



OECD Economics Department Working Papers No. 1804

Towards better social
protection for more workers
in Latin America:
Challenges and policy
considerations

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<https://dx.doi.org/10.1787/76a04c6f-en>

ECONOMICS DEPARTMENT

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By Jens Matthias Arnold, Aida Caldera Sánchez, Paula Garda, Alberto González Pandiella, Sebastián Nieto Parra

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Authorised for publication by Luiz de Mello, Director, Country Studies Branch, Economics Department

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Abstract

Towards better social protection for more workers in Latin America : Challenges and policy considerations

Informality is a long-standing structural challenge of Latin American labour markets, as almost half of people in the region live in a household that depends solely on informal employment. Informal workers are often insufficiently covered by social protection policies, for which the eligibility is often tied to formal-sector employment. The need to reform social protection systems across Latin America to make them more effective and fiscally sustainable has become more salient after the COVID pandemic. This paper argues that a basic set of social protection benefits available to all workers, whether they work in the formal or the informal sector, should and can be put in place, although it would require the ability to raise additional tax revenues. Moreover, the incentives for formal job creation would be strengthened if its principal source of financing for such basic social protection were shifted towards general tax revenues, as opposed to social security contributions, which tend to increase the cost of formal job creation. Reforming social protection systems will not be easy, but these reforms can provide the basis for both stronger and more inclusive growth in Latin America.

JEL classification codes: I38, J32, J46, O17, O43, O54

Keywords: Latin America, Social Protection, Pensions, Poverty, Productivity, Labour Markets

This Working Paper relates to the 2023 OECD Economic Survey of Costa Rica, to the 2022 OECD Economic Surveys of Chile, Colombia and Mexico and to the 2020 OECD Economic Survey of Brazil.

Résumé

Vers une meilleure protection sociale pour davantage de travailleurs en Amérique latine

L'informalité constitue un défi structurel de longue date pour les marchés du travail latino-américains, puisque près de la moitié des habitants de la région vivent dans un ménage qui dépend uniquement de l'emploi informel. Les travailleurs informels sont souvent insuffisamment couverts par les politiques de protection sociale, dont l'éligibilité est souvent liée à l'emploi dans le secteur formel. La nécessité de réformer les systèmes de protection sociale en Amérique latine pour les rendre plus efficaces et financièrement viables est devenue plus évidente après la pandémie de COVID. Cet article soutient qu'un ensemble de prestations de protection sociale de base accessibles à tous les travailleurs, qu'ils travaillent dans le secteur formel ou informel, devrait et peut être mis en place, même si cela requiert mobiliser des revenus publics additionnels. En outre, les incitations à la création d'emplois formels seraient renforcées si la principale source de financement d'une telle protection sociale de base était réorientée vers les recettes fiscales générales, par opposition aux cotisations de sécurité sociale, qui tendent à augmenter le coût de la création d'emplois formels. La réforme des systèmes de protection sociale ne sera pas facile, mais ces réformes peuvent jeter les bases d'une croissance à la fois plus forte et plus inclusive en Amérique latine.

Classification JEL: I38, J32, J46, O17, O43, O54

Mots Clés: Amérique Latine, Protection Sociale, Pensions, Pauvreté, Productivité, Marchés de Travail.

Ce Document de travail a trait aux l'Études économiques de l'OCDE du Costa Rica 2023, du Chili, de la Colombie et du Mexique 2022 et du Brésil 2020.

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Towards better social protection for more workers in Latin America: Challenges and policy considerations

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¹ Jens Matthias Arnold, Aida Caldera Sánchez, Paula Garda, Alberto González Pandiella are with the OECD Economics Department, Sebastián Nieto Parra is with the OECD Development Centre. The authors wish to thank Elena Vidal, Robert Grundke from the OECD Economics Department, Alexander Kolev, Thomas Manfredi, Nathalia Montoya, René Orozco from the OECD Development Centre, Hervé Boulhol, Herwig Immervoll, Raphaela Hyee, Veerle Miranda, Monika Queisser from the OECD Directorate for Employment, Labour and Social Affairs and Bert Brys and Michael Sicsic of the OECD Centre for Tax Policy and Administration. The opinions expressed and arguments employed in this adaptation are the sole responsibility of the authors and should not be reported as representing the official views of the OECD or of its member countries.

1 Informality and existing social protection policies

Informality is a complex and multifaceted phenomenon that affects many countries in the LAC region. The COVID-19 crisis has further highlighted the significant vulnerability of informal workers and the need to protect them and their dependents. As LAC countries attempt to tackle the vulnerability challenge in the informal economy, they need to take the diversity of informal workers and the context of their households into account. Using the Key Indicators of Informality based on Individuals and their Households (KIbIH) database, this chapter provides an overview of informal workers and their households, selected key social protection programmes adopted in the pandemic, and taxation structures in LAC countries.

Informality is one of the most widespread phenomena in the labour markets of developing countries. It is a structural and multi-dimensional phenomenon, and both the cause and consequence of low-income levels (OECD/ILO, 2019^[1]; OECD, 2023^[2]). Official definitions of informality vary across institutions and countries, but one salient feature applied to define informality for the purpose of this paper is that informal firms and workers often do not pay contributions to social security schemes, such as old-age pensions, health, or unemployment benefits. This paper defines informal employment as every type of worker not contributing to social security schemes.

As social protection benefits are often tied to paying contributions, vulnerable households with informal labour incomes often have little or no social protection mechanism to fall on (Robles, Rubio and Stampini, 2019^[3]; Busso et al., 2020^[4]). The conditions associated with informal work leave informal workers, which typically have lower incomes than formal workers, highly vulnerable to monetary poverty in the face of unemployment or old age, often imply a lack of health care coverage, and the lack of workplace regulations leaves them at higher risk of occupational and safety hazards.

Like in other emerging and developing economies, informality is widespread and persistent in Latin American and Caribbean (LAC) countries. Informality remains part of the daily lives of many workers in the LAC region. Recently, the COVID-19 crisis has further highlighted the great and long-standing vulnerability of informal workers and the urgent need to protect them and their dependents (OECD, forthcoming^[5]; OECD et al., 2021^[6]).

Besides its social consequences, widespread informal employment also implies that many firms remain entirely in the informal sector, which in turn has implications for productivity. Productivity levels of informal economic units, especially of small size, are a major concern in the region (OECD et al., 2023^[7]). Firms employing informal workers often stay small as they try to fly below the radar of tax authorities to avoid taxes, including the higher cost of formal labour, but also regulations (Ulysea, 2020^[8]). A generalised lack of access to credit for informal activities further diminishes their growth prospects. Informal firms typically underinvest into the skills of their workers, given that they are often on less stable contracts and suffer high job turnover. Among low-skill informal employees, only between 44 and 53% remained in their employment status the following year, with most moving into informal self-employment, and less than 10 percent moving into formal salaried jobs (Maurizio and Monsalvo, 2021^[9]). Informality also weighs on the productivity of the formal sector through unfair competition. Informal firms have lower operational costs due to non-compliance with costly regulations and can lower prices further than informal firms, “stealing” market shares from formal firms (Amin and Okou, 2020^[10]). These lower prices dampen the profitability of formal firms, reducing their incentive to scale and restricting access to funds for investment and innovation.

Fully understanding the vulnerability created by informal work can be supported by a granular analysis of the workers’ individual and household composition, including their revenues and social conditions. This working paper analyses informality and its associated vulnerabilities in LAC countries using the OECD Key Indicators of Informality based on Individuals and their Households (KIbIH) database (OECD/ILO, 2019^[1]). It also presents selected key social protection programmes adopted during the pandemic and analyses taxation structures in LAC countries.

1.1. An overview of informality at the household level

Informality can be analysed at the individual or at the household level (OECD/ILO, 2019^[1]). While analysis at the individual level has contributed to understanding the heterogeneity of informal workers in terms of their working conditions and to making useful international comparisons, the informality status of working members within a household may have implications on its dependent members and on gender equality in the labour market (OECD, forthcoming^[5]; OECD et al., 2021^[6]).

Informality has remained persistently high across most LAC countries over the last two decades. While negative economic shocks tend to increase informality levels, the specific features of the COVID-19

pandemic led to mixed results in the evolution of informality rates (Figure 1.1). One key factor was the prevalence of widespread informality in sectors that were heavily affected by lockdown and containment measures, compounded by the limited availability of telework opportunities. Similarly, a substantial number of workers within the informal sector became inactive, implying their exclusion from the labour force. As a result, informality showed different patterns across LAC economies when comparing indicators of the immediate post-COVID-19 period with those of 2019. In Uruguay and Chile, labour formality grew, though for different reasons. In Uruguay, formalisation went along with a decline in total employment, with a larger fall in informality than formality. In Chile, total employment grew, and the process of formalisation occurred because informal job losses were offset by growth in formal jobs. Conversely, in the Dominican Republic, Ecuador and Peru, the labour market tilted towards more informal jobs, mainly because informal employment growth exceeded that for formal employment. Finally, in Argentina, Brazil, Costa Rica, Mexico and Paraguay, the share of informal employment in total employment remained similar to the level of 2019 (OECD et al., 2023^[7]).

Figure 1.1. Distribution of informal workers at the household level, selected LAC economies



Note: Households informality is based on the composition of the working adults in each family. If both are informal workers, household is defined as informal. If one is a formal worker and the other informal, the household is defined as mixed. If both workers are formal, the household is considered completely formal.

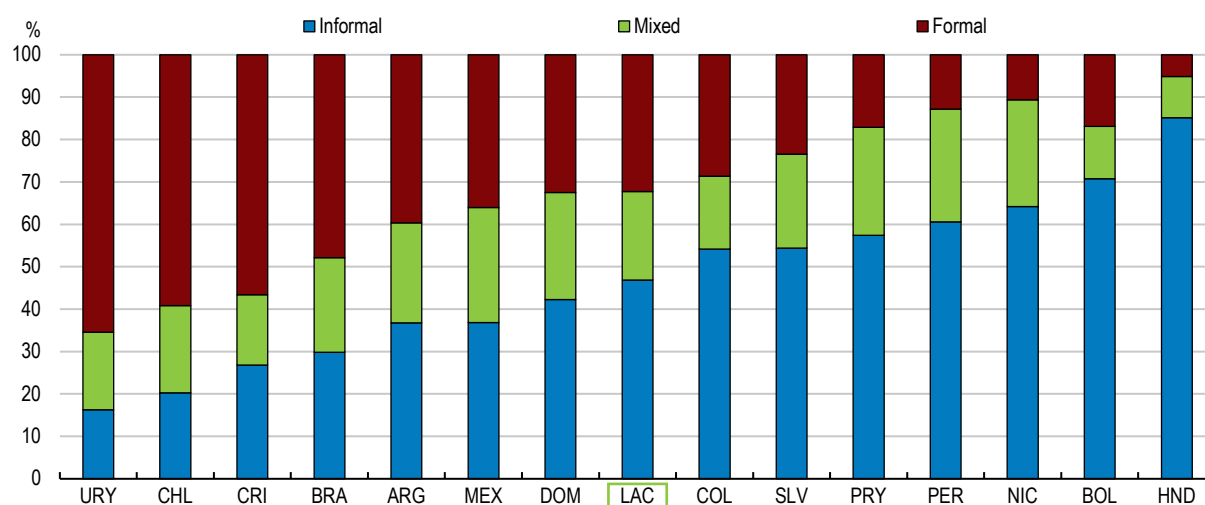
Source: (OECD et al., 2023^[7]) based on the [Key Indicators of Informality based on Individuals and their Household \(KIIBIH\) - OECD](#).

On average, almost half (47%) of people in LAC countries live in a household that depends solely on informal employment (henceforth referred to as informal households), close to 21% live in households with formal and informal workers (mixed households), and the remaining 32% live in completely formal households (formal households) (Figure 1.2). Households sampled for this analysis include only those with at least one working member, representing between 90% and 100% of the households in the 14 countries covered (OECD, forthcoming^[5]).

There are also large disparities across countries as to the distribution of the population according to the degree of household informality. In some countries like Uruguay (65.4%) and Chile (59.2%), a majority of the population lives in formal households. Other countries have a vast majority of people living in informal households. In Nicaragua, Bolivia, Honduras and Peru, more than 60% of the population relies entirely on informal employment. The coverage of social security benefits is often more comprehensive for members of mixed households, compared with completely informal households (OECD, forthcoming^[5]).

Informal workers are disproportionately concentrated in informal households, meaning that other household members are often equally affected by informality. Most Latin American informal workers live and pool resources with other informal workers, whether they are employees, employers, self-employed or contributing family workers. Figure 1.2 shows the distribution of LAC countries' population by the degree of the informality of households. Almost half of informal workers live in a completely informal household, potentially limiting their access to schemes where household members are covered by employment-based social protection schemes of formal workers (OECD, forthcoming^[5]; OECD et al., 2021^[6]).

Figure 1.2. Distribution of population, by the degree of the informality of households, latest year available

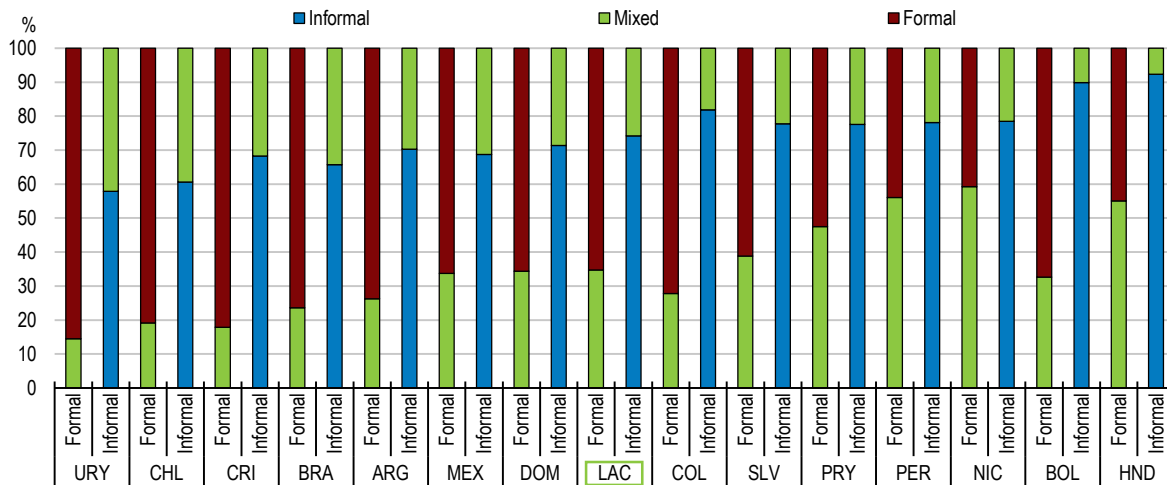


Note: LAC average is an unweighted average. Countries are listed according to the proportion of informal employment in total employment. Each country presents data from its latest year available: 2018 for Argentina, Bolivia, Dominican Republic, Paraguay, and Uruguay; 2019 for Brazil and Peru; 2017 for Chile; 2021 for Colombia and El Salvador; 2020 for Costa Rica and Mexico; and 2014 for Honduras.

Source: OECD (forthcoming^[5]), *Portraying informality and households' vulnerabilities in Latin America*, OECD Publishing, Paris. Based on the [Key Indicators of Informality based on Individuals and their Household \(KIIBIH\) - OECD](#)

Despite the high probability of informal workers belonging to the same household, nearly half of Latin America's formal workers pool resources in households with informal workers. Over 65% of formal workers live in a completely formal household, meaning that almost 35% of formal workers live with informal workers in mixed households (Figure 1.3). In Chile and Uruguay, around 40% of informal workers live in mixed households. In contrast, in Bolivia and Honduras, around 10% of workers in informal employment are part of a household with a formal worker.

Figure 1.3. Distribution of formal and informal workers by the degree of the informality of their households



Note: LAC average is an unweighted average. Countries are listed according to the proportion of informal employment in total employment. Each country presents data from its latest year available: 2018 for Argentina, Bolivia, Dominican Republic, Paraguay, and Uruguay; 2019 for Brazil and Peru; 2017 for Chile; 2021 for Colombia and El Salvador; 2020 for Costa Rica and Mexico; and 2014 for Honduras. Source: OECD (forthcoming^[5]), Portraying informality and households' vulnerabilities in Latin America, OECD Publishing, Paris. Based on the [Key Indicators of Informality based on Individuals and their Household \(KIbIH\) - OECD](#)

1.2. Expanding social protection schemes during the COVID-19 crisis

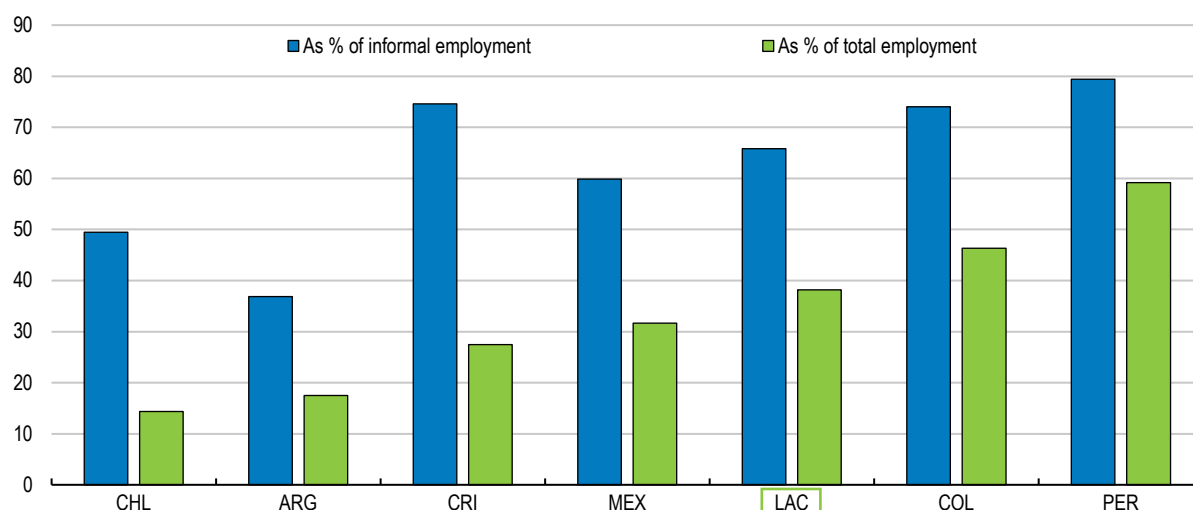
The COVID-19 crisis resulted in massive job losses and millions of households living on informal labour incomes suddenly lost their livelihoods. Many informal jobs were destroyed during the crisis, and unlike in the case of previous economic recessions, the informal economy was not able to provide a buffer against the loss of formal employment. The LAC region lost 26 million jobs due to the COVID-19 pandemic, according to ILO estimates (Maurizio, 2021^[11]). Due to limited employment alternatives and the supply shock caused by containment measurements, many of those job losses represented exit from the labour force, instead of fully translating into increasing unemployment rates. As a result, the LAC region has been the most affected in terms of loss of earnings and worked hours (ILO, 2020^[12]). The negative job and income dynamics exacerbated by the crisis have squeezed the middle class and threaten to deepen existing social and economic gaps. Some 32 million more people than before the crisis now earn a low income, defined as those living in vulnerable, poor and extremely poor households (OECD et al., 2021^[6]).

Almost all contributory social protection regimes in Latin America, which constitute the bulk of overall social spending, are tied to formal employment, thus excluding informal workers (Levy and Cruces, 2021^[13]). Short-time work schemes or other social security elements of the policy response to Covid-19 were therefore inaccessible to informal workers. Weak social protection mechanisms in the region failed to prevent the deep social crisis caused by the pandemic. Owing to the lack of robust social protection mechanisms in LAC, millions of families working in the informal economy experienced a dramatic drop in income during the confinements as LAC countries shut down their economies (OECD, 2020^[14]; OECD, 2021^[15]).

Gradual expansions of social protection programmes since the 2000s have allowed informal workers to access benefit programmes where traditionally they would not have been eligible for any kind of coverage. These reforms across the region have managed to reach some informal workers by unlinking eligibility from formal employment. These programmes are often referred to as non-contributory social assistance programmes (ILO, 2018^[16]; OECD et al., 2021^[6]). Even after these reforms, however, more than 60% of economically vulnerable and informal workers benefit from neither labour-based social protection nor from non-contributory social assistance programmes, such as conditional cash transfers (Figure 1.4).

One of the most immediate responses in LAC countries was to scale up social protection programmes, under the constraint of the limited fiscal space of the governments of the region. This was achieved essentially by: (i) expanding coverage and benefits of existing programmes, (ii) developing new temporary programmes, and (iii) making administrative requirements for claiming benefits simpler and more user-friendly (Figure 1.5) (OECD, forthcoming^[5]; OECD et al., 2021^[6]).

Figure 1.4. Share of workers without social insurance or social assistance coverage



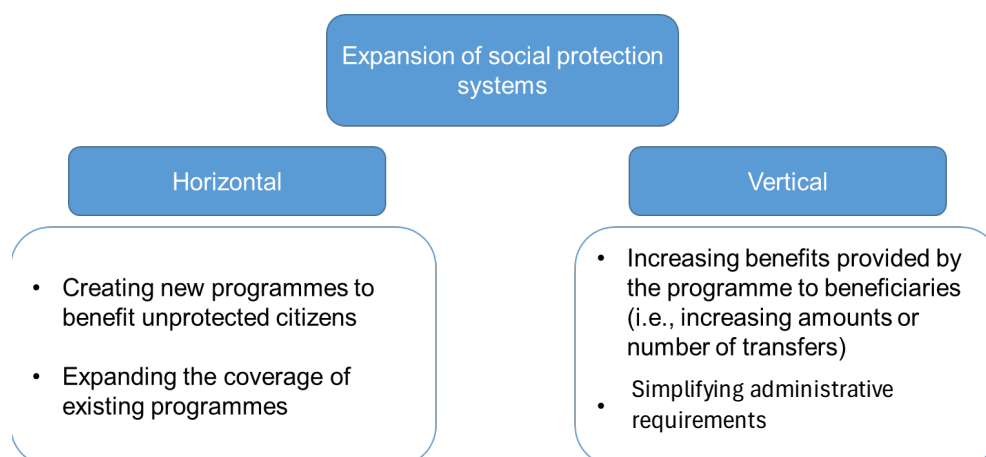
Notes: Regional average is an unweighted average. Informality definition is based on OECD/ILO (2019^[17]). The main social assistance programmes refer only to main CCT programmes and non-contributory social pensions, although the availability of data of beneficiaries in household surveys varies by country, which may result in non-comparable data that the harmonisation process cannot fully solve. In the case of Argentina and Brazil, these percentages are estimated based on social programme targeting conditions. Owing to the systematic approach to producing internationally comparable data and the use of household surveys different from labour force surveys, informality estimates may differ from the estimates presented in other sources, including national statistics.

Source: OECD et al. (2021^[6]) based on household surveys: Argentina: EPH 2018. Brasil: PNAD 2015. Chile: CASEN 2017. Colombia: ENCV 2017. Costa Rica: ENH 2018. Mexico: ENH 2018. Peru: ENH 2018.

Reaching informal workers during the pandemic became a priority among Latin American governments, with many pledging additional cash assistance to the broad sector of informal households by the end of April 2020 (Blofield, Giamb Bruno and Filgueira, 2020^[18]). Reaching these workers, however, was a challenge requiring innovative ideas. Several governments allowed people to self-identify and apply for assistance. In Brazil, more than 50 million people used a smartphone application to apply for an emergency benefit established after the outbreak. In Chile, the programme Ingreso Familiar de Emergencia (IFE) was expanded to include a government-created website, through which individuals could apply to receive a cash transfer. In the case of the Ingreso Solidario programme in Colombia, applications were not even necessary. Recipients for the cash transfer were identified through existing registry databases, cross-referenced with existing beneficiary registries from the largest cash transfers programmes and administrative records from other public entities, making it possible, for the first time, to identify and target low-income and vulnerable households not currently receiving benefits (Gallego et al., 2021^[19]).

New social assistance programmes, included: “*Bono Universal*” in Bolivia, “*Auxilio Emergencial*” in Brazil, “*Ingreso Solidario*” in Colombia, “*Bono Proteger*” in Costa Rica, “*Programmea Pytyvõ*” in Paraguay, as well as, the programmes “*Bono Covid*”, “*Ingreso Familiar de emergencia*” and “*Bono Covid Navidad*” in Chile. All those programmes consisted of measures to support household through cash transfers targeted to unemployed or temporary inactive informal workers and other vulnerable social groups normally not covered by social insurance or social assistance.

Figure 1.5. Types of expansion of social protection systems in LAC countries



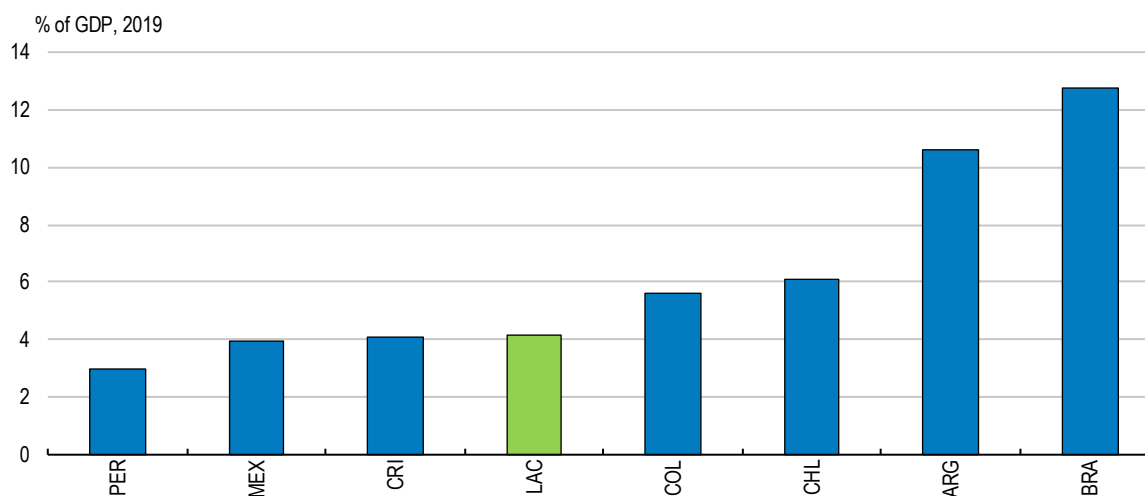
Source: OECD (forthcoming^[5]), Portraying informality and households' vulnerabilities in Latin America, OECD Publishing, Paris.

According to official information, between 1 March 2020 and 31 October 2021, 33 LAC countries adopted 378 non-contributory emergency measures. These include three types: monetary transfers, in-kind transfers and securing and facilitating access to basic services. While most of these measures were put in place in 2020, given the protracted and deep economic and social consequences of the COVID crisis, it has been necessary to extend existing or implement new measures in 2021 (OECD, forthcoming^[5]; OECD et al., 2021^[6]).

Crisis support was also channelled through the increases of transfers within existing social assistance programmes in several countries, such as Argentina and Colombia. In Argentina, the benefit levels of “Asignación Universal por Hijo”, “Asignación por Hijo con Discapacidad” and “Asignación Universal por Embarazo” were increased by 5%. Similarly, in Colombia, the beneficiaries of the “Familias en Acción”, “Jóvenes en Acción” and “Colombia Mayor” programmes were increased to compensate for the effects of quarantines and the difficult economic situation faced by the population (OECD, forthcoming^[5]; OECD et al., 2021^[6]). (OECD, 2020^[20]; OECD, 2022^[21]; OECD, 2022^[22]; OECD, 2023^[23]; OECD, 2022^[24])

1.3. Social spending varies widely across LAC economies

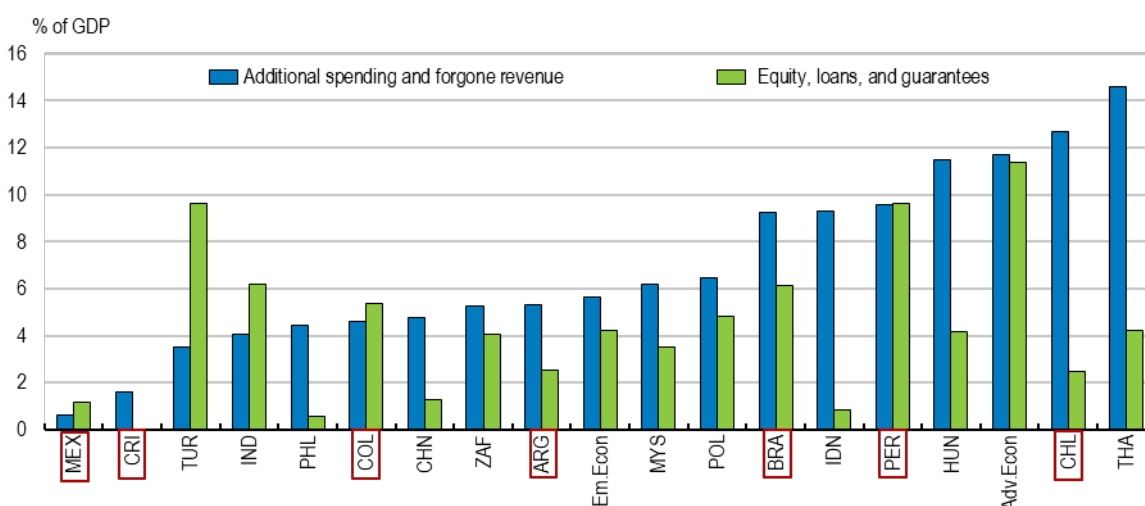
Countries in the region embarked on this generalised expansion of social protection from different starting points. Overall public spending on social protection varies from 4% of GDP in countries like Mexico and Costa Rica, while exceeding 12% of GDP in the case of Brazil (Figure 1.6). For those countries with already larger social safety nets, it was usually easier to build on these as the emergency struck.

Figure 1.6. Public Social Expenditure on social protection, in % of GDP in 2019

Source: CEPALSTAT ECLAC

Note: Official figures on public expenditure by the classifications of the function of government (COFOG) are provided by the respective government institutions in each country expressed in local currency at current prices. GDP at current prices corresponds to a spliced GDP series prepared by the Statistics Division of ECLAC for use in the calculation of fiscal ratios.

Accordingly, the fiscal response to COVID-19 of individual countries in the region was also heterogeneous, but in some of them, it approached or exceeded the size of the policy response of advanced economies (Figure 1.7). Several governments enacted emergency spending in excess of 4% of GDP.

Figure 1.7. The cumulative discretionary fiscal response to Covid-19 has been substantial

Note: Estimates as of September 27, 2021. Em Econ = simple average of emerging economies shown in chart. Adv Econ = simple average of AUS, BEL, CAN, CHE, CZE, DEU, DNK, ESP, FIN, FRA, GBR, ITA, JPN, KOR, NLD, NOR, NZL, SGP, SWE, USA.

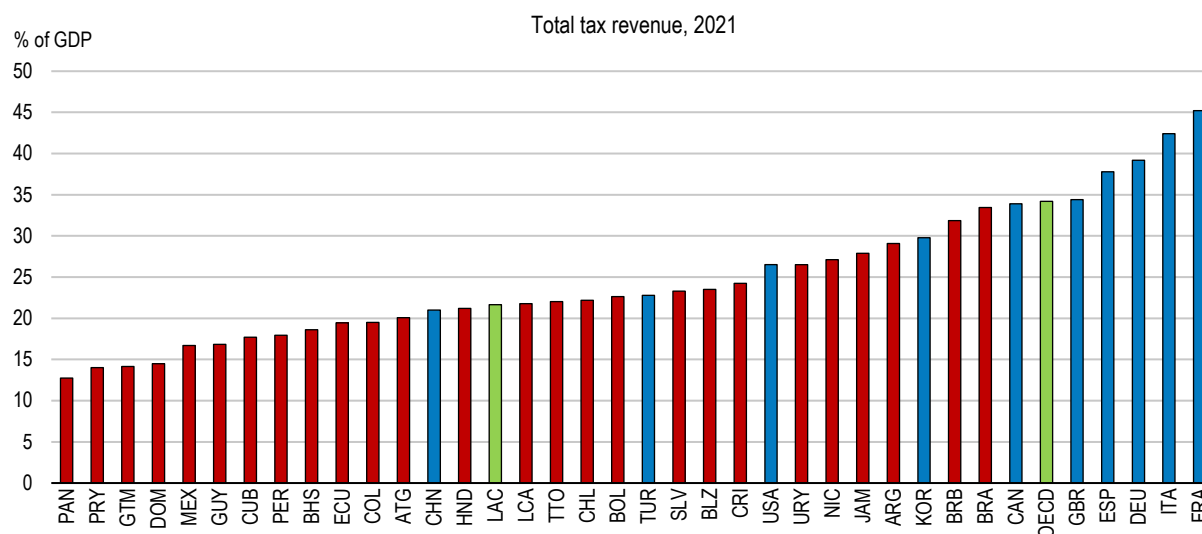
Source: IMF Database of Country Fiscal Measures in Response to the COVID-19 Pandemic, available at <https://www.imf.org/en/Topics/imf-and-covid19/Fiscal-Policies-Database-in-Response-to-COVID-19>

In most of the countries, however, the policy response placed a significant burden on the fiscal accounts, which were already lacking fiscal space or in some cases even experiencing mounting stress prior to the pandemic. For most countries, such high levels of additional public spending were not sustainable, at least not without additional tax revenues, and they have by now scaled back their income support measures to varying degrees.

1.4. Most LAC economies have low tax revenues

Latin American and Caribbean economies are characterised by comparatively low tax revenues, potentially imposing limits on the financing of social protection unless new revenue sources can be mobilised (Figure 1.8). In 2021, the region's average tax revenues represented 21.7% of GDP, compared to 34.2% in OECD economies. However, the region's low average also hides significant heterogeneity, with tax revenues ranging from 12.7% of GDP in Panama to 33.5% in Brazil. All LAC countries in the figure below recorded a tax to GDP ratio below the OECD average of 34.2% of GDP, or 35.7% when excluding Latin American OECD countries (OECD et al., 2023^[25]).

Figure 1.8. Tax-to-GDP ratios in the LAC region, 2021



Note: The figures exclude local government revenues for Argentina (but include provincial revenues). OECD represents the unweighted average of the 38 OECD member countries, including Chile, Colombia, Costa Rica, and Mexico. The LAC average represents the simple average of Panama, Paraguay, Guatemala, the Dominican Republic, Mexico, Guyana, Cuba, Peru, Bahamas, Ecuador, Colombia, Antigua and Barbuda, Honduras, Saint Lucia, Trinidad and Tobago, Chile, Bolivia, El Salvador, Belize, Costa Rica, Uruguay, Nicaragua, Jamaica, Argentina, Barbados and Brazil.

Source: OECD, Global tax revenue database and Revenue Statistics in Latin America and the Caribbean, 2023 (OECD et al., 2023^[25]).

Furthermore, tax structures in the region differ markedly from the average OECD country. LAC countries rely considerably more on taxes on goods and services, which make up just under half of tax revenues on average, compared with around one-third in OECD economies. Corporate income tax revenues are relatively high at 15.4% of total tax revenues in the LAC region, compared with 9.0% in the OECD. By contrast, personal income taxes contributed 9.4% of total tax revenues in the LAC region, compared to 24.1% in the OECD (OECD et al., 2023^[25]). The latter may be related to high participation thresholds, also called basic allowances, in personal income taxes, but also to informality. For example, in Argentina, Chile, Brazil, Costa Rica and Colombia basic allowances for personal income taxes exceed the average wage, so those with incomes in the vicinity of the minimum wage typically quite some distance away from paying personal income taxes. The small base of personal income taxes is one of the factors that limit the potential for progressivity of the overall tax system, as personal income taxes are particularly suitable for progressive tax schedules, which can significantly reduce income inequalities and complement income redistribution achieved through public expenditures.

2 Breaking the vicious circle: Better social protection for more workers

This chapter argues that among the many roots of labour informality, including low access to high-quality education and training and a weak institutional framework and enforcement, the design of the social protection system is a key factor, and one that may deserve more attention than it has received. Labour informality and social protection coverage may be interlinked, and high social contributions can be a key barrier to formal job creation in the region. Reforming social protection systems to ensure some basic social protection coverage for all, regardless of whether they work in the formal or informal sector, while simultaneously reducing the cost of formal employment, has significant potential to reduce labour informality, raise productivity, and decrease poverty and inequality, all of which are long-standing challenges in the region. To do so, basic social protection would need to be financed by general tax revenues, rather than social security contributions. One necessary condition for this to be implemented successfully would therefore be the capacity to either raise additional tax revenues or reduce expenditures in other areas.

The need to build more effective, fiscally sustainable social protection mechanisms that include informal workers and entrepreneurs emerges as one of the main lessons from the COVID-19 crisis. As soon as the health crisis was over, however, many of the extraordinary, non-contributory cash transfers that were effective in reaching informal workers were gradually withdrawn or scaled back, returning to the original situation where only part of the population is covered by social protection. The pandemic was special in that it caused simultaneous job and income losses for millions of people. At the individual level, however, the same phenomenon happens every day to some households, even in the absence of a pandemic. Households will always be exposed to significant risks regarding their livelihoods, and they will need protection against severe shocks, even if not all at the same time.

Building stronger social protection for all could be achieved with a stronger focus on non-contributory social protection benefits. Labour informality is so widespread in Latin America that tying transfer benefits to formal labour market participation, which is the salient characteristic of most social protection benefits across Latin America, may risk leaving behind too many of those in need. At the same time, history has shown that countries will not simply grow their way out of informality, which can be part of a vicious circle (OECD, 2024^[26]). Even those LAC countries with a strong growth trajectory, such as Perú, or those with higher per-capita incomes, such as Argentina and Uruguay, still have significant levels of informality.

This is not to say that past efforts to reduce informality have not borne any fruits and to the extent that they have, they should be continued. Addressing informality will require simultaneous reforms on several fronts (Jessen and Kluve, 2021^[27]) (OECD, 2024^[26]; OECD, 2023^[28]). This certainly includes strengthening institutions and enhancing enforcement, but relying solely on enforcement does not look like a winning strategy given how endemic informality is in Latin America. Too much of a focus on enforcement before addressing other bottlenecks could also worsen unemployment and poverty, as shutting down undeclared activities is not the same as formalising them. Better education and training will also have a role to play in the fight against informality, but the fruits of these improvements will take time to materialise.

There is now a strong case for stepping up efforts to fight informality substantially, and this is where broader social protection reforms may come into play, given how strongly the design of social protection can affect incentives for formal job creation. Redesigning social protection in a way that takes full account of the incentives generated by social contributions has the potential for much more visible progress in formalization, given that these contributions are a core element of the price differential between creating a formal job and an informal job.

2.1. The link between social protection and informal employment

Informality can be related to multiple factors, such as a lack of access to quality education and training, low levels of investment, costly regulations to formalise and grow firms, but also weak enforcement and monitoring of both labour laws and tax policy (Jessen and Kluve, 2021^[27]) (OECD et al., 2023^[29]) (Box 2.1). Beyond these, another potentially relevant factor that has received relatively less attention in policy discussions, and the one that this chapter attempts to highlight, is the significant cost difference between creating formal and informal jobs (Box 2.1) (OECD/IDB/CIAT, 2016^[30]). Given the low levels of labour productivity in the region, one of the main impediments to formal job creation could be the relatively high mandatory social contributions and other payroll taxes that finance formal sector social protection and that reduce incentives for firms to hire workers formally (IMF, 2021^[31]; Meléndez, Alvarado and Pantoja, 2021^[32]; Levy and Cruces, 2021^[13]; Loayza, 2018^[33]). As an illustration, in Latin America, on average, minimum wages plus contributions for pensions, health insurance and unemployment insurance amount to 36% of GDP per worker, compared to 22% of GDP per worker in OECD countries (Ripani et al., 2023^[34]). Because regulations are imperfectly enforced, firms effectively have the possibility to evade the costs of social insurance and hire salaried workers informally, and they regularly do.

Box 2.1. Literature on the possible causes of labour informality in Latin America

A significant amount of attention has been given in the literature to the question of why informality persists in Latin America, and in developing economies more widely (La Porta and Shleifer, 2014^[35]; Perry et al., 2007^[36]). There are three main theories, although given the complexity of informality, this is not meant to be an exhaustive list of potential explanations. The first is that the cost of formalisation is too high, leading firms and workers to choose to operate informally (Meléndez, Alvarado and Pantoja, 2021^[32]). The cost of formalisation for firms includes adhering to relevant policies, such as minimum wage regulations and mandatory pension contributions. The cost of formalization for individual workers includes mandatory contributions to social protection schemes, and for the self-employed, administrative fees and taxes, business regulations, and administrative requirements such as book-keeping.

A second theory explains informality as a survival strategy. In this view, informality is not seen as a choice over what type of work, formal or informal, but a choice between working and being unemployed (Acevedo et al., 2021^[37]). The data suggests that this theory is particularly true for informal employees, who make up about 33.1 percent of informal workers in Latin America, and who express a preference to work as formal salaried employees or to be self-employed, but do not have access to such jobs (ILO, 2018^[38]). The lack of access to formal jobs may be due to a lack of employment opportunities in formal firms or a lack of the educational level necessary for a formal job. Indeed, transitions from the informal to the formal sector are most pronounced for higher-skill, higher-educated informal wage employees, only about one third of whom maintain their work status from year to year, and most of whom move into the formal sector (Ulyssea, 2020^[8]). Transitions from the formal to the informal sector are more pronounced among young people, women, and low-skill workers, who make up most of the informal workforce, and who, at any one time, face a higher probability of transitioning to informal employment than other populations. This theory, however, is fully compatible with the first explanation based on the cost of formalization. Workers who do not manage to get a foothold in the formal sector may simply have a productivity level below the cost of formal employment, for example due to their education level, or firms that use an informal workforce may not be able to achieve the productivity level necessary to bear the cost of formality.

The third and final theory posits that informal workers and firms may be able to formalise, but choose not to because the costs outweigh the benefits of formalisation. In other words, workers and firms may be productive enough to survive in the formal sector but choose not to, to benefit from a cost advantage over formal firms or to benefit from non-contributory social protection policies which may be better than social protection received through formal work. There is some evidence to support this theory in specific circumstances. The Universal Child Allowance program in Argentina, for example, was found to strongly disincentivize the labor market formalization of beneficiaries (Garganta and Gasparini, 2015^[39]). The possibility of voluntary informality points to the importance of designing strong incentives for moving into the formal sector, for example by ensuring that the additional cost of going formal is lower than the additional benefits of doing so.

In summary, many structural factors play a role in shaping labour informality, including people's educational level and opportunities, tax and business regulations, and labor market regulations, including social security contributions, hiring and firing costs or minimum wage policies. Transportation and housing policies may also play a role in the cost-benefit analysis of workers and firms when deciding whether to participate in the informal or the formal sector.

The design of social protection (Box 2.2) in the region has led to an outcome that may be problematic from several perspectives. First, the lack of a formal work contract precludes many poor and vulnerable households from social protection instruments whose eligibility depends on having a formal job. As an example, even in countries with lower rates of labour informality such as Uruguay or Chile, the percentage of workers in the lowest income quintile who pay pension contributions is less than 50%. Second, the relatively high social security contributions that finance contributory social protection may actually exclude many workers from the formal labour market because of the substantial cost difference between formal and informal jobs.

Box 2.2. The design of social protection systems in Latin America

Social protection systems across the LAC region are complex, spanning multiple objectives and are generally fragmented into two parallel systems: contributory benefits, and non-contributory benefits. Many countries add to this labour market regulations such as mandatory severance payments to laid-off workers and minimum wage rules, which are typically binding only for formal-sector workers (Machinea and Uthoff, 2007^[40]).

Contributory social protection systems vary from country to country but share some common features typically including contributory pension schemes such as old-age, disability, and survivor's pensions, as well as health and unemployment insurance, and maternity or sick leave. They are financed social security contributions from employers and/or employees. Rates of employer and employee contributions vary significantly across the region, with the highest rates of employee contributions in Chile at 20.6% in 2018, and of employer contributions in Argentina, at 30% (Leyva and Urrutia, 2020^[41]).

Non-contributory social protection, by contrast, is generally not financed from individual contributions, but from general tax revenues. Starting in the 1990's, Latin American economies began investing in and expanding the coverage of non-contributory social protection, including non-contributory pensions and conditional cash transfers. While the benefit levels and the coverage of the target population often remain low in most countries, non-contributory social protection benefits have further reduced the incentives for seeking formal employment, by reducing the gap between the benefits available to formal and informal workers. For example, evidence from Colombia suggests that the introduction of non-contributory healthcare benefits for informal workers that are almost equal to those of the contributory healthcare scheme was followed by increases in informality (Camacho, Conover and Hoyos, 2014^[42]).

Reforming social protection systems may have the potential to help reducing informal employment in Latin America, as part of a comprehensive package of reforms that should include better enforcement, simpler labour regulations, and more investment in human capital. LAC countries differ substantially in their level of development and the social protection systems so the reforms to be implemented will vary from country to country. But to overcome the main weaknesses of the current setup a better social protection system could pay closer attention to two basic ideas:

1) A basic set of social protection benefits should be made available to all workers, making no distinction between formal and informal workers. The basic set would cover basic needs, such as a minimum pension and/or access to basic health services.

2) The financing of basic social protection should minimise disincentives to formal job creation, particularly in the lower income ranges predominantly affected by informality. One way to minimise such disincentives would be to reduce social security contributions in the lower income ranges, for example around the entry-level wage in the formal sector. Such a reform would, of course, only be possible if countries can rely more on general tax revenues for financing basic social protection. More comprehensive benefit packages could be available for those willing and able to pay additional contributions.

2.2. A proposal for a re-design of pension systems to fight old -age poverty and reduce informality

Looking ahead, pension systems will become increasingly relevant in the context of population ageing. In 2022, the Latin American and Caribbean region was home to 88.6 million people over the age of 60, representing 13.4% of the total population. This figure will reach 16.5% in 2030 (CEPAL, 2022). Life expectancy for both sexes has also risen, from 48.6 years in 1950 to 75.1 years in 2019. The increase in the proportion of older people and the lengthening of the life cycle present opportunities but will also place demands on pension systems in the region.

Old-age pensions are meant to provide a regular income stream to those who are no longer in working age. Pension systems serve essentially two purposes: to prevent old-age poverty, and to allow some degree of consumption smoothing, allowing the elderly to maintain similar material living standards before and after they retire. Old-age pensions are a driving factor behind differences in the incidence of old-age poverty in Latin America (Gasparini et al., 2010^[43]). Where pension coverage is extensive, such as Argentina, Brazil, and Chile, old-age poverty rates are often lower than poverty rates for the general population, while the opposite is true in Colombia and Mexico. Extreme poverty in old age was around 1% in Brazil and Chile, 11% in Mexico and 16% in Colombia (SIMS, 2021).

While some countries in the region have achieved almost universal pension coverage among the elderly, pension coverage remains low in many others despite several efforts to increase coverage over the last decade (Table 2.1). In Latin America, only 6 out of 10 elderly adults aged 65 and above had a contributory and/or a non-contributory pension in 2019. Focusing only on contributory pensions, the average coverage was only 38%, ranging from around 21% in Peru to 87% in Chile (ILO, 2020^[44]). Coverage tends to be lower for women, rural workers, workers in small firms, and workers with low incomes and levels of education. This difference is largely driven by the high levels of informality among those groups. Despite progress in female labour force participation in recent years, the percentage of women who have access to a contributory pension (36%) is considerably lower than that of men (44%) in Latin America. While Costa Rica, Peru and Mexico are among the countries with the largest coverage gaps between women and men, with differences in the range of 15-25 percentage points, other countries such as Argentina, Uruguay and Chile have smaller gaps or even better coverage for women. In addition to the coverage gaps, there are also differences in the levels of pension benefits. Despite considerable progress in recent years, effective replacement rates of women tended to be around 20 percentage points lower over 2016-2020.

Table 2.1. Pension coverage for those aged 65+ in Latin America, 2020-22

| Share of population aged 65+: | Covered by contributory pension | Covered by any pension |
|-------------------------------|---------------------------------|------------------------|
| Argentina | 79.0 | 79.0 |
| Brazil | 81.3 | 86.3 |
| Chile | 87.3 | 87.3 |
| Colombia | 27.7 | 56.8 |
| Costa Rica | 50.6 | 69.0 |
| Mexico | 32.2 | 72.3 |
| Peru | 21.4 | 45.0 |

Note: Data refer to 2022 for Argentina, Brazil, Costa Rica and Peru, 2021 for Colombia, 2020 for Chile and Mexico.

Sources: IDB SIMS database, available at <https://www.iadb.org/en/sector/social-investment/sims/sims-institutions>.

Recognising the generally insufficient pension coverage by contributory schemes, many countries in the region have introduced non-contributory pension schemes over the last two decades (de la Torre and Rudolph, 2018^[45]). More than a dozen Latin American countries now have some form of non-contributory

pension, including Mexico, Colombia, Peru, Chile, Costa Rica, Brazil, and Argentina. Many of these are limited to old-age pensions, but some countries like Brazil also provide non-contributory disability pensions. Still, usually these non-contributory pensions are not integrated into the pension system and are part of social assistance policies. Their benefit levels range from a fraction of the extreme poverty line in Colombia to a full minimum wage in Brazil.

Countries have followed different strategies. One strategy has been to provide universal access to non-contributory pensions, regardless of whether someone also benefits from a contributory pension, as in Chile, Bolivia, Mexico and Trinidad and Tobago. A second strategy has been to expand the contributory system towards those who were not part of it, such as certain self-employed or domestic workers, by making it mandatory to contribute to the system. This choice was more common in countries that had stronger contributory pension systems and higher rates of contributory pension coverage to start with, like Argentina, Brazil, Chile, Panama, and Uruguay (Rofman, Apella and Vezza, 2015^[46]). A third strategy has been to target older adults who are living in poverty with separate non-contributory programmes, with selection based on some means proxy test. This has often happened in countries with higher informality and lower rates of contributory pension coverage, including Colombia, Costa Rica, Ecuador, El Salvador, Panama, Paraguay, and Peru (Rofman, Apella and Vezza, 2015^[46]).

The way forward: A multi pillar pension system

A pension system with at least two, possibly three, complementary and well-integrated pillars would be able to achieve universal coverage while delivering adequate pension benefit levels and minimising disincentives for formal job creation:

A first non-contributory basic pillar: Preventing old-age poverty could be achieved through a universal basic pension benefiting the entire elderly population, aiming at a full coverage of those aged 65+, regardless of individual work histories in the formal and informal sectors. This basic benefit could be largely financed through general taxation, so that it would not raise the cost of formal job creation during working lives. For those earning close to the formal-sector entry wage, typically the full-time minimum wage in countries with minimum wage regulations, this would be the only mandatory pension system covering them. As a result, contributions could be very low, potentially starting near zero, given that the main focus in this income range is to avoid disincentives for formal work. One way to lower fiscal costs would be to exclude very high-income individuals from receiving the non-contributory pension, as for example in Chile (OECD/IDB/The World Bank, 2014^[47]).

Determining the generosity of the basic pension should consider several factors. In principle, given that the overarching aim of the basic pillar would be to fight old-age poverty, the minimum benefit could be at the level of a well-defined poverty line. In practice, a country's fiscal space and the scope for raising additional tax revenues, rationalising, or reprioritising expenditures are key factors to take into consideration when defining the level of this minimum pension benefit.

As finding the necessary resources may be a gradual process, the basic pension could in some cases start initially at a low level, such as the extreme poverty line that some countries in the region define as the income required to buy the necessary food for survival. In some countries, such a minimum benefit would already be an important step forward. For example, Colombia's non-contributory pension scheme *Colombia Mayor*, currently pays out benefits that amount to only a fraction of the extreme poverty line. But there could also be good political arguments for going beyond the poverty line if it is considered that living with an income at the level of the poverty line is inappropriate for the elderly, most of which will have worked their entire lives. A basic universal non-contributory pension benefit set at the level of the poverty line could often be sufficient not only to protect these workers from old-age poverty, but also to provide a sufficient replacement rate and ensure an adequate degree of consumption smoothing, given the distance between the poverty line and the minimum wage in many countries in the region.

Such a universal basic pension would also help to close gender gaps in social protection coverage (Tuesta and Bhardwaj, 2023^[48]). As women typically have a lower rate of labour force participation in Latin America, they are also less likely to access contributory pensions.

A second, contributory pillar would complement the basic pension for those with higher incomes, to achieve pension benefit levels that not only prevent old-age poverty, but are also a decent replacement for working-age incomes. The contributory and non-contributory pillars should be seamlessly integrated within the pension system to achieve the desired replacement rates for everyone in an effective way.

For higher-income earners, contributions could rise gradually with wages, avoiding discontinuities that could create incentives for reporting a lower than actual income. The schedule of contributions could be guided by the following considerations: If contributions become too high too early, this may create incentives against formal job creation. If the contributions only start rising at high wage levels, the resulting replacement rates will be low and hence provide too little consumption smoothing.

The contributory pillar could be organised in different ways. First, as a pay-as-you-go system where current contributions finance the benefits of current pensioners. Second, as a funded scheme, where individual contributions are channelled to individual accounts to finance future pension benefits for the contributor. Third, as notional accounts where the system tracks contributions and applies a formula to determine the pension entitlement based on the worker's career earnings and the notional account balance.

The contributory pillar could in principle be administered by either private or by public entities. OECD countries have taken different avenues with success (Box 2.3), and there is no single set-up that would be inherently preferable to others.

A third pillar of voluntary individual savings could complement the basic and contributory pillar. In OECD countries, voluntary savings improve on average replacement rates by 25 percentage points for the mid-income worker (OECD, 2023^[49]). In ten OECD countries, private voluntary schemes cover more than 40% of the economically active population and occupational pension plans are playing an important role providing coverage and adequacy for retirement. Automatic enrolment to these types of schemes has been effective in increasing the take-up in countries such as the United States, United Kingdom, New Zealand and Turkey.

A key aspect for the feasibility of this multi-pillar proposal is how to finance it. Most countries in the region will need to carry out tax and spending reforms to ensure its fiscal sustainability in the short and long run and should be confident that they can achieve this before considering this proposal. Reforms should only proceed as financing to the extent that adequate financing sources can be identified. Financially unsustainable pension systems have substantial negative consequences both for future pensioners, who fear for their pension, and for fiscal accounts, as countries may face higher borrowing costs to the extent that concerns about fiscal sustainability grow among investors.

The resources dedicated to the universal pension could be seen as an investment. As this spending reduces the cost of formal employment, especially for low-income workers, it could boost formality, productivity and potentially even future tax collection.

Box 2.3. Funded defined-contribution pension systems in selected OECD countries

OECD countries have different arrangements in the management of funded defined-contribution schemes with private and/or public institutions involved. There is not one single model for success in their design. Some examples taken from recent OECD Economic Surveys include the following countries:

Australia

The Australian pension system has three components: a means-tested non-contributory component (“Age Pension”) that reaches 75% of the elderly; a superannuation guarantee with a compulsory employer contribution to private superannuation savings; and a voluntary superannuation contributions and other private savings (OECD, 2020_[50]). The Age Pension is designed to provide a safety net for those unable to save enough through their working life and to supplement the retirement savings of others. The Superannuation system, a defined contribution scheme, is not subject to financial sustainability issues and as the system reaches full maturity, fewer individuals will be reliant on the Age Pension safety-net.

Denmark

The Danish pension system rests on the public pension, which consists of a basic pension and a means-tested pension supplement that is paid to the financially most disadvantaged pensioners, in addition to a mandatory occupational pension scheme based on lump-sum defined contributions called ATP and quasi-mandatory occupational pension plans. ATP is as a public pension provider, investor and administrator of welfare benefits. It is one of Europe’s largest pension funds with 5.4 million members and pension assets exceeding USD 882 bn (229% of GDP). In addition, quasi-mandatory occupational pension schemes negotiated as part of collective agreements cover about 90% of the employed work force. The public pension and ATP ensure that all pensioners, regardless of labour market attachment, will have an adequate basic income. Occupational pension schemes ensure that a person’s income in retirement will not be markedly lower than the income earned during working life.

Sweden

The Swedish pension system consists mainly of public schemes and quasi-mandatory occupational plans (OECD, 2020_[50]). Mandatory public earning-related pensions include both a notional defined contribution scheme and a funded defined contribution scheme. Both cover earnings up to roughly the average wage. On top of these schemes, quasi mandatory occupational pension plans negotiated by social partners in collective agreements cover around 90% of workers. A residence based basic pension (guaranteed pension) ensures a minimum level of pensions at 21% of gross earnings.

2.3. Working-age transfers

In Latin America, the larger part of income support for those in working age is distributed through so-called contributory “social insurance” schemes (Gragnotati et al., 2015^[51]). Just as in the case of contributory pensions, access to this support is typically tied to contributions levied on formal workers’ wages. All 18 countries in Latin America provide sickness insurance and workplace accident benefits to formal workers and several countries in the region also provide unemployment benefits (Blofield, Giamb Bruno and Filgueira, 2020^[18]). In some cases, expecting mothers or families with children also receive income support. An overview of the main benefits provided by cash transfer programmes in seven countries in the region can be found in (Table 2.2).

These contributory schemes often cover only part of the working population due to informality. Even among those who do pay contributions, gaps between legal and effective coverage have emerged and some beneficiaries who fulfil the eligibility criteria specified by law do not receive the benefits or do not take them up (Table 2.2). There could be many reasons for this, including weak programme implementation structures, difficulties in accessing benefits or low take-up, which in turn may have many reasons (ILO, 2020^[44]).

Table 2.2. Legal and Effective Coverage of Social Protection Systems

| Type of benefit | Unemployment | | Work Injury | | Maternity | | Children/Family | |
|-----------------|--------------|-----------|-------------|-----------|-----------|-----------|-----------------|-----------|
| | Legal | Effective | Legal | Effective | Legal | Effective | Legal | Effective |
| Argentina | 28.8 | 10.8 | 41.1 | 47.4 | 34.9 | 31.7 | 102.4 | 79.6 |
| Brazil | 48.7 | 17.6 | 37.8 | 48.7 | 56.2 | 47.8 | 100 | 67.7 |
| Chile | 42.5 | 27 | 58.2 | 68.7 | 47.8 | 46.6 | 68.9 | 68.5 |
| Colombia | 62.1 | 4.6 | 62.1 | 37.7 | 25.6 | | 100 | 36 |
| Costa Rica | 41 | | 54.8 | 58.1 | 41 | 23.4 | 26.4 | 38.8 |
| Mexico | 0 | 6 | 70.3 | 35.4 | 37.2 | 10.4 | 96.8 | 23.4 |
| Peru | 75.1 | | 75.1 | 7.4 | 27.3 | 8.8 | 18.8 | 16.1 |

Note: Legal coverage refers to the percentage of working age population with a right to be covered by a specific benefit. Effective coverage refers to the ratio of recipients of unemployment cash benefits to the number of unemployed persons (for unemployment benefits); the ratio of women receiving maternity cash benefits to women giving birth in the same year (for maternity benefits); the ratio of children/households receiving child/family cash benefits to the total number of children/households with children (for child benefits).

Sources: ILO, World Social Protection Database, based on SSI; ISSA/SSA, Social Security Programmes Throughout the World; ILOSTAT, ECLAC, IMF, WHO, WB, UNDP, UNICEF, completed with national data sources.

These shortcomings in the implementation of contributory income support programmes in Latin America have led many LAC countries to introduce means-tested, non-contributory cash transfer programmes in the 2000’s, often referred to as social assistance programmes. These programmes are typically financed by general tax revenues, with the explicit objective of alleviating poverty among households that are unable to generate a minimum income on their own. As with contributory benefits, the characteristics of non-contributory programmes vary significantly across countries.

In many cases, these benefits have combined means-tested income transfers with measures aimed at lifting families out of poverty over the longer run by encouraging investments into their children through conditionalities attached to benefit disbursement. These are meant to encourage school attendance and medical check-ups for children and expecting mothers, for example. These conditional cash transfers (CCTs), are perhaps the most prominent element of non-contributory social benefits in Latin America, despite their limited size. But not all of the non-contributory benefits have conditionalities attached, and means-testing is sometimes done on the basis of proxy measures, such as the place of residence.

It should be said clearly that the definitions often used in the discussion on social protection in Latin America, and that this paper follows, may at times diverge from the definition used by the OECD in the

discussion of OECD member economies. In the OECD context, social assistance generally refers to unconditional transfers, beyond the means-testing, while in many Latin American economies, social assistance cash transfers often do have conditionalities attached. Even if the intention to provide transfers may have been the dominant motivation for policy makers, the general experience with conditionalities in Latin America is positive and not including them may have seemed like a lost opportunity.

Non-contributory cash transfer programmes were initially launched at the local level in Brazil, while the first systematic rollout at the national level took place in Mexico in 1997, with the Programme for Education, Health, and Nutrition (Progresa), formerly known as Progresa and Oportunidades (Cecchini and Madariaga, 2011^[52]). Chile established its Chile Solidario programme in 2002. In 2003, Brazil followed suit with the nationwide rollout of the Bolsa Família programme, temporarily rebaptised to Auxílio Brasil between 2020 and 2022. These programmes have both become well-known and highly regarded programmes, whose multifaceted success has motivated the proliferation of similar programmes around the world. By 2015, every country in Latin America had a CCT programme modelled after Progresa and Bolsa Familia (Fiszbein et al., 2009^[53]), and by 2019, there were more than 30 active CCT programmes in place in the region (Abramo, Cecchini and Morales, 2019^[54]). Several countries have more than one such programme, and this fragmentation can easily lead to overlaps and inefficiencies.

A large body of evidence suggests that such cash transfers have contributed to significant reductions in poverty (Soares, Ribas and Osório, 2010^[55]; Sewall, 2008^[56]; Stampini and Tornarolli, 2012^[57]; Robles, Rubio and Stampini, 2019^[3]; Millán et al., 2019^[58]). These cash transfers can also bring more long-term benefits for society, such as promoting credit access, better eating habits, better school attendance, better academic results, better cognitive development, reduction of domestic violence, and female economic empowerment (Banerjee, Niehaus and Suri, 2019^[59]). A comparative study of CCTs has shown that they are typically more effective when paired with other measures designed to improve productive inclusion and employment, and in particular, when those other measures help integrate informal workers into the formal economy (Papadopoulos and Leyer, 2016^[60]). This suggests that programme structure and context make a significant difference for programme success. At the same time, CCTs have been criticised for having negative effects in reinforcing the gendered distribution of unpaid work (and – consequently – women’s ability to participate in paid labour markets) as traditionally mothers are the ones responsible for ensuring that conditions like children’s schooling and healthcare are met (UN Women, 2019^[61]).

Spending on non-contributory cash transfers and trends in spending vary significantly across countries, but are generally far lower than spending on formal-sector social insurance. The Bolsa Familia programme represented 0.5% of GDP in 2019 and covered a quarter of the total Brazilian population, although it has been expanded since (OECD, 2020^[20]). Progresa represented 0.35% of Mexican GDP and covered almost a quarter of the population in 2018. Ecuador was the biggest spender on CCTs at 1 % of GDP, while Chile was the lowest at 0.14% of GDP, just under half of the regional average of 0.32% of GDP (ECLAC, 2022^[62]).

The evidence on the impact of cash transfers on the incentives for labour participation and formal employment is mixed (Baird, McKenzie and Özler, 2018^[63]; Skoufias and Di Maro, 2008^[64]). While some evidence suggests that cash transfers do not discourage - and in some cases even encourage - labour participation by beneficiaries (Banerjee et al., 2017^[65]), other evidence from the region suggests that transfers can decrease incentives to participate in formal employment (Bergolo and Cruces, 2021^[66]). This is often related to design weaknesses in the programmes. For example, abrupt benefit withdrawals for beneficiaries who find a job or earn more can imply high implicit tax rates for workers who lose the transfer if they earn additional income that lifts them above the eligibility threshold stipulated in the targeting mechanism. That said, it is important that cash transfers maintain strong incentives that encourage those who can generate their own income to do so. The need for strong work incentives will put limits on benefit levels for those in working age, in contrast to the elderly for whom maintaining work incentives are usually not a policy objective.

The way forward: A single cash transfer for the poor

Latin America's successful experiences with non-contributory cash transfer schemes provide a unique opportunity to build on them to strengthen social protection. Where fragmented benefit systems create unnecessary complexity and scope for benefit duplication, unifying and integrating existing cash transfers into a single national programme would be a first useful step, but that may still fall short of providing universal access to such transfers.

Applying the idea of making social protection benefits available to all those who need them as outlined at the beginning of this section would imply getting rid of any eligibility restrictions that are not related to means-testing, i.e. extending eligibility for conditional cash transfers to the entire population. This does not mean that everyone would receive benefits, but those that qualify for them due to their low earned incomes or other qualifying conditions should be able to receive benefits without undue delays.

That is far from being the case at present. Many countries focus on specific regions within the country or within urban areas for benefit eligibility on the grounds that poverty is concentrated there. In Colombia, for example, a household has to be specifically chosen to qualify for the conditional cash transfer programme *Familias en Acción*, and low income alone is no guarantee for eligibility. Another example is Peru, where the conditional cash transfer programme, *Juntos*, is targeted to rural areas. In most cases, these mechanisms are designed as some way to allocate resources that are insufficient to cover the entire population that meets the income-threshold criteria.

Universality also implies the possibility of rapid enrolment when a household loses a vital income source. Long waiting lines for programme enrolment, as have occurred in Brazil's *Bolsa Família* programme in the past, for example, impede CCT programmes to fulfil their potential role of earnings replacement. If properly designed and implemented, CCTs could provide a backstop for those losing their job or income and could serve as a very rudimentary, non-contributory universal pillar of an unemployment benefit system for those who cannot access more formal unemployment insurance. In several countries, however, enrolment processes are in practice either too much top-down, leaving little scope for needy households to apply for help, or too slow to support people in the face of sudden income losses. An important first step would therefore be to make cash transfer programmes more agile, so that they can disburse quickly when people lose their livelihoods, following the examples of the UK's Universal Credit or Malaysia's BSH cash transfer programme.

One option for designing a single cash transfer for the poor would be to extend current non-contributory benefits to all those who pass the relevant means test, effectively turning non-contributory benefits into a guaranteed-minimum-income benefit scheme for the population aged below 65. This would be a periodic cash transfer to supplement the income received by poor households to reach a certain minimum income level.

Financed from general taxation revenues, such a scheme could build on existing conditional and unconditional cash transfers for the vulnerable and poor. The amount given to each household could consist of fixed and variable elements depending on household characteristics, as in Brazil's *Bolsa Família* programme. Such a benefit is different from a Universal Basic Income, which grants an identical amount to every citizen, regardless of income (Box 2.4).

Applying some mild conditionalities to a guaranteed minimum income scheme has proven particularly valuable when children are part of the household. In that case, the cash transfer can be conditional on school enrolment of the children and necessary health check-ups for children and expecting mothers, as is current practice in many current CCT programmes around Latin America. Such conditionalities do not aim at excluding anyone but are meant to generate incentives for investing in education and health, which may facilitate the chances of a family moving out of poverty in the longer run.

To maintain the incentives for taking up work opportunities, programme design could include a graduation phase, in which the value of the transfer forgone is smaller than the additional income. This is important to

avoid situations where beneficiaries might be reluctant to take up work for fear of losing their benefit, even if they become eligible again at a later moment. The design could include a phase in which for every additional income earned by the household or individual, only some part of the additional earnings are taken into account to calculate the cash benefit, until gradually reaching a point where no subsidy is available at all. Preliminary and ex-post impact assessments should be systematically conducted to evaluate the effects on (formal) labour force participation and adjust the design if necessary.

Box 2.4. The pros and cons of a Universal Basic Income

A universal basic income (UBI) is an unconditional cash transfer granted at regular intervals to all residents, regardless of their wealth, earnings or employment status. Commonly cited advantages of such a programme are that it is simple and coverage is, by definition, universal.

The main disadvantage of an UBI is that it could be extremely costly. An unconditional payment to everyone at meaningful but fiscally realistic levels would require strong tax rises and possibly reductions in existing benefits, and would not often be an effective tool for reducing income poverty (OECD, 2017^[67]). Some disadvantaged groups would lose out when existing benefits (usually all other social programmes) are replaced by a universal basic income, illustrating the downsides of social protection without any form of targeting at all (Gentilini et al., 2020^[68]).

Similar to the above findings for OECD countries a truly universal Basic Income would be fiscally unviable in most of Latin America unless benefit amounts are reduced to a level where they lose their effectiveness in providing an acceptable living to those in need. Illustrative calculations for Colombia suggest that disbursing a monetary transfer at the level of the extreme poverty line to resident would have costed 8.7% of GDP in 2020. This UBI levels still would leave many households in poverty, especially those at old-age not receiving any pensions or the unemployed or inactive. If the transfer were set to the level of the poverty line, the cost would be 20% of GDP, almost equivalent to Colombia's entire tax revenues (OECD, 2022^[69]).

Those able to work but without jobs should register with the public employment services and when they find a job, part of their wage could be temporarily exempted from the calculation of the benefit. For those adults already working but able to work more, additional hours worked and better jobs are encouraged, and for each extra income they earn the benefit is reduced by a smaller amount.

A single cash transfer for the poor would gain from strengthening state capacities to check up on self-declared information provided by the. This includes earnings from informal labour, which is far more difficult for the state to observe. Local networks and social assistants can play a key role checking the veracity of self-reported information. Brazil, for example, has made significant progress in building up a granular network of social workers and social centres that help in determining the fulfilment of income eligibility conditions for the *Bolsa Família* programme. In some cases, it has also been helpful to design incentives to encourage citizen responsibility, for example by implementing some kind of penalty for those who provide inaccurate or false information (Universidad de los Andes, 2020^[70]). Maintaining large and up to date social registries of poor households are the key instruments for administering such schemes (Box 2.5).

Box 2.5. Improving social registries

Social registries of recipients identify the socioeconomic characteristics of individuals and households who are likely to receive assistance from the welfare system. Social registries help in the design, implementation and evaluation of social policies. They are typically used to identify beneficiaries or verify self-declared beneficiary information, calculate the amount of the benefit due, deliver the benefits and measuring their impact ex-post.

The coverage, accuracy, and quality of information collected and recorded in social registries has improved visibly since the late 1990s, as Latin American countries have collected more information to build the targeting instrument upon which their conditional and unconditional cash transfer programmes were founded.

In some of the less elaborate registries, individuals communicate their information each time they seek assistance. For others, social registries are based on information collected at regular intervals, for example through broad surveys that target vulnerable populations. Most countries choose to supplement these with the option for individuals to update their information via a request for a new survey. In this case, an agent or a social worker administers a new questionnaire in the applicant's home.

One recent innovation has been to use additional data sources such as administrative databases to complete and/or update the information already available in the social registries. The cross-checking of self-reported information from individuals with administrative data has been a feature of so-called "second generation" registries, which require significant efforts to identify households uniquely and unequivocally, so as to minimise duplication, inclusion, or exclusion errors in the programmes. Social registries are also increasingly combined with the massive use of information and communication technologies to inform individuals about their eligibility for a programme and/or to deliver their entitlements, for example during the COVID-19 pandemic.

With these innovations, some of which were driven by the pandemic, governments sought to improve the information available on people already receiving social benefits and expand the scope of social action to individuals not previously covered. Building on these efforts made during the crisis would further improve the targeting and the effectiveness of social benefit delivery.

One lesson that emerges from the pandemic is that large parts of the population are potentially in a situation of requiring assistance at some point, which calls for social registries to be as universal as possible, rather than being limited to poor and vulnerable populations. Connecting different data sources can be a way to achieve this, including tax records, land registry records, vehicle registrations, civil registers. Social registries should also be sufficiently flexible so that the information they hold can be regularly corrected, completed, or updated without the need for mass surveys, promoting and facilitating the process and its corresponding validation (control visits and cross-validation with other sources) (ECLAC, 2020b). This is particularly important in the case of dismissals, where people with previously sufficient incomes to make a living will need rapid support.

The level of the guaranteed minimum income benefit could be determined in various ways, but a relevant poverty line, which exists in most countries, is often a useful reference. By calculating the cash transfer as the difference from the per capita household income level and its distance from the poverty line, the programme would ensure that no household or individual is left in poverty.

Another option to provide income support would be through a negative income tax, where income support would be provided through the tax system. Workers would be required to register with the tax authority and file personal income taxes. Those whose declared their revenue is below a defined threshold would be exempt from paying the tax and would instead receive a payment from the revenue authorities. This

payment decreases gradually as the individual earns more from work. Channelling the income support through the tax system has the advantage of targeting the support to low-income workers while encouraging the take-up of formal jobs. It can also foster financial inclusion and can reduce the scope for clientelism associated in some cases to some social programmes. Experience from some OECD countries, such as United States experience with the earned income tax credit, is positive (Hoynes; Patel, 2017^[71]), as it has increased formal participation among groups with lower labour market attachment and reduced poverty. Such schemes have been also found to reduce informal employment in developing countries (Gunter, 2013^[72]). This option presents a higher administrative burden for tax authorities, but recent and ongoing enhancements in the capabilities of several tax authorities in the region (e.g. Mexico, Colombia or Costa Rica) make it a viable option. As cash transfers, it would require continuing to enhance capacities to validate self-declared information and providing incentives for individuals to report their income truthfully. The idea of minimising formalisation disincentives calls for financing anti-poverty transfers to those in working age in a way that does not affect incentives towards informality by raising the cost of formal labour. Already, almost all CCT programmes in Latin America are financed through general tax revenues, making them particularly well-placed building blocks for enhancing social protection. To the extent that CCT programmes are enhanced and able to react more rapidly in the case of sudden income losses, they may reduce the need for contribution-based benefit programmes, particularly among low-income workers where the additional cost of a mandatory contribution may have strong effects on the prospects of finding a formal job. As in the case of pensions, a useful benchmark may be to aim for social contributions close to zero for incomes at the crossroads between formality and informality, which is typically the minimum wage.

Given that a guaranteed minimum income is designed to avoid poverty, it may not be able to achieve the full degree of income smoothing or insurance against unexpected variations in household income over time that a society may desire. For example, those with higher incomes may have a legitimate interest in insurance against the sudden and temporary income losses associated with dismissals, for example. But such insurance would need to deliver adequate replacement rates to be attractive. A person earning several multiples of the minimum wage may not be convinced by a guaranteed minimum income scheme designed to prevent people from falling below the poverty line. At the same time, such a person is much less likely to work in the informal sector.

Unemployment benefit schemes could therefore be useful to provide consumption smoothing and maintain living standards for workers above the minimum wage, and probably at some distance from the latter. This second pillar could be based on contributions and provide top-up benefits to the basic scheme. There are several possible ways to design such a complementary contributory scheme for those with higher incomes, and in those countries where such systems already exist, there may be a strong case for implementing only minor reforms.

3

Policy options and implementation challenges

The reforms advocated in the preceding chapter would imply a significant re-design of social protection systems and finding the necessary political consensus will face challenges and opposition. While millions of informal and largely unprotected workers stand to gain from social protection reform, potential implementation challenges and opposition from specific groups will need to be considered. An additional key challenge is to finance such reforms as reducing social security contributions for low-wage earners requires raising additional tax revenues or reallocating expenditure, without which the reduction in contributions will not be possible.

The reforms advocated in this paper are not small reforms; they would imply a significant re-design of social protection systems. Large reforms are usually only justified by large challenges, but the extent and persistence of informality in Latin America, and the exclusion from adequate social protection it implies, is a large challenge.

Finding the necessary political consensus for a significant redesign of social protection in the region will face challenges, that will differ from country to country. One of these relates to the tax system. Reducing social security contributions for low-wage earners will inevitably require raising additional tax revenues or reallocating spending. Raising additional tax revenues and reducing social security contributions has proven challenging for most Latin American countries, most of which are characterised by low tax revenues relative to their GDP, with the notable exception of Argentina and Brazil (Figure 1.8). Most countries in the region have scope for expanding tax revenues and to improve the efficiency of spending. However, if countries are not able to compensate the reduction in social security contributions that the reform would require by raising sufficient additional tax revenues to finance basic social protection, the reforms proposed in this paper will not be feasible, or there is a risk is that social protection is weakened overall or remains weak, which is not desirable. To ensure fiscal sustainability, it will be crucial to ensure that these reforms effectively generate the needed revenue when committing to permanent increases in spending. Increasing social spending should proceed only gradually once permanent revenues are available. Countries would need to set up a clear and detailed reform agenda linking tax reforms with social protection reforms.

A second challenge is that once non-wage labour costs are lowered significantly for those earning the minimum wage, there may eventually be a wage range above the minimum wage where marginal contribution rates will be high. This may make it more costly for firms to raise wages, possibly giving rise to low-wage traps, especially in countries with high minimum wages. This has been discussed at length in some OECD countries, including France, where social contributions for low-wage workers saw considerable reduction in the recent past. At present, this issue seems less pressing than the need to get more people into formal jobs in the first place, but it is something to bear in mind for the future.

reforming social protection systems, although necessary, will not be enough to fully tackle informality. Better enforcement of tax and labour laws, simpler labour regulations and lower perceived benefits from informal employment and more investment in human capital and improved rule of law will also be needed. An upside and a reason to start with reforms to social protection is that they could have a more immediate impact on informality if accompanied by stronger enforcement of labour and tax laws than other reforms, such as policies to strengthen education and productivity that typically take longer to bear fruit.

A key question, and precondition for the successful implementation of the reforms advocated in this report, is how to raise the substantial amount of additional tax revenues that are needed to finance them. For example, estimates suggest that in Colombia such reform would cost 1% of GDP (OECD, 2022^[73]). There are significant differences across countries in the region in tax burdens and levels of taxation so the specific tax reforms would vary from country to country. Overall, the most important sources of tax revenue in the region, as in most countries around the world are value added, individual income, and corporate income taxes. Corporate tax revenues in LAC are higher than in the advanced countries, relative to overall tax revenues. Corporate tax rates are often high, but compliance is typically low, and higher rates may lead to further evasion. One way to make collection of corporate taxes more efficient would be to streamline collections and eliminating exceptions, to reduce the nominal burden (lower the rate) but increase overall enforcement.

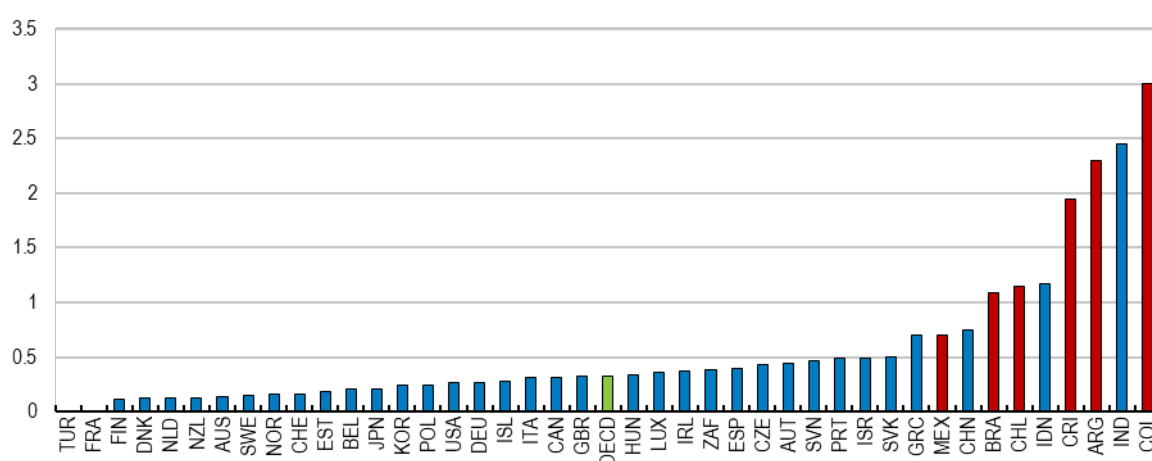
The relatively low contribution of personal income taxes makes income taxes one key element of a possible source of new revenue. LAC countries' low individual income burden is due to low coverage, rather than low rates on top earners. In most countries, only the top 20 percent of citizens pay any income tax, so the tax burden is unusually concentrated. One reason is that personal income tax systems are generally characterised by high income thresholds as of which households start paying taxes, also referred to as basic allowances (Figure 3.1). These are often a multiple of the minimum wage, leaving the incomes of a

large part of the upper and middle classes with incomes in between the current basic PIT allowance and the minimum wage untaxed. Moreover, in many countries, there are numerous personal income exemptions and tax expenditures, often to the benefit of more affluent taxpayers (IMF, 2019^[74]; OECD, 2020^[20]; OECD, 2018^[75]; OECD, 2022^[73]). Reforms could focus on broadening the personal income tax base by lowering exemption thresholds. Caution is needed in lowering the personal income tax exemption as there could be possible negative impacts on labour market participation and hours worked, as well as increases in informality. Those that would start paying personal income tax would need to have incomes far above those for whom social security contributions would be lowered, so the combined effect of higher personal income taxes and lower social security contributions is progressive overall, and to ensure a reduction in non-wage labour costs in the relevant lower income ranges where informality is most prevalent.

Expanding the reach of the personal income tax system could be a valuable objective, as authorities would also gain more information for operating the social protection system, which is currently based on social registries (see Box 2.5). People with incomes below the basic allowance could be required to file simple tax returns. But caution is needed not to affect non-wage labour costs in the lowest income range close to the minimum wage, and not to raise compliance costs for those same low-income people the reform is trying to help by expanding basic social protection.

Figure 3.1. Personal tax income threshold relative to the average wage in Latin America

Income threshold where single taxpayers start paying income tax, measured as a multiple of the average wage



Note: For India, the average worker income is for the organised manufacturing sector as reported in the Annual Survey of Industries.

Source: OECD calculations for Argentina, China, India, Indonesia, South Africa and Peru; OECD Taxing Wages 2017 for Costa Rica and Brazil; OECD Taxing Wages 2023 for the rest of countries.

In addition to reforms to personal income taxes, property taxes, inheritance taxes and broader VAT bases can play an important role. Many Latin American countries have low property tax collection. Improving, updating and completing property registries and ensuring accurate property valuation systems are common challenges and can help raise revenues. Building the capacity of local governments to manage and administer property taxes effectively should be also part of the strategy. Many countries in the region have also margin to raise compliance and limit the scope for exemptions and reduced rates in the VAT while compensating the poorest households through the transfer system. A priority could be to reduce those exemptions that primarily benefit the better-off. This reform could increase VAT revenues, while reducing distortions and addressing equity concerns. Inheritance taxes could be used far more in Latin America and are typically very progressive. Considering that for some LAC countries energy subsidies represent high percentages of their GDP, reducing them and adopting a carbon tax would generate

revenues of relevance. Modernizing tax administrations, starting with improvements in human capital, information systems and the use of advanced technologies, systematically crossing information from different sources and improving electronic invoicing could also help to raise additional revenues.

Greater efforts to increase spending efficiency can contribute to create the fiscal space to finance the reforms. This could be achieved by making a more systematic use of spending reviews including tax expenditures, cost-benefit analysis, improving means testing mechanisms and social registries and public procurement processes. More systematic evaluations of social policies and more rigorous and transparent cost-benefit analysis of infrastructure projects could also help to boost efficiency.

Identifying potential obstacles to the political implementation of a major social protection reform such as the one advocated here implies identifying those who would win and those who would lose from the reform.

The first question has a straightforward answer: The main winner would be the most vulnerable households in Latin American societies, given that expanding social protection would foster more equal societies and more social inclusion. Among individual groups, the greatest benefits of social protection reform would be the millions of Latin Americans that currently lack access to pensions and/or basic protection against poverty. These are the most vulnerable segments of the population, but they may not be the ones with the strongest political voice.

Beyond low-income households, there would also be large potential benefits for society at large, as widespread informality is negatively linked to productivity (Levy and Cruces, 2021^[13]; Maloney, 2004^[76]; Amin and Okou, 2020^[10]). In the past, favourable demographics and high commodity prices have allowed several Latin American countries to grow without much productivity growth. Now, as less and less young people join the labour force, the population will begin to age rapidly over the next decades. In Latin America as a whole, demographics will turn into a drag on growth rather than supporting it as in the past in about ten years from now, and in some countries in the region, that process is set to start much earlier. In this changing scenario, productivity growth will also need to become the basis for sustainable improvements in wages and living standards. That will hinge on policy reforms that can raise productivity, and incentivising more workers and firms to join the formal economy could play a significant role in this context.

By contrast, groups with a less obvious payoff would include those who are already enjoying the privilege of the formal labour market. Among formal workers, those with incomes close to the minimum wage may not be the ones who would lose out. After all, their take-home pay would probably rise due to the reduction of social security contributions, while their future pension benefits would in most cases not be lower than under the current setup.

Formal workers in the higher income ranges may oppose the reform to the extent that more of them would be paying personal income taxes than before. Since most of these have incomes significantly above those of low-income households that currently struggle to join the formal sector, the reform would have a progressive distributional effect overall. Some of these higher income formal workers may also enjoy special privileged pension schemes that deliver better actuarial value than the standard pension regime, for example civil servants, teachers, members of the judiciary or others. To the extent that these -often costly- special regimes would be integrated into the general system, this could trigger additional political opposition. But it would also further equity and fairness of the pension system, especially considering that these special regimes are often more a legacy of power struggles of the past than of rational policy design.

Social security administrators may oppose any reform that would leave them fearing for their revenues when social security contributions are replaced by taxes. That may have political weight when thinking about private pension funds, but in countries where these are large and are generally perceived to function well, there is no reason why they should not play a strong role in the design of the contributory pension pillar.

A wider concern may be a general mistrust in the capacity of the state to use additional tax revenues for the benefit of the population. In some countries, even where tax revenues are low, some citizens tend to

oppose giving government a greater role for fear of these resources being lost in corruption or embezzlement. Enhancing trust in the government will be fundamental for successfully designing, approving, and implementing reforms that increase the resources administered by the public sector. Mistrust of government is high in much of Latin America, reducing support for tax reforms to finance education, social protection, policing and redistribution (Keefer, Scartascini and Vlaicu, 2018^[77]). Reducing corruption and increasing transparency and government accountability can increase trust in government (Scartascini and Valle Luna, 2020^[78]).

To boost feasibility of the proposed reforms, a policy debate to reach the necessary consensus is essential. This policy debate should be evidence-based and should not shy away from a clear identification of the winners and losers of the reforms, quantification of the costs and possible impact on different population groups. An analysis of the sequence and timing of the reforms will also play a very important role. Having a clear mandate and political leadership from the government showing the will and commitment to act would also be important (Tompson, 2009^[79]).

An effective communication strategy on the need for the reforms and their impact on different population groups and the society in general will be essential to lead to acceptance by the population and avoid misperceptions on the impact of reforms. An effective communication strategy can include the provision of information, as well as consultation and dialogue with stakeholders. To reap its full potential, however, authorities can establish a two-way dialogue with the public (OECD, 2020^[80]).

Another key aspect for the successful adoption and implementation of some of these reforms is to incorporate gradual transition mechanisms, which can reduce resistance to proposed changes (CAF, 2020^[81]). A clear sequencing and gradual implementation of tax reforms will be necessary to make them politically viable. This is also the case for pension reforms. Changing the pension system requires a prolonged period of transition, in which those close to retirement and those already retired are not affected. These individuals would hardly be able to make decisions in the short term that could cushion the impact that such reforms may potentially have on their incomes. The reform recommendations in this chapter can be implemented gradually, but in a coordinated manner, applying a whole of the government approach. In the past, small patches to punctual problems have often failed to consider the broader picture, and often created as many new challenges.

Tackling informality also requires a stronger enforcement of the rules, especially when these rules aim to strengthen formalisation incentives. One key challenge for governments will be to ensure that no abuses of the existing legislation are committed, as would be the case when companies falsely classify workers as self-employed or use service contracts to escape regulatory and tax commitments. Authorities should also step-up enforcement efforts to make sure that workers, including the self-employed, and firms pay their taxes. Although the region has made significant efforts to reduce tax evasion, including continued improvements to the tax authority's digital system and electronic invoicing, there remains scope for further improvements in tax administration. Continued efforts to ensure sufficient resources to institutions tasked with the enforcement of labour laws, which should count with well-trained inspectors and the capacity to collect and analyse relevant data and information. Streamlining the penalty enforcement and improving its presence in rural areas are also open agendas in many LAC countries.

Moreover, reforms require regular monitoring and evaluations of their impact, to ensure that progress is made towards the reform's objectives. A robust monitoring and evaluation framework would increase trust in the reform and support the social protection system, while offering the most productive tool to simultaneously assess the programme's effectiveness and provide guidance for improvements. Colombia, for example, already has an advanced monitoring and evaluation framework of public policies in place, and so do several other countries in the region. Continuous efforts to enhance this process, stronger links between planning, budgeting and evaluation, more frequent and faster links between results and decision-making, and better quality of data from the beginning of the programme implementation would help improve social policy implementation and increase feasibility of reforms.

Finally, there is also a question of finding the right timing for undertaking large reforms. The strong negative impact of the Covid-19 pandemic on social inclusion and potential growth may have generated momentum for reform. Not only is there extensive literature showing that structural reforms, including those related to social protection, may be more easily undertaken in times of economic difficulties (Sturzenegger and Tommasi, 1998^[82]; Drazen and Grilli, 1993^[83]). The Covid-19 pandemic has also triggered an unprecedented level of emergency support to citizens, including many new or expanded social benefits. In light of the significant policy support that most governments in the region and the world have provided during the pandemic, citizens may now be more inclined to turn to the state when they are in severe need, and the expectations about the state's role and capacity to provide social protection may be much higher now than only a few years back.

All these considerations provide a strong rationale for moving forward towards a social protection system that is compatible with low incentives for informality, providing benefits to all those in need. Building social protection systems in Latin America was a long and arduous task, but it eventually happened, despite all the unresolved challenges in its design. Now is the moment to reform the system to achieve better material living standards and more inclusive societies for all Latin Americans.

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