6	1,384.7	1,334.2
Total number of contracts in UISA	429.4	1039.4	1,588.2	2,067.9	2,471.6	2,856.8	3,165.8	3,235.0	3,505.9	3,815.5	4,102.8	4,271.5	4,327.1	4,447.2
Total Labour Force (NENE)	6,177.4	6,395.5	6,605.1	6,798.5	6,806.2	6,949.5	7,201.3	7,302.4	7,774.6	8,054.2	8,150.2	8,280.4	8,435.7	8,557.0
UISA Coverage of Labour Force	7.0%	16.3%	24.0%	30.4%	36.3%	41.1%	44.0%	44.3%	45.1%	47.4%	50.3%	51.6%	51.3%	52.0%
Total Salaried Labour Force (NENE)	3617.6	3670.5	3807.7	3986.1	4166.3	4360.9	4582.5	4501.9	4910.5	5143.0	5361.9	5481.4	5530.7	5651.1
UISA Coverage of Salaried Labour Force	11.9%	28.3%	41.7%	51.9%	59.3%	65.5%	69.1%	71.9%	71.4%	74.2%	76.5%	77.9%	78.2%	78.7%

Source: Authors' calculations based on data provided by the annual reports published by the Superintendencia de Pensiones in Chile. Labour force data is from Chile's official labour force survey, the Nueva Encuesta Nacional de Empleo (NENE).

Table 3. Development of the UISA system in terms of its contributors (In thousands and percent)

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Proportion of people working with OCs or FCs on November	64.5	61.2%	60.5%	59.5%	60.2 %	58.0 %	54.2 %	55.3 %	56.0 %	55.9 %	54.7 %	53.0 %	51.5 %
Proportion of people without contributing to the UISA on November	35.5	38.8%	39.5%	40.5%	39.8 %	42.0 %	45.8 %	44.7 %	44.0 %	44.1 %	45.3 %	47.0 %	48.5 %
Proportion of Open-ended Contracts	36.7	46.1%	51.9%	54.0%	57.5 %	59.9 %	64.6 %	63.3 %	63.7 %	65.1 %	67.0 %	67.6 %	70.1 %
Proportion of Fixed-term Contracts	63.3	53.9%	48.1%	46.0%	42.5 %	40.1 %	35.4 %	36.7 %	36.3 %	34.9 %	33.0 %	32.4 %	29.9 %
Average income of FCs as a Proportion of Average Income of OCs	64.3	62.8%	62.2%	61.8%	57.8 %	58.5 %	59.1 %	57.0 %	57.4 %	58.9 %	61.0 %	61.4 %	61.7 %
Average income of FCs as a Proportion of Median Income of OCs	78.7	73.5%	71.6%	70.4%	66.5 %	66.8 %	64.3 %	63.0 %	62.5 %	64.1 %	65.8 %	66.3 %	68.9 %
Averageduration of OCs	7.2	11.6	15.4	18.4	20.5	23.4	26.8	29.8	31.3	33.0	35.2	37.7	39.1
Proportion of OCs lasting 3 months or less	22.8%	16.0%	12.6%	11.6%	10.3 %	9.1%	7.6%	7.2%	7.3%	6.3%	6.0%	6.7%	6.2%
Averageduration of FCs	4.9	6.2	7.6	7.9	8.2	8.9	8.9	9.1	9.1	9.0	9.5	9.4	9.7
Proportion of FCs lasting 3 months or less	51.9%	51.4%	47.1%	47.8%	48.6 %	46.7 %	48.5 %	49.0 %	48.8 %	47.5 %	47.5 %	49.6 %	49.1 %
Average duration of non-contribution (months) in 2 years for OCs	—	1.3	2.0	2.0	2.1	2.0	1.9	2.1	2.0	1.9	1.9	1.7	1.7
Proportion of periods of non-contribution lasting more than 3 months, OCs	—	14.1%	18.9%	19.3%	19.9 %	18.8 %	17.5 %	18.6 %	18.1 %	17.5 %	17.7 %	15.7 %	16.6 %
Average duration of non-contribution (months) in 2 years for FCs	—	3.6	4.9	5.3	5.5	5.3	5.9	6.2	5.9	5.7	5.6	5.8	6.1
Proportion of periods of non-contribution lasting more than 3 months, FCs	—	35.9%	43.9%	45.5%	47.2 %	44.8 %	50.1 %	51.8 %	48.9 %	47.5 %	47.1 %	49.2 %	50.7 %

Source: Authors' calculations based on a random sample from UI administrative data (5 percent of the total). Data for November of each year (sample 1).

Table 4. Development of the UISA system in terms of its benefits

Year	Number of employees who terminate their employment	Number of UI request (total)	Percentage of total UISA benefits requested	Number of ui requests approved	Percentage of requested UISA benefits approved	Percentages of people with benefits who had fixed-term contracts	Percentages of people with benefits who had open-ended contracts	Benefits received that include SF payments: All contracts	Benefits received that include SF payments: Open-ended contracts	Benefits received that include SF payments: Fixed-term contracts	Average Number of payment received	Total Replacement Rate
2003	93747	5613	6.0%	5589	6.0%	80.3%	19.7%	—	—	—	1.0	20.9%
2004	119952	22438	18.7%	21279	17.7%	75.0%	25.0%	3.2%	2.9%	0.9%	1.1	28.9%
2005	138529	32059	23.1%	30689	22.2%	72.7%	27.3%	3.9%	3.4%	1.3%	1.2	30.7%
2006	159293	40577	25.5%	38727	24.3%	70.2%	29.8%	6.1%	5.6%	1.1%	1.3	31.6%
2007	178176	44436	24.9%	42835	24.0%	68.7%	31.3%	6.1%	4.7%	2.5%	1.4	32.2%
2008	191795	48992	25.5%	47168	24.6%	67.6%	32.4%	6.6%	5.3%	2.0%	1.6	34.4%
2009	176240	54456	30.9%	52559	29.8%	64.9%	35.1%	12.5%	10.2%	3.6%	1.9	35.2%
2010	186608	36940	19.8%	35700	19.1%	67.9%	32.1%	16.8%	11.7%	9.7%	1.9	36.9%
2011	206052	51029	24.8%	49455	24.0%	66.8%	33.2%	11.6%	8.7%	4.6%	2.0	37.9%
2012	216522	53396	24.7%	51889	24.0%	67.0%	33.0%	10.9%	8.5%	4.1%	2.0	38.3%
2013	221919	57745	26.0%	55793	25.1%	65.5%	34.5%	11.2%	8.4%	4.0%	2.1	39.1%
2014	220066	62535	28.4%	60534	27.5%	64.2%	35.8%	8.9%	7.1%	3.5%	2.1	40.5%
2015	220421	61684	28.0%	60070	27.3%	62.5%	37.5%	15.3%	11.2%	5.8%	2.2	44.4%

Source: Authors' calculations based on a random sample from UI administrative data (5 percent of the total). Data for formal employees who terminate their employment in a year (sample 2)

Table 5. Coverage of the UISA of formal employees who terminate their employment in a year

	2009	2010	2011	2012	2013	2014	2015
OCswithinsufficientcontributions	12.7	10.6	10.1	9.9	11.4	12.3	14.2
FCswithinsufficientcontributions	35.5	32.8	30.7	31.0	30.5	31.3	36.0
Subtotal	48.2	43.5	40.8	40.9	41.9	43.5	50.1
OCs-Right to Solidarity Fund	18.4	17.7	18.8	18.1	18.8	18.7	17.4
FCs-Right to Solidarity Fund	10.4	13.6	13.3	12.3	11.4	10.3	8.0
OCs-Enough savings, no Solidarity Fund	5.4	5.9	5.9	6.5	6.5	7.1	6.3
FCs-Enough savings, no Solidarity Fund	17.6	19.4	21.2	22.2	21.5	20.4	18.2
Subtotal	51.8	56.5	59.2	59.1	58.2	56.5	49.9
Total	100	100	100	100	100	100	100

Source: Authors' calculations based on a random sample from UI administrative data (5 percent of the total). Data for formal employees who terminate their employment in a year (sample 2). OCs stands for open-ended contracts, and FCs stands for fixed term contracts.

Table 6: The Characteristics of workers with at least one month pause of contribution to UISA in 2015

Variables	Workers with insufficient contributions		Workers entitled to Solidarity Fund Payments		Workers entitled only to Individual Saving Account Payments	
	Open-ended contracts	Fixed-term contracts	Open-ended contracts	Fixed term contracts	Open-ended contracts	Fixed term contracts
Percentage in the sample	14.2%	36.0%	17.4%	8.0%	6.3%	18.2%
Percentage of women	35.9%	33.6%	44.9%	33.9%	36.9%	24.7%
Average age (years)	32.1	31.0	34.3	32.0	38.0	35.2
Education Level						
Non High School	19.2%	28.3%	19.0%	31.0%	15.4%	33.9%
High School	48.1%	40.6%	51.6%	42.4%	41.5%	47.7%
Complete Higher Education Degree	7.9%	4.1%	9.0%	4.5%	19.0%	8.2%
Without information about education level	24.8%	26.9%	20.4%	22.1%	24.1%	10.2%
Average income of formal work before ceasing contributions	409,874	271,755	447,145	278,080	1,003,153	469,426
Average duration of the most recent formal work before ceasing contributions	6.6	3.2	25.0	5.6	39.3	9.2
Average duration of the break in contributions	5.2	5.3	5.7	4.9	5.7	4.2
Economic Sector						
Not specified	0.9%	0.8%	0.7%	0.7%	0.7%	0.8%
Agriculture	3.8%	16.5%	3.4%	14.6%	2.9%	10.8%
Fisheries	0.5%	0.7%	0.7%	0.8%	0.7%	0.6%
Mining	0.8%	0.3%	0.8%	0.4%	2.7%	0.5%
Manufacturing (non-metalic)	5.7%	5.5%	6.9%	4.9%	7.1%	4.0%
Manufacturing (metalic)	3.2%	2.2%	2.7%	1.8%	3.4%	3.0%
Electricity, Gas and Water	0.2%	0.2%	0.2%	0.2%	0.9%	0.4%
Construction	12.9%	24.3%	7.1%	24.5%	9.5%	33.9%
Commerce	16.6%	13.0%	19.3%	11.5%	15.9%	8.7%
Hotels and Restaurants	9.2%	5.1%	6.8%	4.6%	3.8%	2.5%
Transport and Communication	7.9%	4.0%	8.1%	4.3%	7.7%	4.8%
Financial services	3.2%	1.4%	3.8%	1.2%	9.2%	1.6%
Real Estate	21.7%	17.1%	22.1%	17.5%	19.8%	17.6%
Public Administration	3.4%	1.2%	4.6%	1.8%	4.2%	1.9%
Teaching	1.5%	1.6%	2.9%	3.2%	4.3%	3.1%
Healthservices	1.4%	0.6%	2.5%	0.6%	2.2%	0.6%
Otherservices	7.1%	5.6%	7.6%	7.4%	4.9%	5.4%

Source: Authors' calculations based on a random sample from UI administrative data (5 percent of the total).
Data for formal employees who terminate their employment in a year (sample 2)

Table 7: Probit on the probability of using the UI for 2010-2016 (Marginal effects)

	AllSample		Enough Savings + Right to SF		Right to SF	
	Beta	Std. Error	Beta	Std. Error	Beta	Std. Error
Contract (open-ended)	0.106***	(0.008)	0.177***	(0.012)	0.116***	(0.018)
Gender (female)	0.057***	(0.008)	0.04***	(0.011)	0.015	(0.013)
Age	-0.016***	(0.002)	0.003	(0.003)	0.002	(0.004)
Age squared	0***	(0)	0***	(0)	0***	(0)
Education						
Non High School	(Ref)		(Ref)		(Ref)	
High School	0.085***	(0.008)	0.146***	(0.011)	0.151***	(0.015)
Complete HigherEducationDegree	-0.055***	(0.013)	0	(0.017)	0.046*	(0.024)
Withour information about education level	-3.144***	(0.038)	-3.858***	(0.06)	-3.931***	(0.071)
Log of income	0.16***	(0.005)	0.08***	(0.007)	0.074***	(0.011)
Duration of employment	0.004***	(0)	0.001***	(0)	0.001***	(0)
Duration of last pause	0.225***	(0.001)	0.324***	(0.002)	0.327***	(0.002)
Economic Activity						
Not specified	(Ref)		(Ref)		(Ref)	
Agriculture	0.099***	(0.035)	0.036	(0.051)	0.075	(0.069)
Fisheries	0.352***	(0.049)	0.29***	(0.067)	0.291***	(0.09)
Mining	0.016	(0.045)	0.019	(0.06)	0.071	(0.094)
Manufacturing (non-metalic)	0.149***	(0.036)	0.095	(0.051)	0.115	(0.067)
Manufacturing (metalic)	0.111***	(0.039)	0.05	(0.055)	0.05	(0.074)
Electricity, Gas and Water	0.12*	(0.061)	0.053	(0.081)	0.03	(0.117)
Construction	0.227***	(0.034)	0.166***	(0.049)	0.156*	(0.066)
Commerce	0.146***	(0.034)	0.102*	(0.049)	0.107	(0.065)
Hotels and Restaurants	0.137***	(0.037)	0.124*	(0.053)	0.1	(0.068)
Transport and Communication	0.097***	(0.036)	0.071	(0.051)	0.088	(0.067)
Financialservices	0.093*	(0.038)	0.053	(0.053)	0.092	(0.072)
Real State	0.12***	(0.034)	0.092	(0.049)	0.094	(0.065)
PublicAdministration	0.236***	(0.039)	0.057	(0.055)	0.095	(0.072)
Teaching	-0.037	(0.039)	-0.222***	(0.054)	-0.186***	(0.072)
Health services	0.032	(0.044)	0.005	(0.06)	0.034	(0.077)
Other communitary services	0.084*	(0.037)	0.012	(0.052)	0.029	(0.069)
Building management councils	0.103	(0.06)	0.061	(0.087)	-0.026	(0.106)
Extraterritorial organizations	-0.056	(0.215)	0.121	(0.275)	-0.245	(0.482)
Constant	-3.639***	(0.079)	-2.864***	(0.113)	-2.61***	(0.164)
Observations	445410		252053		138134	

Source: Standard error in parenthesis. *** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$. Authors' calculations based on a random sample from UI administrative data (5 percent of the total). Data for formal employees who terminate their employment in a year (sample 2)

DECH-15-473.R1

Unemployment Insurance based on Individual Savings Accounts

(R1 07.12.16; original 02.12.15)

R2: 20th Oct 2017

GENERAL COMMENTS:

- we have rewritten this paper based on an updated version of the unemployment insurance database, which we received since the paper was last reviewed.
 - we have constructed new samples from the database to better analyse the data. Both the samples we have constructed and the new calculations are explained in the text and also in the detailed comments below.
 - we have reinforced the analytical aspects of this paper by including a probit regression that previously was not a part of this paper.
 - In addition, we have addressed the comments of the reviewers from the last revision. We have noted below in CAPS how we have addressed these comments.
-
- we have eliminated the discussion of the Multiruts in the paper as recent conversations we have had with officials from the Ministry of Labour have indicated that the reform undertaken and discussed previously in this paper has not had a significant impact. This means that the job rotation described in this paper is not due to the Multirut phenomenon as the Ministry had previously assumed.

Referees' comments:Referee #1:

I find the revised paper more focused and better substantiated.

I would only encourage the author(s) to refer to the paper that provides evidence about the Chilean system addressing the moral hazard. As the other reviewer says in his/her last remark: "UISA succeeded in avoiding moral hazard. There is an article by Reyes, van Ours, Vodopivec on that topic that is missing in the reference list." Since addressing moral hazard was very much in the forefront of the introduction of the Chilean system, it would make sense to refer to that paper (and not only claim that the Chilean system succeeded in avoiding moral hazard, without providing evidence, on p. 22).

WE HAVE INCLUDED THIS REFERENCE IN OUR DISCUSSION.

Referee #2:

The paper has considerably improved compared to the first version, but still requires further, extensive revisions.

General comments

- The paper has been restructured, and is much more readable now. A numbering of the sections, however, would still help to guide the reader through the study.

WE HAVE STUCK TO THE AUTHOR GUIDELINES STIPULATED BY DEVELOPMENT AND CHANGE, WHICH STIPULATE THE FOLLOWING

Avoid numbered (sub-)headings. *Development and Change* uses the following hierarchy of headings within the text:

HEADING LEVEL A

Heading Level B

Heading Level C

- The fourth section (Empirical evidence) has only one subsection (Coverage of the Chilean UISA) that is identical to the complete section, but no further subsections. Since this section spans over seven pages, a further subdivision would be helpful.

WE HAVE CREATED AN ADDITIONAL SUBSECTION. EACH DISCUSSES A DIFFERENT ASPECT OF THE INSURANCE SYSTEM.

- While the language has improved compared to the first version, the writing would still benefit from a thorough revision with regard to: repetitions, style, coherence of sentences, and typos. Some sentences are written in a rather simple language, are not always easy to understand, and contain small mistakes that should be avoided (see also detailed comments).

WE HAVE ADDRESSED THE DETAILED COMMENTS MADE BELOW AND ALSO TIGHTENED THE TEXT FURTHER TO AVOID REPETITION OF CONTENT.

- While the UISA system in Chile has already undergone two reforms since its inception, I do not see this as a purely negative point. It can also be argued that Chile started with a limited benefits system to avoid implementing a comprehensive, but possibly unsustainable scheme, and expanded it gradually over time via two reforms, closely monitoring the drawbacks. It rather shows that the Chilean government was willing to quickly adapt to the necessary changes.

WE AGREE, AND HAVE MADE THIS POINT CLEAR IN SECTION

- p. 10: how can it be that policymakers had absolutely no idea about the flexibilization of the labour market?

THEY REALLY HAD NO IDEA: We could write a separate paper on the topic of how lack of data on employment conditions has negatively affected policy making in Chile (as well as in many other developing and developed countries). Legislators who designed this insurance

system knew that the Chilean labour market had become more "precarious", but had no hard data with which to estimate the extent to which this was the case. The lack of data created much space for ideological policy prescriptions as the quote from Haagh illustrates. The UI was, in fact, designed, without any reliable information on the types of contracts used, the duration of these contracts or of the characteristics of workers who became unemployed. The official Chilean labour market survey (Encuesta Nacional del Empleo) included questions on the type of contract and on employment duration in 2010. Before then, the Chilean national household survey (Caracterización Socioeconómica de Hogares, CASEN) asked about contracts and duration in 1996. However, the results from this survey show that the survey information and the administrative data are very different. One of the authors of this paper worked in or advised the Ministry of Labour during 2002-4, and witnessed first-hand the shocked reaction of the minister and his cabinet when the first administrative data from the UI came in.

We can include information to this effect in the paper if you think it relevant. For now, we have only expanded the existing footnote as we think that more detail would distract the reader from the central argument in the paper. Also, if the reviewer is interested, the author can provide more information on this point.

- The description of Table 3 on p. 17 is confusing and not clear to the reader. REVISED.

- Table 3 and Table 5 in the appendix are two completely black boxes in the version I received. WE HAVE PROVIDED THE TABLES AS SEPARATE DOCUMENTS BOTH IN WORD AND EXCEL.

- In the introduction the author(s) state that the administrative database is matured (p. 3, para 3), while they state the opposite in the conclusion (p. 21, para 4, last sentence on this page). WE HAVE ELIMINATED THIS PHRASE FROM THE CONCLUSIONS AS WE DO CONSIDER THAT THE DATABASE HAS MATURED SINCE 2009. THIS IS ESPECIALLY THE CASE IN THIS VERSION OF THE PAPER AS IT INCLUDES DATA UP TO 2015.

Methodology and data

Overall a discussion of the methodology is missing, as well as a more detailed description about the data used: SEE COMMENTS BELOW.

- Various interviews have been conducted for this paper, which is a valuable source of information. This approach, however, completely lacks information on how it was conducted: how were the interview partners sampled, how many interviews were conducted, in which format, etc. A description of this qualitative approach is an important part of the paper, but so far completely missing.

THIS PAPER IS NOT BASED ON A SYSTEMATIC QUALITATIVE STUDY. EXPERTS FROM THE MINISTRY OF LABOUR HAVE BEEN CONSULTED AT DIFFERENT STAGES OF THE RESEARCH TO OBTAIN INFORMATION ON THE FUNCTIONING OF THE UI, ITS DATABASE, AND TO CROSS CHECK OUR RESEACH RESULTS. WE HAVE ADDED A NOTE IN THE TEXT TO THIS EFFECT.

- Some interview partners are named (e.g. footnote 15), but other partners remain anonymous (e.g. another influential Chilean labour market analyst, p. 9). A consistent approach is recommended.

WE HAVE PRESERVED THE ANONYMITY OF ALL THE EXPERTS INTERVIEWED FOR THIS PAPER WITH THE EXCEPTION OF THIS FOOTNOTE AS THE QUOTATION COMES FROM HAAGH (2002) WHO CITES THE AUTHOR BY NAME.

- Section 4: some additional description of the administrative data would be beneficial for the paper. WE HAVE INCLUDED THIS DESCRIPTION AT THE BEGINNING OF SECTION 4.

- While the author(s) write that an econometric approach is beyond the scope of the paper, they could still consider a probit model to analyze if certain characteristics are significant in explaining differences. Otherwise conducting tests could also be interesting to know if differences are statistically significant.

WE HAVE NOW INCLUDED A PROBIT MODEL IN THE PAPER THAT PROVIDES THIS ANALYSIS.

Specific comments

- Suggestion to rephrase the title to ‘The Political Economy of Unemployment Insurance based on Individual Savings Accounts: Lessons from Chile for other Developing Countries’.

CORRECTED.

- The author(s) use frequently the word ‘very’ throughout the paper (16x in total) – suggestion to reduce the usage of this word, or replace it with synonyms where appropriate. Also some other words in this line, such as ‘extremely’ should be used with care.

DONE. VERY IS NOW USED 3 TIMES AND EXTREMELY HAS BEEN ELIMINATED.

- Revise how references are cited within the paper, particularly in the footnotes (e.g. footnotes 5, 6, 7 -> years are not in brackets).

WE HAVE REVISED THE CITATION OF REFERENCES IN THE FOOTNOTES.

- p. 2, para 1: last sentence, text in brackets -> people receiving benefits and working informally. WE HAVE ELIMINATED THIS PHRASE TO AVOID REPETITION WITH LATER SECTIONS OF THE PAPER.

- p. 2, para 2: the abbreviation ISA has already been explained in para 1. CORRECTED.

- p. 3, para 2: revise beginning of first sentence. NOT SURE WHAT THIS REFERS TO.

- p. 13, para 1 + 2: there is still inconsistency on how the workers are addressed: see 'his or her ISA' in para 1 versus 'his status' in para 2 -> check with journal requirements. CORRECTED.

- p. 16, para 2 + footnote 25: the author(s) refer to a paper by Sehnbruch and Carranza (2015) that uses a duration model – however, no such duration model can be found there. WE HAVE DELETED THIS FOOTNOTE AS THE PAPER NOW INCLUDES A PROBIT MODEL.

OTHER COMMENTS RAISED BY THE REVIEWER HAVE ALSO BE DEALT WITH IN THE TEXT, OR ARE NO LONGER APPLICABLE TO THE REVISED DOCUMENT.

References

Revise reference comprehensively and for consistency: the style differs from reference to reference.

DONE.