

### CHAPTER III

## SLOW TRANSITION TOWARDS A NEW SOCIAL CONTRACT

“Discrimination, which generates humiliation, breeds hate, and sets people against people, not only violates our elementary sense of justice but is also incompatible with treating people as ends in themselves.”<sup>1</sup>

Even though PAYG was implemented world-wide as a basis to democratize retirement and reduce poverty in old age, during the 1980s and 1990s the viability of state-run PAYG pension schemes was severely questioned due to a complete package of problems: demographic changes, the retirement of the baby boom generation in the near future, early retirement and the increasing social security expenditures of industrialized countries in the western hemisphere.<sup>2</sup> The result of several analyses was that PAYG pension schemes were basically broke and that the system was not going to be able to sustain pensions for further generations.<sup>3</sup> This entire package of problems created a policy maker panic, and as a consequence several solutions were explored and debated.

One possibility to solve the pension problem required the complete reform of PAYG, privatizing the system and basing it on a fully funded structure not subject to the problems mentioned above. This would allow the continuity of a pension system.<sup>4</sup> Even though at first light this seems like an adequate solution, this chapter shows that, after a careful analysis using the parameters presented in chapter two, the implications of the new system, commonly known as Individual Accounts (IA), extend far beyond the realm of economic viability.

Leaving financial considerations aside, when the IA system was designed, apparently the main purpose was to mitigate financial liabilities created by the PAYG scheme and its

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<sup>1</sup> Amitai Etzioni, “Forward,” *Transformation of the Welfare State: The Silent Surrender of Public Responsibility*, Neil Gilbert (New York: Oxford University Press, 2004), xv.

<sup>2</sup> Frances Cairncross, “Pension Reform and the Welfare of Pensioners,” *Fiscal Studies* 26, no. 1 (2005): 1.

<sup>3</sup> Cairncross, “Pension Reform and the Welfare of Pensioners,” 2.

<sup>4</sup> Monika Queisser, “Pension Reform and International Organizations: From Conflict to Convergence,” *International Social Security Review* 53 (February 2000): 32.

intergenerational contract. The easiest solution was to cancel the most important pillar of PAYG, intergenerational cooperation; and to ground the new system on individual responsibility. The effects of the “easy way out” were the inevitable severing of the links of social cooperation and obligation. In addition, given that the primary focus of the system is the sole individual, this does not allow the newly designed system to have an expanded vision of the different needs of age groups, therefore disregarding the moral relevancy of certain age groups, specifically of the elderly as a disadvantaged group. Considering the above, it would be difficult not to recognize that issues of social justice failed to be taken into account in the design of IA, thus overlooking its inherent flaws.

Even though it might seem that the flaws of IA are pale considering the alternative of the financial bankruptcy of PAYG, I show here that they are critical parameters which, left aside, have important implications that translate into the advancement of radical individualism in social policy.

I first offer a clear and concise explanation of the Individual Accounts system, presenting its most important characteristics and pillars. This will allow me to identify the considerable differences with PAYG. I use these differences to apply the parameters put forth in the second chapter of this dissertation, to argue that IA left aside considerations of social justice, therefore advancing radical individualism in social policy as a considerable negative effect of social policy.

### **Individual Accounts System: The Beginning**

After the First World War and the Great Depression it became evident, for governments like the United States and England, that deregulated free-market policies following the theories of Adam Smith, could eventually succumb to crisis and therefore leave members of society severely unprotected and at risk from these contingencies. After the Second World War, states around the world adopted a new role that expanded its

responsibilities and implemented social policies, which awarded citizens a safety net against global economic risks. Scandinavian countries went much further and designed policies that further protected citizens from natural contingencies, such as health, education, housing, and old age risks. These policies were considered during the 1950s and 1960s as the birth of the Welfare State.<sup>5</sup> Beyond the global economic issues why the Welfare State was implemented, lies a philosophical reasoning related to the contractarian tradition. In his theory of social justice, Rawls found the underlying justification of social policies in the *fair* distribution of benefits and burdens of social cooperation.

The fair distribution of benefits and burdens would translate into redistributive policies that aided the least advantaged members of society, such as public education, health care and housing. These policies were financed by progressive taxation of citizens, whereby the most fortunate payed more to allow the less fortunate access to these services. In these particular cases, the citizens targeted to receive such benefits were identified by their economic standing, and not necessarily by their age. One important policy that targeted the specific contingencies of old age was the state-run pension scheme. The back-bone of most pension programs world-wide has been an intergenerational solidarity contract, where the young provide for the elderly under the understanding that when this young generation reaches old age, the new younger population will provide for them (Pay-As-You-Go).<sup>6</sup>

PAYG is structured as immediate transfers to the elderly, thus its continuity depends on healthy demographic pyramids which are comprised with a fairly large base of young individuals, and a smaller tip of elderly. A healthy demographic pyramid allows dependency ratios to be leveled without putting too much pressure on the younger population. This

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<sup>5</sup> Neil Gilbert, *Transformation of the Welfare State: The Silent Surrender of Public Responsibility* (Oxford: Oxford University Press, 2004), 4.

<sup>6</sup> John B. Williamson and Matthew Williams, "Notional Defined Contribution Accounts: Neoliberal Ideology and the Political Economy of Pension Reform," *The American Journal of Economics and Sociology* 64, no. 2 (April 2005): 487.

equilibrium was placed in question when the very large baby boom generation, born after the Second World War, had a very low birth rate. In addition, the baby boomers would constitute a generation with increased longevity.<sup>7</sup> Basically, the generation that would pay the pension of the baby boomers, for an increased amount of time, was too small. And in the case of the United States, social security funds had saved an important amount of surplus from the PAYG scheme. However, different administrations had borrowed this surplus during eras of economic crisis, and were now unable to use them to subsidize the system.<sup>8</sup> The result as Frances Cairncross points out is that, “[m]ost such schemes around the world are bust. Governments have made promises that they simply cannot keep.”<sup>9</sup>

This impending crisis brought about a number of solutions such as an extension in retirement age, the decrease of benefits, the increase of contributions.<sup>10</sup> All these possible solutions did not entail a change of regime, they would all range within the PAYG systems. Yet another solution was brought to light which required the complete reform of the PAYG scheme into an individual responsibility structure. The government of Augusto Pinochet in Chile designed the new system and pioneered the privatization of pension schemes in 1981.<sup>11</sup> José Piñera, the head designer of the private scheme, justified privatization as a way for workers to continue receiving a pension and to promote economic growth in Chile.<sup>12</sup> One of the main promises of IA was also that it would increase capital markets and investment.<sup>13</sup>

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<sup>7</sup> Michal Engelman and Summer Johnson, “Population Aging and International Development: Addressing Competing Claims of Distributive Justice,” *Developing World Bioethics* (2006): 1.

<sup>8</sup> “Status of the Social Security and Medicare Programs” *Social Security Online* (23 March 2005 [cited 2 March 2009]): available from <http://www.ssa.gov/OACT/TRSUM/trsummary.html>

<sup>9</sup> Cairncross, “Pension Reform and the Welfare of Pensioners,” 2.

<sup>10</sup> Erik Schokkaert and Phillipe Van Parjis, “Pensions Policies for a Just Europe: Individual versus Collective Responsibilities,” *Journal of European Social Policy* 13, no. 3 (2003): 2.

<sup>11</sup> Williamson and Williams, “Notional Defined Contribution Accounts,” 488.

<sup>12</sup> José Piñera, “La Revolución Mundial del Sistema de Pensiones,” *El Cato Institute* [June 19, 2001 (cited March 3, 2009)]: available at [www.elcato.org/pensiones\\_jp.htm](http://www.elcato.org/pensiones_jp.htm)

<sup>13</sup> Evelyn Huber and John D. Stephens, “The Political Economy of Pension Reform: Latin America in Comparative Perspective,” *United Nations Research Institute for Social Development* (2000): 5.

The general design of the new IA system is structured as a fully funded scheme, where the worker's future pension is being provided for during her active working life. Ricardo Pulgar mentions the six basic pillars of IA. The first is the transfer of a mandatory percentage of the workers' income to their accounts. The second pillar refers to the management of the accounts by Private Pension Funds (PPF) who, in turn, invest the savings of the accounts in different financial instruments, creating a profit for the workers.<sup>14</sup> The third is constituted by the payment of these account management institutions. PPFs charge a fee for the management of accounts, paid for by the workers. The fourth entails a diversity of PPFs from where the worker is allowed to choose. The fifth is that the role of the state is limited to a supervising level.<sup>15</sup> Finally, the sixth requires the workers to reach the country's legal age of retirement to receive their saved benefits.<sup>16</sup>

The six pillars of IA are substantially different to the state-run PAYG system. Three of the pillars, the second, third and fourth, represent the transformation of PAYG into a private system and the economic costs of such a reform. The consequences of the implementation of these pillars will be analyzed in detail in the next chapter concerning the case of Mexico, as they entail the economic returns of pensioners and their welfare. In this chapter, I focus my attention on the pillars that substantially disregard the fundamental social justice foundations that lie behind the pensions social policy; the first, second and fifth. It is important to note that some of the pillars that entail the (dis)consideration of social justice also entail the (in)stability of pensioners' economic welfare. This overlap can be understood as the effect that social justice has on economic welfare.

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<sup>14</sup> Williamson and Williams, "Notional Defined Contribution Accounts," 488.

<sup>15</sup> Even though the pillars of this scheme are variable, critical variations have been found specifically in this pillar depending on the country. Some countries that have already implemented IA, have enlarged the role of the state, or have even allowed the state to manage the accounts.

<sup>16</sup> Ricardo Pulgar, "Breve Descripción del Sistema de Pensiones de Chile," *Fundación Interamericana para el Desarrollo y Formación de Fondos de Pensiones Laborales* (April 2001 [cited March 2, 2009]): available at [www.finteramericana.org/librosdoc/publica/Pulgar1.doc](http://www.finteramericana.org/librosdoc/publica/Pulgar1.doc)

## **The New Pension System: The Privilege of a Few**

One of the most important differences between the state-run PAYG and IA can be identified in the first pillar of IA. The contributions that workers payed in order for the state to provide the pension of the retired generation in PAYG, are now used for individual savings. This substantial change implies the elimination of the PAYG intergenerational contract, therefore avoiding economic liabilities for the state. It is first important to analyze this pillar using the two levels of analysis of intergenerational justice issues, before shouting out the economic victory of IA.

As explained in the previous chapter, there are fundamentally two basis of analysis of the intergenerational contract: cooperation between birth cohorts and the needs of age groups where the elderly have moral relevancy as a least advantaged group. In the first case and remembering that birth cohorts are the generations presently living, IA can be characterized as an answer to the question, who has to pay for what, and is this fair? By structuring the program as individual accounts, IA automatically relieves the pressure of the younger cohorts to fund the pension of older ones,<sup>17</sup> cancelling social cooperation between cohorts, and not only the burdens it brought with it, but necessarily the benefits also.

In the case of PAYG, social cooperation between birth cohorts was the fundamental pillar of the system. The most important obligations derived from PAYG were the mandatory contributions of younger cohorts to pay the pension of older ones. This obligation was transferred from cohort to cohort, creating a cycle of collective cohort cooperation, where the “burden” to pay the pension of the elderly was not carried by a single individual, but by entire cohorts. From a Rawlsian perspective this can be understood as the normal process of social cooperation where burdens are shared by the collective, and the benefits are distributed fairly between the individuals that comprise that collective. The importance Rawls awards to

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<sup>17</sup> Schokkaert and Van Parijs, “Pensions Policies for a Just Europe,” 9.

individuality does not (dis)regard the critical importance of the collective, without which individuality cannot be achieved. The IA program eliminates this collective responsibility, and by extension the collective cooperation cycle, as would be suggested by Nozick. Under the new system, birth cohorts do not have the obligation to pay to sustain the pension of the elderly. It is implicit, therefore, that if birth cohorts stop contributing for the elderly, younger cohorts will not have the obligation to contribute for them when they reach old age. The result of such a system is the elimination of collective cooperation to avoid collective responsibilities which, under a Nozickean system, is not a detrimental result. On the contrary, collective responsibilities that require individuals of a collective to contribute are unacceptable since they force members of society to give up some of their self-owned and self-earned goods to provide for others. While this might seem as a relief of social obligation pressures, it also entails social cooperation benefits.

In a PAYG scheme, the fundamental right awarded by social cooperation, was the reception of a pension during old-age and protection from exogenous risks.<sup>18</sup> Following the Musgrave rule presented in chapter two, if a birth cohort is impacted severely by economic or environmental shocks during its younger years, their ability to save for old age will not be high. Fortunately, social cooperation and risk-sharing between cohorts alleviates these unfortunate circumstances, when this cohort arrives at old age they might receive larger benefits from the luckier cohorts born afterwards. Also, considering the younger cohort under severe shocks, one way to pool the risks might be by decreasing the level of contributions.<sup>19</sup> In the case of IA, compromises made between cohorts are no longer possible, since social cooperation is eliminated. Cohorts have to sustain the whole weight of exogenous shocks by themselves, they are not able to receive the benefit of protection. Since they no longer have

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<sup>18</sup> Schokkaert and Van Parjis, “Pensions Policies for a Just Europe,” 5.

<sup>19</sup> Schokkaert and Van Parjis, “Pensions Policies for a Just Europe,” 5.

any responsibilities, cohorts will not be able to have claims of justice towards other generations, whatever their situation might be. Unfortunately, Nozick does not provide a solution to this result as he would not disagree with it. The unfortunate circumstances of some birth cohorts do not warrant social cooperation or action from the state. In any case Nozick might suggest altruistic gestures.<sup>20</sup> If cohorts wish to help others as an altruistic gesture, this does contradict the Entitlement Theory. Nevertheless, the Entitlement Theory does not consider in principle the needs of cohorts, therefore, altruism is a choice not a responsibility. The result of IA as a Nozickean-founded scheme is that it leaves individuals in positions of risk, where too much is left to chance and choice.

This effect of cancelling social cooperation overlaps to the benefit of pension reception. Cohorts will not be awarded a pension provided by collective cooperation. Single individuals within cohorts will be solely responsible for their pension in old age. If unfavorable circumstances shock a cohort, their possibilities to fund their future pension will be considerably diminished. As social cooperation within cohorts is eliminated, individuals will be left to fend for themselves even though this might entail negative consequences in their old age.

These negative results can also be perceived by the third pillar of IA. The state-run PAYG system was designed so that it, not only recognized the elderly as a disadvantaged group, but also it aided the least advantaged individuals within cohorts following a Rawlsian perspective. Young least advantaged individuals that could not afford to save for their old-age, were aided through cohort cooperation. At the end of their productive life, their pension was provided by younger cohorts independent of their minimal contributions, which allows them to pursue their life-plans as others more advantaged.

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<sup>20</sup> Robert Nozick, *Anarchy, State and Utopia* (United States of America: Basic Books Inc., 1974), 334.

In the case of IA, the system, through the third pillar, directly attacks the least advantaged. A study by Evelyn Huber and John D. Stephens has shown that the fees that PPFs charge, can be considered a regressive tax.<sup>21</sup> Let us assume that individual A earns \$10,000 a month, and individual B earns \$5000. In this case, the least advantaged individual is B. Let us further assume that both, A and B, give their monthly savings to the same PPF, which in turn charges \$2000 as a monthly fee. A will be able to save \$8000 a month, while B will only save \$3000; therefore saving considerably less for her retirement. This example suggests that IA was not designed to have social justice considerations for the advantaged/disadvantaged, and by extension to the second principle of justice. The result of PPF's fees will therefore have a considerable detrimental effect on the least advantaged.

Furthermore, the effects of eliminating social cooperation in the IA system overlaps into the age group level of analysis. As was presented in chapter two, Norman Daniels' Prudential Life Time Account is very useful to identify the different needs of age groups.<sup>22</sup> It is important at this point to remember that one of my criticisms to Daniels was that the importance he awards to old age seems only as a suggestion. If old age is introduced as morally relevant, then the focus of institutions on the elderly has to be mandatory, recognizing their increasing needs due to their least advantaged position. Nevertheless, IA is primarily focused on individual responsibility and individual savings. The level in which IA works, does not allow it to recognize the needs of age groups, particularly the old age group. This is more a responsibility of social institutions created by the state,<sup>23</sup> Private Pension Funds, as is stated in the second pillar, are not social, they are private financial institutions.<sup>24</sup> Given their private foundations, PPF's are not necessarily responsible of unequal treatment in

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<sup>21</sup> Huber and Stephens, "The Political Economy of Pension Reform," 16-17.

<sup>22</sup> See Norman Daniels, *Am I My Parents' Keeper? An Essay On Justice Between the Young and the Old* (Oxford: Oxford University Press, 1988).

<sup>23</sup> Huber and Stephens, "The Political Economy of Pension Reform," 1.

<sup>24</sup> Pulgar, "Breve Descripción del Sistema de Pensiones de Chile."

favor of the elderly, or any other age group for that matter. Their sole commitment is the management of worker accounts. The impact of this reduction of responsibilities towards age groups can be perceived on two main fronts.

State-run PAYG systems had two important objectives to recognize the moral relevancy of the elderly as an age group; to democratize the possibility of retirement and to avoid poverty in old age.<sup>25</sup> In the first case, PAYG awarded all workers the opportunity to retire. IA does not. Individuals are responsible for saving enough for their old age years. Considering inequality gaps existent in all countries, some will be able to save enough and some will not. The obligations of PPF's will not include the fair arrangement of pensions. It is therefore, possible that a part of the population will have the opportunity to retire, while others will not. It might be the case that the state can provide for the least advantaged workers, however according to the fifth pillar of IA, the role of the state is limited to require PPF's to manage the saving accounts according to law, and providing the required interest rates for workers' savings.<sup>26</sup> The restriction of the state as a provider of equality and protection is mainly Nozickean. Nozick agrees with a minimal state that is primarily concerned with overseeing the natural development of the free-market and the Entitlement Theory. It follows that Nozick would not allow the state to go further than this. In a Nozickean society, the relevance of the least advantaged is not a priority, as is not the fact that under his system retirement would turn into a "privilege of a few,"<sup>27</sup> like in the case of IA.

Following the analysis of the previous chapter where the status of the elderly is awarded moral relevancy for their decrease of natural talents, the effect of turning retirement into the "privilege of a few," would mainly impact the workers that do not have enough

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<sup>25</sup> John Myles, "A New Social Contract for the Elderly?" in *Why We Need a New Welfare State*, ed. Gosta Esping-Andersen (Oxford: Oxford University Press, 2002), 132.

<sup>26</sup> It is important to remember that not all countries that have introduced IA have allowed the state's role to shrink that much. Mexico, for example, allowed the state to provide minimum pensions for worker's that do not reach the necessary amounts during their productive years.

<sup>27</sup> Myles, "A New Social Contract for the Elderly?" 132.

resources to retire, and therefore need to continue working. Even though, certain laws that comply with Rawlsian liberalism have been implemented, in countries like the United States that prohibit discrimination on an age basis, important studies have shown that employers are reluctant to hire individuals from the old age group.<sup>28</sup> The important decrease of the natural talents and health of the elderly would have a detrimental impact on their income levels due to the availability of jobs. These circumstances would eventually lead to important percentages of poverty in old age. The democratization of retirement allowed individuals to retire and to have a stable income that did not decrease as their age increased. The possibility of retirement with IA is not spread to the general population. This, in turn, would negatively affect the welfare of the elderly, extending the working life of some that cannot save enough during their productive years and experiencing the decrease of their income as their age increases.

Furthermore, the second pillar of IA states that Private Pension Funds have to invest the worker's savings in financial instruments, to increase savings. Even though PPF's are not allowed by law to engage in highly risky investment,<sup>29</sup> pension funds can still be subjected to the increased volatility of financial markets, which might eventually decrease the interest rates of savings, therefore impacting the future welfare of workers.<sup>30</sup> Even though Nozick would strongly oppose state maneuvers to soften the effects of the free-market, some states have argued for a larger role where the government might be allowed to implement redistribution schemes to avoid poverty within the workers that are highly impacted by the volatility of financial markets.<sup>31</sup> Nevertheless, the dependency on financial markets cannot necessarily guarantee an adequate level of pensions to reduce poverty in old age.<sup>32</sup>

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<sup>28</sup> See David Neumark, "The Age Discrimination in Employment Act and the Challenges of Population Aging," *Research on Ageing* 31, no. 1 (January 1, 2009).

<sup>29</sup> Alejandro Ferreiro Yazigi, *El Sistema Chileno de Pensiones Derivado de la Capitalización Individual* (Santiago, Chile: Superintendencia de Administradora de Fondos, 2002), 55.

<sup>30</sup> Queisser, "Pension Reform and International Organizations," 36.

<sup>31</sup> Ferreiro, *El Sistema Chileno de Pensiones*, 65.

From a Rawlsian perspective, particularly the second principle of justice, it is critical to redistribute social and economic inequalities in favor of the least advantaged; and to create institutions that follow fair equality of opportunity. In this sense, IA fails to promote social justice. To redistribute social and economic inequalities in favor of the disadvantaged, it is first necessary to identify them. In chapter two, I argued strongly that the elderly are part of this group. However, IA does give any relevancy to the different needs of age groups, therefore disregarding the moral position of the elderly as disadvantaged members of society.

To redistribute social and economic inequalities inevitably implies social cooperation between members of society. Social cooperation between birth cohorts is cancelled by IA, therefore leaving cohorts to deal with their unfortunate or fortunate circumstances by themselves. Finally, Rawlsian fair equality of opportunity awards opportunities for the advantaged and the disadvantaged to reach certain positions. In the case of retirement, both groups have to have a fair chance to retire with a pension. Nevertheless, IA is an individualized system that awards the right to retire to those who can purchase it, with their life savings. It follows that the design of IA is not structured to promote social welfare on the basis of social justice, but succeeds in advancing Nozickean libertarianism along with the unfortunate result of a Nozickean-styled slavery.

The previous analysis suggests that the cancellation of social cooperation, and the disregard of the elderly, imply a whole new social structure in pension programs, mainly based on Nozickean libertarianism which awards opportunities to the individual on the basis of her ability to pay. In this sense, Huber and Stephens suggest that IA attacks “[t]he values of solidarity and redistribution in private fully funded individual accounts systems.”<sup>33</sup> Therefore, the question one should ask is, what are the consequences of promoting Nozickean values?

### **Changing Paradigms: From Collective Responsibility to Radical Individualism**

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<sup>33</sup> Huber and Stephens, “The Political Economy of Pension Reform,” 19.

The analysis in the previous section suggests that IA has a whole new different agenda than welfare policies, which were designed to provide welfare and protection of external contingencies based on collective cooperation and responsibility. As I mentioned earlier, IA was deemed as a new program that would further the existence of pensions (for a privileged few, as I already argued), and the “promotion of capital markets, investments and economic growth.”<sup>34</sup> Moreover, it is important to note that several International Financial Institutions, such as the World Bank, the International Monetary Fund, and the Inter-American Bank for Development, along with neo-liberal advocates in the different countries this program has been implemented, have supported the implementation of such a program. Even though, the financial agenda of IA is relevant, there are other considerations that overlap into the social arena, such as the undeniable (dis)regard of the collective by IA.

With the cancellation of collective cooperation by IA, one can assume that the new program is based on the individual. Furthermore, IA eliminates collective responsibility, transferring the sole responsibility of pensions to the individual. The Rawlsian approach suggests that the elderly be considered by society as least advantaged group. Since the collective is no longer relevant in IA, then who is to award moral relevancy to the elderly? The answer to this question can be found in the foundations of IA and in Nozickian libertarianism. The individual is responsible for recognizing herself as least advantaged when she reaches old age, therefore she will have the sole responsibility of providing for herself.

It might be quite hard to imagine sole individuals providing for their health care in old age, especially if during their productive years their ability to save was not great. Nevertheless, one is forced to imagine this scenario under the new system. The structure of family, and the care it used to provide in passed decades, cannot be compared to current reality. As Alan Walker argues, several developments during the twentieth century such as the

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<sup>34</sup> Huber and Stephens, “The Political Economy of Pension Reform,” 5.

rise of capitalism, feminism and the need of women to enter the labor market, have completely reformed the scene of family care.<sup>35</sup> Even though it is not a general rule, the possibilities of the elderly to be taken care of by their families is actually decreasing. I am not, of course, arguing against the liberalization of women, or the introduction of women to the labor force; or that I believe these events to be negative. On the contrary, my basic argument at this point is that pension programs can be an important aid, for women and men alike, to overcome the limitations of old age, and the scarcity of care. Nevertheless, the new system, considered as an “every man for himself” system, that turns the opportunity of retirement to a “privilege of a few,” does not really provide for this possibility.

While this scenario is limited to the elderly, it is important to remember the undeniable fact that underlies the argument of Daniels, “we age.”<sup>36</sup> These circumstances will eventually apply to every individual that does not die an untimely death. In this sense, the effects of an economic policy such as the privatization of pensions are not restricted to a sole age group, they have an impact on society as a whole. To limit unfortunate economic circumstances that might derive of the natural decrease of natural endowments in old age, individuals will have to strive to save as much as they can during their productive years, even though they might not be able to. The fear of falling into a disadvantaged position will drive, or provide an incentive for, individuals to be permanently employed. Therefore, transforming the Welfare State into the Enabling State, where the drive is individual responsibility, a market-driven state, and a considerable reduction of benefits,<sup>37</sup> all of which can be identified as primary elements of Nozickean libertarianism.

Even though there is an increasing amount of support for the Enabling State, as Neil Gilbert argues, there are detrimental social effects based on the elimination of collective

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<sup>35</sup> Alan Walker, *The New Generational Contract* (London: University College London: 1996), 1.

<sup>36</sup> Daniels, *Am I My Parents' Keeper?* 43.

<sup>37</sup> Gilbert, *Transformation of the Welfare State*, 4.

responsibility.<sup>38</sup> One of the most important impacts Gilbert finds is that the cancellation of collective responsibility, by extension, eliminates also public purpose, public service, social protection and security; by substituting these for competition, weighting costs and benefits, desire for the maximization of gain and individual choice.<sup>39</sup>

This increased promotion of individualism finds its origins in Nozick's theory. His main objective is to promote individuality, however the means to achieve it deny the possibility of ever reaching the objective altogether. In chapter one I argued that Nozickean libertarianism is essentially flawed because he does not recognize that to promote individuality requires self-determination. Self-determination cannot be achieved by some individuals without a certain amount of collective aid, and therefore the Nozickean recognition of individuality is not universal, but selective. On the other hand, Rawlsian principles of social justice do not deny the importance of individualism. His theory of justice is based on the recognition of individuality to further Kant's imperative to treat each individual not merely as means, but as ends in themselves. As the first chapter stressed, the form in which Rawls recognizes individuality is through an acknowledgment of the purposes, plans of life or conceptions of the good of each and every individual, awarding them equal worth.<sup>40</sup> Rawls considers that to achieve this individualistic objective, a fair distribution of society's resources is necessary, which is realizable through the second principle of justice.<sup>41</sup> Rawlsian principles also allow talented individuals to succeed, yet the condition is that the least advantaged are also benefited, therefore recognizing the individuality of the least advantaged. In this sense, Rawls is not limiting the most advantaged to succeed, he is only allowing the least advantaged to succeed as well. Hence it is possible to acknowledge that

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<sup>38</sup> Gilbert, *Transformation of the Welfare State*, 185.

<sup>39</sup> Gilbert, *Transformation of the Welfare State*, 189.

<sup>40</sup> T.M. Scanlon, "Rawls' Theory of Justice," in *Reading Rawls Critical Studies on Rawls': A Theory of Justice*, ed. Norman Daniels (Stanford, California: Stanford University Press, 1989), 170-171.

<sup>41</sup> Will Kymlicka, *Introduction to Political Philosophy*, 108.

Rawls does further individualism. Nevertheless, he founds the promotion of individualism in strong bonds of social cooperation, that allow everyone to succeed as much as possible and, particularly, does not threaten least advantaged individuals.

Quite clearly IA does not follow Rawlsian principles, it promotes selective and antagonist individualism, where individuals that fear a disadvantaged position will base their decisions on the maximization of gain, without consideration of social cooperation to aid the least advantaged. Breaking the bonds of social cooperation does not allow individuals to see that in order to maximize their gain, and to be free to enhance their individuality, there is an inherent need of social cooperation. Their personal interests take such a priority that they are unable to see relation between the possibility of individuality and the rest of society, which characterizes radical individualism.<sup>42</sup> This relationship can be found in the precepts of Rawlsian theory, where the recognition of individuality is possible due to social cooperation, that not only furthers some conceptions of the good, but all. Freedom to pursue life-plans is awarded by a social cooperation willing to redistribute resources, and tolerate differences. Nevertheless, where social cooperation is no longer the foundation of society, radical individualism takes its place. Individuals, that fall into this kind of individualism, “define their own success in terms of their individual efforts through competition in the marketplace independent of politics and government or cooperation with their fellow citizens.”<sup>43</sup> Antagonism within individuals might not arise, as long as resources do not scarce. Nevertheless, when there is a scarcity of resources, radical individualism might have an antagonistic effect within members of society, that face an an unprotected, risk-unfree future.

Under a scarcity of resources, IA, characterized as an “every man for himself” system, will promote a battle of resources between “an every man for himself” versus every other

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<sup>42</sup> William Hudson, *American Democracy in Peril* (Chatham, NJ: Chatham House, 1998), 81.

<sup>43</sup> Hudson, *American Democracy in Peril*, 84.

“every man for himself.” Or as Thomas Hobbes uniquely put it, “*bellum omnium contra omnes, homo homini lupus.*”<sup>44</sup> In this sense, it is possible to argue that IA, inadvertently, promotes individualism that tends to go from moderate to radical.<sup>45</sup> Even though the consequences of radical individualism within social policies have not reached this unacceptable low, and remain contained within the frames of pension, birth cohorts and age groups; it is a step that is not going towards ‘the integration of society,’ it is going in the opposite direction, promoting individualism, severing links of cooperation and obligation.

The neglect of social justice as a critical foundation of social policy has long-term effects, not only on the values on which a society is built, but also on the welfare of citizens; in this case, the welfare of the elderly. Several studies have shown that IA does not deliver as promised since it does not solve the problem of poverty in old age, and also increases the levels of inequality, as will be shown in the case of Mexico.

## CONCLUSIONS

In this chapter I have portrayed the main problems that can be found in the privatization of state-run PAYG schemes, which generally can be summed up as issues of social justice. Following Rawls’ Difference Principle and the moral relevancy of old age, it has become evident that the Individual Accounts system fails to promote such a principle on various levels. Not only does IA eliminate social cooperation, it disregards completely the advantaged/disadvantaged identification, so much needed for social justice considerations and for the purposes of self-determination and autonomy. Furthermore, IA does not focus on the moral relevancy of the elderly. On this specific point, one stops to wonder that if IA does not award importance to the moral relevancy of old age, then is it actually a program designed for the welfare of the elderly, or is it that its objectives do not include welfare?

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<sup>44</sup> Thomas Hobbes, *Leviathan* ([cited April 23, 2009] Oregon State University): available at <http://oregonstate.edu/instruct/phl302/texts/hobbes/leviathan-contents.html>

<sup>45</sup> Hudson, *American Democracy in Peril*, 80-81.

PAYG was a part of a safety net, designed to protect individuals from exogenous contingencies, as well as natural ones.<sup>46</sup> IA shoots holes through that safety net, workers that cannot save enough will be doomed to live under a minimum pension that might not be much at all. IA also depend too much of financial markets, which cannot guarantee stability or continuous interest rates.

The privatized scheme that was sold as a solution to PAYG problems was actually not that, since it did not solve justice problems between birth cohorts, it only closed its eyes to them, and in the meantime it tends to radicalize inequality between social classes. It is more likely that IA is a road towards the compliance of liberalization commitments, and towards enhancing national capital markets.<sup>47</sup> If this is the case, is it possible that IA is only a transition that will eventually lead to enhance social policy as such? It is prudent to ask this question of countries that are thinking of this option, since there is yet another social justice issue that should be introduced, justice between generations.

Rawls considered that it is the duty of present generations to sustain a certain level of education, knowledge, environmental health, and values for generations to come.<sup>48</sup> If IA is here to stay, then it is possible to argue that our legacy towards future generations will be the foundations of radical individualism and the destruction of social cohesion within social policy. As I stated in this chapter, privatization of pensions without the necessary considerations of justice, is a *small* step towards this road to radical individualism as a result of Nozickean libertarianism, but still a step in the wrong direction.

Considering that IA is here to stay, a door has been opened for other reforms within social policy, based only on productivity and competitiveness of national markets. It will not

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<sup>46</sup> Huber and Stephens, "The Political Economy of Pension Reform," 19.

<sup>47</sup> Huber and Stephens, "The Political Economy of Pension Reform," 20.

<sup>48</sup> Rawls, *A Theory of Justice* (Cambridge, Massachusetts: The Belknap Press of Harvard University Press, 1971), 284-285.

be the case anymore that social policy searches for social development, but for national economic competitiveness.<sup>49</sup> It will be, therefore, the responsibility of future generations to reform these policies, or to bear the consequences of them. If future generations do not take it upon themselves to change the path of radical individualism, then it is possible that Johan Galtung is correct when he states that,

[i]n short: at the end of the road winding through history and into the future we see a social formation (“society” may no longer be the term) basically atomized into individuals, thinly and weakly related, each acting out of egocentric cost-benefit calculations. We are close to this state of atomie, but there is still some interaction left. We are also close to anomie, where the only binding normative culture left would be individualized cost-benefit analysis. Anarchy would be another term, *bellum omnium contra omnes*, *homo homini lupus*. The social fabric (*le tissu, el tejido*), the social body, *lo social*, falls apart.<sup>50</sup>

I do not mean to imply, with this negative scenario, that the financial problems of PAYG are not important. On the contrary, it is possible that reform is urgent to sustain pension programs. However, it is of critical importance that the decision of reform be made, not only on economic or financial reasons, but on social justice considerations as well. As I will in the next chapter, the case of Mexico helps shed some light on the unfortunate consequences of pension privatization.

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<sup>49</sup> Gilbert, *Transformation of the Welfare State*, 10.

<sup>50</sup> Johan Galtung, “On the Social Costs of Modernization: Social Disintegration, Atomie/Anomie and Social Development,” *United Nations Research Institute for Social Development* (March 1, 1995 [cited April 21, 2009]): available at [http://www.unrisd.org/80256B3C005BCCF9/httpNetITFramePDF?ReadForm&parentunid=03ECD7C3823352BD80256B67005B6779&parentdoctype=paper&netitpath=80256B3C005BCCF9/\(httpAuxPages\)/03ECD7C3823352BD80256B67005B6779/\\$file/dp61.pdf](http://www.unrisd.org/80256B3C005BCCF9/httpNetITFramePDF?ReadForm&parentunid=03ECD7C3823352BD80256B67005B6779&parentdoctype=paper&netitpath=80256B3C005BCCF9/(httpAuxPages)/03ECD7C3823352BD80256B67005B6779/$file/dp61.pdf)