

# EXPANDING SOCIAL PROTECTION AND ADDRESSING INFORMALITY IN LATIN AMERICA

**Alberto González Pandiella, OECD Economics Department**

Montevideo, 17 November 2025

[oe.cd/EcoLac](https://oe.cd/EcoLac)



@OECDeconomy

@OECD

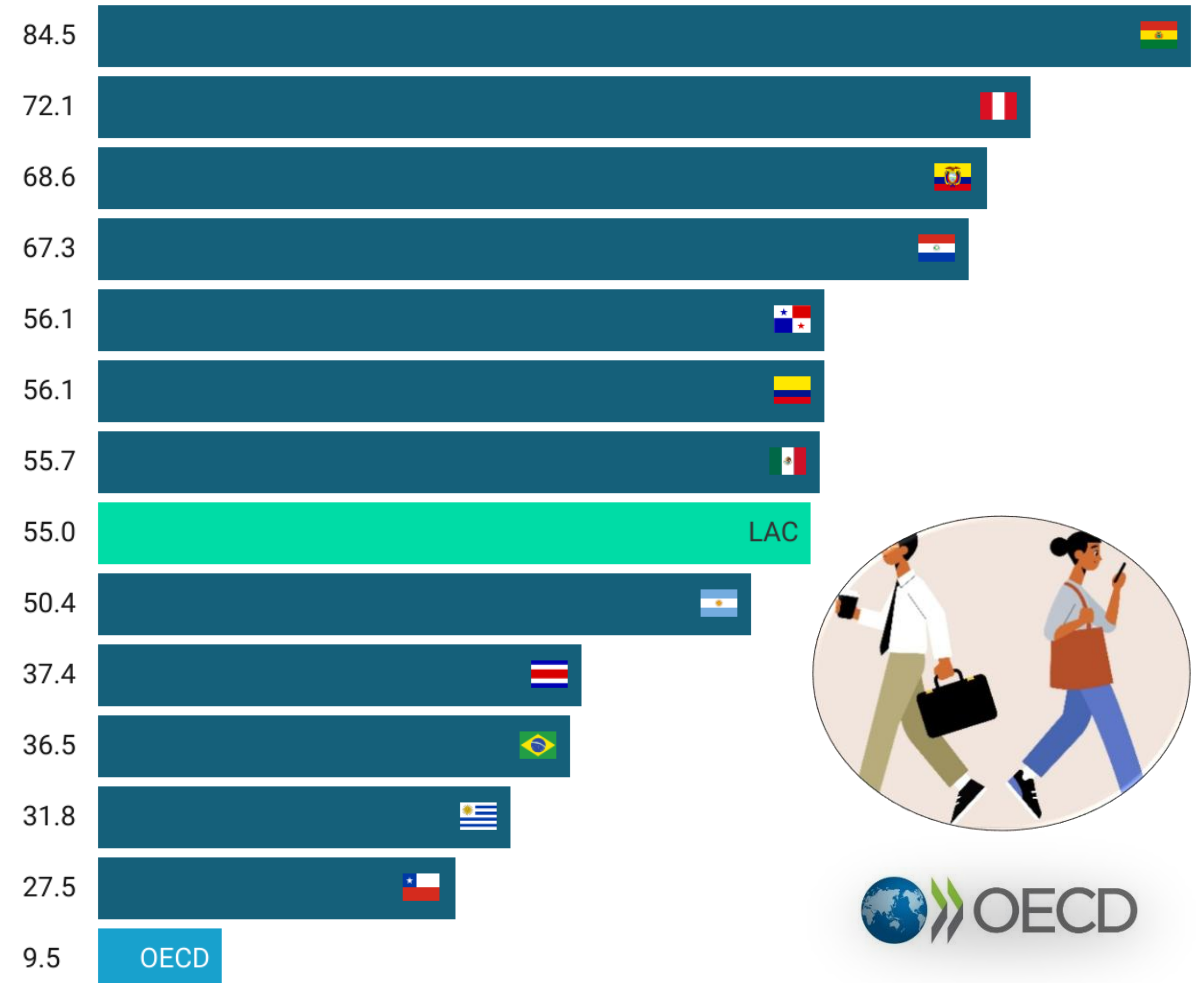


# Informality: a long-standing challenge

- Across Latin America, around **50% of workers** are affected by informal employment
- Significant variation across countries: 27% informality in Chile, around 85% in Bolivia
- Informality has many definitions, but a commonly used one is the absence of access to social security
- High informality and **low productivity**: two sides of the same coin

## Informality rate

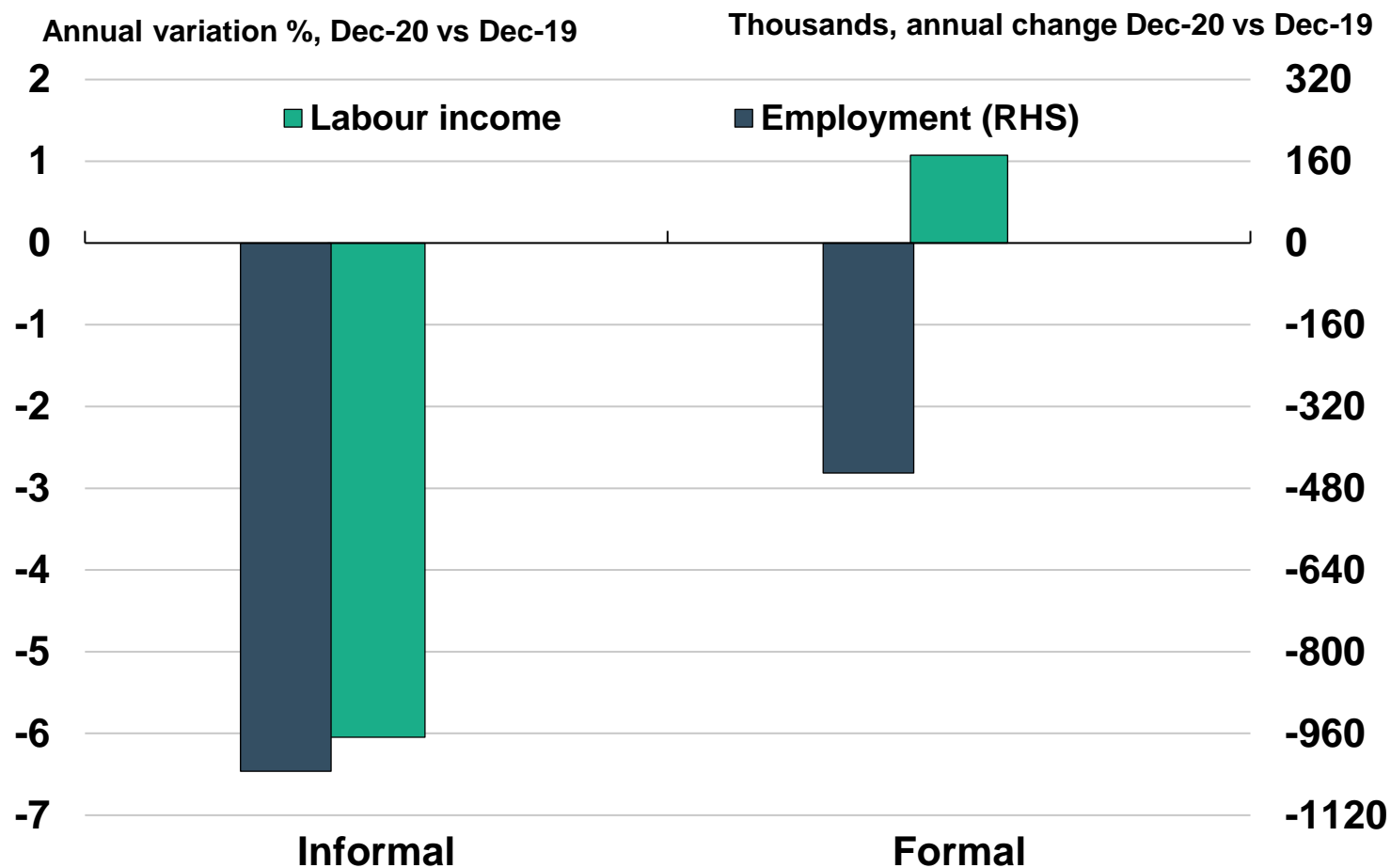
% employment



# Covid-19 has exposed LAC's gaps in social protection

- Informal workers were completely off the radar of public policies, and hard to reach in the emergency.
- This has exposed the gaps of LAC's social protection frameworks, which are mostly based on social security contributions.

Informal workers suffered large job and income losses during the pandemic in **Colombia**

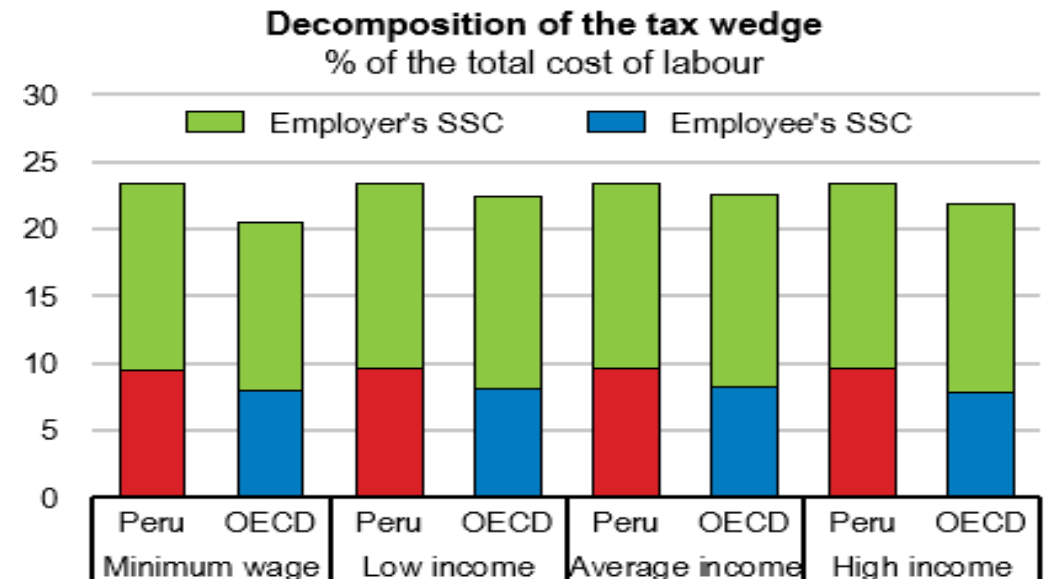
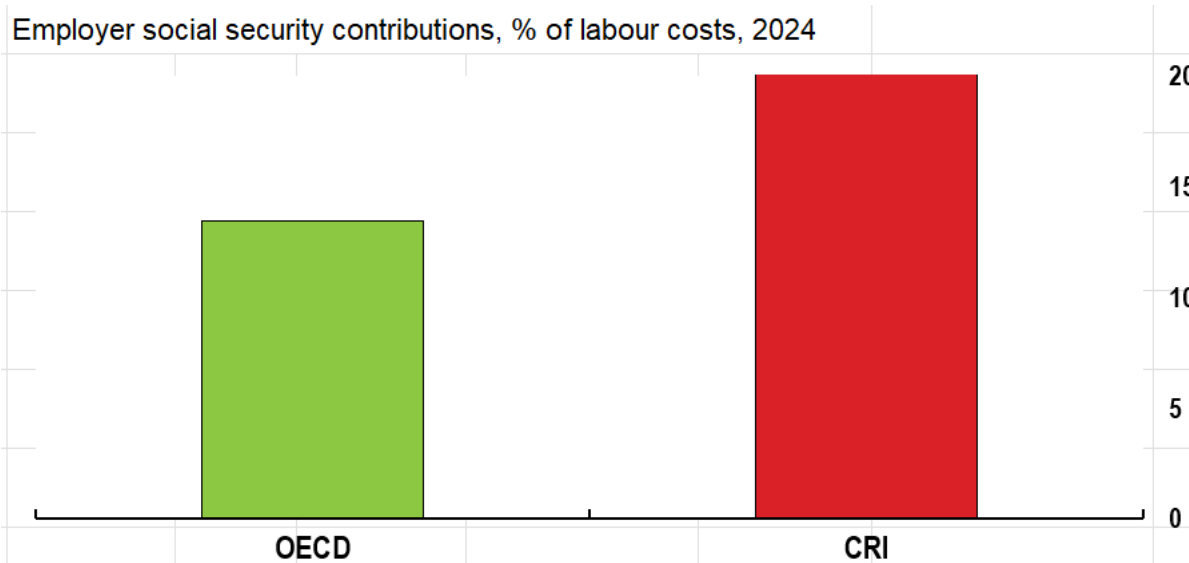


Source: Economic Survey of Colombia (2022).

Restricted Use - À usage restreint

# Potential causes of informality

- Multidimensional causes of informality: low skills, low productivity, weak institutions....and high non-wage costs.
- The **design of social protection and its financing** plays an important role.
- Cost differences between informal and formal jobs can be high, especially at the minimum wage.
- Reducing non-wage labour costs has reduced informality.





# The typical setup of social protection in LAC...

- Workers and employers pay contributions proportional to wages to get access to social security benefits → Only formal workers have access to social insurance.
- During the 1990s, many LAC countries developed non-contributory benefits, but these have often insufficient coverage and benefits. Despite good intentions, they often strengthen incentives for informality.
- **Vicious circle:**
  - The most vulnerable are excluded from most social protection benefits.
  - The financing of these benefits contributes to pricing low-skilled workers out of the formal labour market and perpetuates this duality.

# Contributions are used to finance programmes beyond social security

Table 8.4. Payroll-based contributions in Costa Rica, by entity of destination

| Caja Costarricense de Seguro Social                |          |          |       |
|--|----------|----------|-------|
| Concept  | Employer | Employee | Total |
| SEM/Health   | 9.25     | 5.5      | 14.75 |
| IVM/Pensions                                       | 5.25     | 4        | 9.25  |
| TOTAL CCSS   | 14.5     | 9.5      | 24    |
| Other institutions, all paid by employer           |          |          |       |
| Bank for Communal Development (State-owned bank)   |          |          | 0.25  |
| FODESAF  |          |          | 5.0   |
| IMAS   |          |          | 0.5   |
| National Vocational Institute (INA)                |          |          | 1.5   |
| Total Other institutions                           |          |          | 7.25  |
| Act on Worker's Protection                         |          |          |       |
| Bank for Communal Development (employer)           |          |          | 0.25  |
| Bank for Communal Development (workers)            |          |          | 1.0   |
| Labour Capitalisation Fund (employer)              |          |          | 1.5   |
| Compulsory Complementary Pension Regime (employer) |          |          | 1.5   |
| National Insurance Institute (INS) (employer)      |          |          | 1.0   |
| Total Act on Worker's Protection (AWP)             |          |          | 5.25  |
| TOTAL  |          |          | 36.5  |

Source: CCSS



# A potential solution

- **Two basic principles for reform:**
  1. **Provide a universal basic set of benefits**
  2. **Do not tax formal work to finance that set:**
    - Use general tax revenues instead of social contributions.
    - Ensure significant reductions in non-wage labor costs for low-income workers.






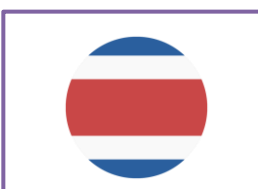






# » What this means for old-age pensions

- Multi-pillar system:
  - Pillar I – **Non-contributory**: A basic, universal and tax-financed pension benefit. Benefit level: at least the poverty line.
  - Pillar II: A complementary, **contributory** benefit to reach adequate replacement rates for those with higher incomes.
    - Contributions can be progressive, lower for low-income workers, and target a replacement rate close to 50% (OECD average).
    - Some countries need deep reforms of contributory schemes.



# Examples: Costs of **financing** universal pensions and a **progressive contribution** structure

|   |   |   |              |
|---|---|---|--------------|
|    |    | A benefit equivalent to 1.3 poverty lines. Current expenditure: 0.1% of GDP; implicit subsidies: 0.5% GDP | 1.6% of GDP. |
|    |    | A benefit equivalent to the poverty line. Current expenditure: 0.1% of GDP                                | 1.5% of GDP. |
|    |    | A benefit equivalent to the poverty line. Previous spending on social pensions: 0.35% of GDP              | 0.95% of GDP |
|   |   | Zero-rate mandatory contributions and payroll taxes on wages up to 1.25 minimum wages.                    | 1.5% of GDP  |
|  |  | Zero-rate mandatory contributions on wages up to 1.25 minimum wages.                                      | 1.1% of GDP  |



# What this means for cash transfers

- Conditional cash transfers programmes have proven effective to reduce poverty.
- Cash-transfers programmes are largely tax-financed and are not limited to formal workers.
- But coverage is often insufficient, benefits are low, and enrolment lags can be long.
- Creating universal means-tested cash transfers could often eliminate poverty at a relative low cost.



# Example from Peru: Cash transfers

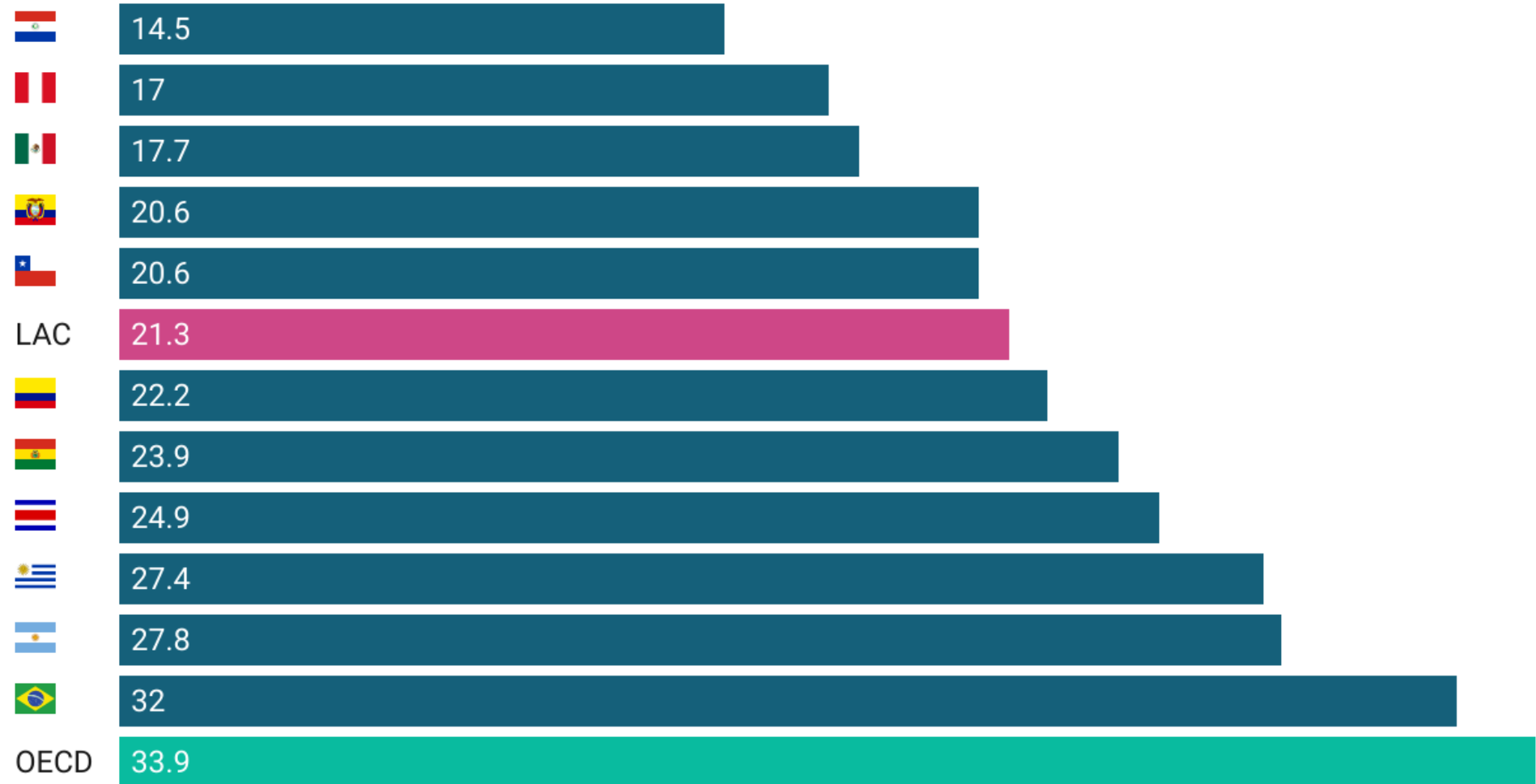
- Current situation in Peru
  - Coverage is low, and low income alone does not imply automatic eligibility.
  - Benefit levels are low and many households are left in poverty even after receiving benefits.
- Reform suggestion:
  - Universal means-tested cash transfer (guaranteed minimum income).
  - Implementation can build on recent improvements in social registries.
  - Accounting for informal labour incomes is challenging, but possible.
  - Cost of reform: around 1% of GDP.

# » The **political economy** of reforming social protection

- Main benefits of these reforms would accrue to **low-income households**, especially to those without formal jobs.
- In the short term, they would gain access to better benefits. In the long term, formalisation opportunities would improve due to lower non-wage labour costs.
- Making basic social protection universal, complemented by progressive contributory schemes, would cost between **1% and 4% of GDP** depending on country in the LAC-7 → **this requires significant reforms to the tax system.**

# Tax revenues in LAC are generally low

% GDP



Note: Year 2024.

Source: OECD Global tax revenue, OECD Revenue Statistics in Latin America and the Caribbean 2025

# In a nutshell

- Current social protection systems are often a major factor behind widespread labour informality and insufficient social safety nets.
- It is possible to design social protection reforms that simultaneously expand coverage and improve formalisation incentives.
- More tax-financing of basic benefits will generally require tax reforms and incur transition costs, but the long-run fiscal costs are usually manageable.
- The post-pandemic environment may have improved the political economy backdrop of such a reform.
- An opportunity for achieving durable reductions of inequality and poverty and productivity gains.



<https://oe.cd/LAC-Informality>

## For more info:

- ✉ [jens.arnold@oecd.org](mailto:jens.arnold@oecd.org)
- ✉ [aida.calderasanchez@oecd.org](mailto:aida.calderasanchez@oecd.org)
- ✉ [paula.garda@oecd.org](mailto:paula.garda@oecd.org)
- ✉ [alberto.gonzalezpandiella@oecd.org](mailto:alberto.gonzalezpandiella@oecd.org)



<https://oe.cd/Eco-LAC>



## Expanding Social Protection and Addressing Informality in Latin America





# Example from Colombia: Healthcare benefits

- Current situation in Colombia
  - A non-contributory healthcare programme with benefits that are almost identical to the basic contributory programme.
  - Formal workers' pay a contribution of 8% of wages for this.
  - Patient health records are not shared across systems.
- Reform suggestion (OECD, 2022):
  - Merge parallel systems into a single and universal basic health programme.
  - A set of basic health care benefits would be fully tax-financed.
  - Contributory/Private health programmes could complement this package.
  - Cost of reform estimated at approximately 0.8% of GDP.



# What this means for **healthcare** benefits

- Several countries have established universal non-contributory public healthcare programmes to improve coverage of healthcare.
- Scope for improvement in access and quality exists, but progress has been impressive in some countries.
- Main challenge is to **avoid creating awkward incentives for informality**, which arise when differences between contributory and non-contributory benefits are not sufficiently valued to justify contributions.